Thompson Taraz

Ten things you need to know about:

Seed Enterprise Investment Scheme (SEIS)

SEIS

“Thompson Taraz is a leader in the effective management of alternative investment funds.”

The Seed Enterprise Investment Scheme (SEIS) is a government initiative designed to attract investment into start-up companies. SEIS came into force following the Finance Act 2012 and applies to investments made after 5 April 2012. This guide takes into account changes to the scheme included in the Finance Bill 2016.

"The Seed Enterprise Investment Scheme (SEIS) is designed to help small, early-stage companies to raise equity finance by offering a range of tax reliefs to individual investors who purchase new shares in those companies. It complements the existing Enterprise Investment Scheme (EIS) which will continue to offer tax reliefs to investors in higher-risk small companies. SEIS is intended to recognise the particular difficulties which very early stage companies face in attracting investment, by offering tax relief at a higher rate than that offered by the existing EIS."

– HM Revenue & Customs

1 SEIS advantages

There are a number of specific advantages offered to investors by the SEIS. These include:

- 50% cash tax relief, irrespective of the investor's rate of income tax (with a maximum relief of £50,000 per year)
- Capital gains reinvestment relief
- Tax free capital gain on exit provided that the SEIS investment is held for more than three years
- 100% exemption from inheritance tax after two years
- Carry back relief - unused relief in one tax year can be carried back to the preceding tax year if there is unused relief available for that year

2

Income tax relief

The amount of relief is 50% of the amount invested up to £100,000, hence the maximum relief is £50,000. The relief is given by way of a reduction in the investor's tax liability irrespective of their marginal rate of tax.

As an example, if Henry invests £10,000 in 2017-18, the SEIS relief is £5,000 (£10,000@50%). His tax liability (before SEIS relief) is £18,000 which will be reduced to £13,000 as a result of his investment.

3

Capital gains tax reinvestment relief

This provides partial exemption (50%) for capital gains up to £100,000 on assets sold in 2017-18 by reinvesting an amount equivalent to the gain.

As an example, Rachel sold assets in 2016-17 and 2017-18 for £50,000 each and realised gains of £10,000 in each (after the annual exemption). She reinvests £20,000 in 2017-18 and elects to carry back £10,000 to 2016-17 £5,000 of the gain in each year is exempt.

4 Tax relief at 64%

The combined effect of income tax and CGT reinvestment relief means that it is possible to get tax relief at 64% in 2016-17 onwards. Continuing the example above, and assuming Rachel's CGT rate is 28%, her £20,000 reinvestment results in the following:

- her income tax liability in 2016-17 is reduced by £5,000 (£10,000@50%)
  and
- her £10,000 chargeable gain in 2016-17 is partially exempt, reducing her CGT liability by £1,400 (£10,000@28%@50%).

The combined income tax and CGT reliefs in 2016-17 total £6,400. The same saving applies for 2017-18.

5 SEIS Funds and EIS hybrids

SEIS funds offer investors an opportunity to participate in the potentially attractive returns available through investing in a diversified portfolio of start-up companies.

A hybrid fund can involve companies preparing an SEIS - backed funding round followed shortly afterwards by further investments using the more established Enterprise Investment Scheme (EIS).

Hybrid funds may offer investors better tax efficiency and more flexibility to switch money into either EIS or SEIS wrappers from the same fund.

SEIS

6 Deal with professional advisers who know about SEIS

A knowledgeable and experienced professional should be able to advise on:

- Eligibility
- Reliefs
- Submitting claims for relief and advance assurance
- Dealing with SEIS certificates
- Dealing with compliance aspects
- Acting for SEIS and EIS funds
- Safe custody and holding client money
- Registrar activities
- Investor communications

7 Qualifying business conditions

To be eligible for the SEIS, the business must have:

- Fewer than 25 employees
- Less than £200,000 in gross assets

Furthermore, the business must be:

- Unquoted on any stock exchange
- Undertaking a new business
- Less than two years old

It must not be:

- Engaged in any excluded activities such as property, finance or leasing-based businesses.

The business must be bona fide, as HMRC will withdraw relief in cases where it appears that a business has been structured purely or mainly to take advantage of the SEIS tax relief.

Furthermore, the investment raised via SEIS can not exceed £150,000 in total.

8 Due diligence

Angel investors should work with suitably qualified professionals to help them carry out focused legal, commercial and financial due diligence on the target business, proportionate to the value of the deal. Investors should check that a company has been properly incorporated and owns all business assets, and that relevant contracts are in place and effective.

Due diligence will vary according to the company but might include the precise ownership details and intricacies of the company's intellectual property, as well as the impact of existing financing and security arrangements, and whether or not any disputes exist or are threatened.

9 Who can invest?

There is no restriction on who can invest in a company's qualifying SEIS shares. However, to qualify for SEIS relief an investor must not hold more than 30% of the ordinary share capital or voting rights, although there are no restrictions on loan capital. Whilst employees cannot invest in the SEIS qualifying shares of their own employing company and qualify for the relief, directors of the company can.

10 Risky business

Start-up businesses have a very high failure rate, with as many as one in three failing in their first three years. In addition, small businesses have been the main casualties of recessions; not only because of falling consumer spending but also due to the difficult lending conditions. That makes investing in start-up companies a risky business; hence the generous tax relief on offer.

If the business should fail and the investment yields a capital loss, this loss can be deducted from net income for income tax purposes in the current and precceding year.

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eisa enterprise investment scheme association

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