

Over the past few years this relief has become more generous, but we would recommend obtaining advice before setting up a company, or investing in such a company, as there are a number of hurdles in the legislation that need to be borne in mind.

Income Tax relief

Income Tax relief can be obtained based on the amount subscribed for shares in an EIS company. In order to obtain relief, both the investor and the company must be eligible for relief.

The relief is given as a tax reducer (deducted from the Income Tax liability) at 30%.

The relief is available on a maximum investment of £1 million per year (amounting to £300,000 of Income Tax relief). This limit is increased to £2 million for investments in knowledge intensive companies (from 6 April 2019).

The relief can be obtained in the tax year of investment or carried back in part or full to the previous tax year. The relief cannot reduce the tax liability in either year below nil.

The relief can be withdrawn in full if the eligibility conditions are breached (such as a sale of the shares) within three years. The relief can also be withdrawn or reduced if any value for the shares is received by the investor.

CGT Deferral Relief

Capital Gains Tax (CGT) liabilities arising on the disposal of other assets can be deferred when investing in EIS shares. The deferred gain will however come back into charge at a later date, for example on the disposal of the EIS shares. When the deferred gain comes back into charge, it's subject to CGT at the relevant rate at that time.

CGT on exit

If you sell the EIS shares within three years, and make a gain on the disposal, it will be chargeable to CGT.

If Income Tax relief is given on the shares, and the EIS shares are held for more than three years from the date of issue, then any gain arising on disposal of the EIS investment itself will be exempt from CGT.

If, however, a loss is made on disposal of the investment, this is an allowable loss. Note though, that the loss is first restricted by the EIS Income Tax relief received. An election can be made for the capital loss to be set against other income of the year of the disposal, or income of the previous year, rather than being set off against capital gains as would normally be the case.

Eligibility for Income Tax relief

Investor

For an individual to be eligible for Income Tax relief, they must not be connected with the company. This is defined as more than a 30% holding in a company and includes associates' shareholdings. There can also be restrictions on being a director of the company.

Company

The company must be an unquoted company carrying out a qualifying trade. There are some trades that are not eligible for relief.

The company can issue EIS shares up to the value of £5 million in any 12-month period, and a maximum of £12 million in the company's lifetime, from any tax efficient scheme. This is increased for knowledge intensive companies (being £10 million and £20 million respectively).

Money invested will not be eligible for EIS relief unless it is used for a qualifying business activity within two years following the issue of the shares, or two years after the trade starts, if later.

Conclusion

EIS can provide very valuable tax relief to investors, but there are a number of conditions to ensure that investors and the company are eligible for relief. The summary above provides examples of this but is not exhaustive.

Find out more

For further information, advice and guidance please contact one of our specialists:

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This is a general illustrative guide only and individual professional advice should be obtained on specific issues. Information is believed correct at time of publication but may alter.

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