Enterprise Investment Scheme: Introduction to National Statistics

Background

1. Introduced in 1994, the Enterprise Investment Scheme (EIS) is one of the three tax-based venture capital schemes. It is designed to help smaller higher-risk trading companies to raise finance by offering a range of tax reliefs to investors who purchase new full-risk ordinary shares in those companies.

2. To qualify for EIS during the latest year of published statistics, 2009-10, a company had to meet the following requirements:

   - The company must be unquoted
   - It must not be controlled by another company
   - subsidiaries must be qualifying subsidiaries (defined as the parent company owning over 50% of the ordinary share capital)
   - It must be a small company (defined as gross assets not exceeding £7 million before the share issue and £8 million after)
   - It must carry out or be preparing to carry out a qualifying trade (or be the parent of an at least 90% subsidiary that is doing so)
   - The trade must be carried out wholly or mainly in the UK
   - 80% of money raised must be spent within 12 months and the remainder within another 12 months. The trade must be conducted on a commercial basis with a view to the realisation of profits. Most trades qualify, but some do not – termed 'excluded activities'.[1]
   - A company can carry on some excluded activities, but these must not be 'substantial' part of the company's trade (defined as greater than 20%).
   - Relief is withdrawn from investors if the company fails to meet any of the above requirements throughout the three years following the share issue.

Relief to Shareholders

3. Latest published statistics are for 2009-10, when tax relief comprised:

   - **Income tax relief:** Individuals can claim relief at 20% on investments of up to £500,000 per tax year, provided they are not connected with the company and the shares must be held for at least three years.

[1] In 2009-10, the excluded trades were dealing in land, commodities, or financial instruments; dealing in goods, other than an ordinary trade of retail or wholesale distribution; banking, insurance, money-lending, debt-factoring, hire-purchase financing or any other financial activities; leasing or letting assets (except certain ship-chartering activities); receiving royalties or licence fees (except if arising from the exploitation of an intangible asset the company has created); legal or accountancy services; property development; farming or market gardening; forestry or timber production; hotels or comparable establishments; nursing homes or residential care homes; and providing services to another person whose trade substantially consists of excluded activities and that person also controls the company providing the services.

- **Capital gains tax exemption:** A gain arising from the disposal of shares for which EIS income tax relief was obtained and retained is exempt from capital gains tax.

- **Loss relief:** If shares for which EIS income tax relief was obtained are disposed of at a loss, the loss, less any income tax relief given, can be set against income instead of against capital gains.

- **Capital gains tax deferral:** The payment of tax on a capital gain can be deferred where the gain is invested in shares of an EIS qualifying company. The gain can be from the disposal of any asset, but must be invested one year before or three years after it arose. The gain can be any amount and it does not matter whether the investor is connected with the company or not. Unconnected investors may claim both income tax and capital gains deferral relief. There is no minimum period for which the shares must be held; the deferred capital gain is brought back into charge whenever the shares are disposed of, or are deemed to have been disposed of.

Key Policy Changes

4. There have been some policy changes to the scheme since its inception that could be reflected in the statistics. Some of the key changes are:

   - **1997-98:** From 17 March 1998, farming, market gardening, property management, hotels, guesthouses, care and nursing homes became 'excluded activities'.
   - **1998-99:** From 6 April 1998, capital gains tax deferral relief was extended to include shares that do not obtain income tax relief. Previously, deferral relief was only available such shares. In addition, a company gross assets limit of £15 million before investment and £16 million after was introduced. Prior to this, there was no limit on company size, but a company could raise only up to £1 million per tax year through EIS (though certain qualifying shipping activities could raise up to £5 million). Also, the maximum amount of investment on which income tax relief can be obtained was increased from £100,000 to £150,000.
   - **1998-99:** Capital gains tax exemption introduced from 1 January 1999.
   - **2000-01:** Change in the definition of research & development. The period for which shares must be held to retain income tax relief was reduced from five years to three.
   - **2001-02:** The requirement that all money be employed in qualifying activities within 12 months was changed to 80 per cent (with the remaining 20 per cent to be employed within the next 12 months).
   - **2004-05:** Maximum amount of investment on which income tax relief can be obtained increased from £150,000 to £200,000.
   - **2006-07:** Gross assets limit reduced to £7 million before investment and £8 million after investment. Maximum amount of investment on which income tax relief can be obtained increased from £200,000 to £400,000.
   - **2007-08:** From 19 July 2007, companies must have raised no more than £2 million under any or all of the tax-based venture capital schemes (Venture

Capital Trusts, Enterprise Investment Scheme and Corporate Venturing Scheme).

- **2008-09:** Maximum amount of investment on which income tax relief can be obtained increased from £400,000 to £500,000.

5. Further details on EIS scheme and policy changes can be found at: http://www.hmrc.gov.uk/eis/guidance.pdf

Description of the Statistical Tables

6. Tables 8.1 to 8.4 take information on the total levels of fundraising and the companies from the form EIS1 that companies are required to submit within 3 years of issuing shares.[2] Table 8.5 uses information on the number of investors and the amounts invested reported on investors' Self Assessment tax returns, specifically, in 2008-09, where an amount had been entered in Tax Return: Additional Information: Page Ai 2 (Other tax reliefs box 2), and equivalent boxes in the earlier years, meaning it presents only investments that claimed income tax relief.[3]

7. **Table 8.1** shows the number of companies raising funds and the number of subscriptions and amounts raised through EIS for 1993-94 to 2009-10^{P}.

8. **Table 8.2** shows the number of companies and amount of funds raised, by industry through EIS for 2007-08 to 2009-10^{P}.

9. **Table 8.3** shows the number of companies and amount of funds raised, by size of funds through EIS for 2007-08 to 2009-10^{P}.

10. **Table 8.4** shows amount of funds raised, by region through EIS for 2007-08 to 2009-10^{P}.

11. **Table 8.5** shows for income tax relief; in percentages, the distribution of investors and amount of investment claimed for years 2007-08 to 2009-10.

Enquiries

12. Statistical enquiries should be addressed to: Elizabeth Ojomo, VCT Statistics, KAI Direct Business Taxes, HM Revenue & Customs, Room 2/43,100 Parliament Street, London, SW1A 2BQ.Tel: 020 7147 3102, mailto:elizabeth.ojomo@hmrc.gsi.gov.uk

    For more general enquiries please refer to the HMRC website: **www.hmrc.gov.uk**

13. For all detailed enquiries relating to investing in Enterprise Investment Scheme, please contact Small Company Enterprise Centre (SCEC), 1st Floor, Ferrers House, Castle Meadow Road, Nottingham, NG2 1BB. Telephone 0115 974 1250.

[2] http://www.hmrc.gov.uk/forms/eis1.pdf
[3] http://www.hmrc.gov.uk/sa/forms/content.htm