

Enterprise Investment Scheme

Nigel Burke

November 2014

Enterprise Investment Scheme

- What is EIS?
- What EIS offers the investor
- Downside mitigation
- Upside efficiency
- Conditions for the investor
- Conditions on EIS shares

Overview (Cont'd)

- Restrictions on the EIS company
- Qualifying trade
- Regulatory requirements
- Interaction with other sources of finance
- Basic structure

What is EIS?

- The Enterprise Investment Scheme
- Government scheme to encourage investors
- Operating since 1994
- Well Worn Path
- Not to be confused with other investment schemes which may or may not promise a tax advantage
- Pre approval mechanism- “Advanced Assurance”

What EIS offers the Investor

- Income Tax : 30% relief up to £1,000,000 invested in shares
- Capital Gains Tax : gains on disposal of shares exempt
- Capital Gains Tax : gains on the disposal of any asset can be deferred for CGT by “freezing” the Gain and attaching it to their EIS shares – not subject to the £1,000,000 limit
- Inheritance Tax : shares are potentially exempt from IHT if still held at death
- Loss Relief : if shareholder incurs a Capital Loss, that Loss (less the I.T Relief) can potentially be offset against income.

Downside Mitigation

Can reduce a 45% Taxpayer's exposure to 38.5% in the event of shares becoming valueless

	40% Taxpayer £	45% Taxpayer £
Initial Investment in Ordinary Shares	(100,000)	(100,000)
Income Tax Relief at 30%	30,000	30,000
Net cost of Initial Investment	<u>(70,000)</u>	<u>(70,000)</u>
 If Shares then become Valueless		
Income tax Relief for Capital Loss	28,000	31,500
Loss to Investor after Tax Relief	<u>(42,000)</u>	<u>(38,500)</u>
	42.00%	38.50%

Downside Mitigation

Can reduce a 45% Taxpayer's exposure to 28.6% on a UK Tax Credit Qualifying Video Game in the event of shares becoming valueless.

	40% Taxpayer £	45% Taxpayer £
Initial Investment in Ordinary Shares	(100,000)	(100,000)
Income Tax Relief at 30%	30,000	30,000
Net cost of Initial Investment	<u>(70,000)</u>	<u>(70,000)</u>
<u>UK Tax Credit</u>	18,000	18,000
If Shares then become Valueless		
Income tax Relief for Capital Loss	20,800	23,400
Loss to Investor after Tax Relief	<u>(31,200)</u>	<u>(28,600)</u>
	31.20%	28.60%

Upside Efficiency

	Non-EIS	EIS
Investment	100,000	100,000
EIS I.T. Relief	-	(30,000)
Net cost to investor	100,000	70,000
Exit	200,000	200,000
Less CGT	(28,000)	-
Gain net of tax	72,000	130,000

Conditions for the Investor

- The Investor must not be “connected” with the EIS Company:
 - Employees or Directors (paid)
 - Capital Connection via shares or voting power
 - Reciprocal Arrangements : mirroring acquisitions
- No Linked Loans : loans made on special terms due to subscription for shares
- No Tax Avoidance involved : EIS must not be used as part of a broad scheme. Stand-alone arrangements are fine.

Conditions for the EIS Shares

- The shares must be new Ordinary Shares: no preferential rights (whether express or implied)
- No returns of capital to investors for 3 years
- There must be no pre-arranged exits for shareholders (though you can express a possible exit strategy)
- The shares must not be part of a tax “scheme”

Restrictions on the EIS Company

- The company must exist (wholly or partly) for the purpose of a Qualifying Trade for approx. 3 years
- The company must be unquoted (AIM is OK) and not be controlled by another company
- The company can raise a maximum of £5m from EIS in any 12month period
- Gross Assets must not exceed £15m before and £16m after the issue

Restrictions on the Company Cont'd

- The company must have no more than 249 full-time employees
- If the trade is to be carried on by a subsidiary, it must be at least a 90% subsidiary
- Excluded Activities – most are irrelevant for video games, film, TV and music, but take care if receiving royalties or license fees
- Seek HMRC Advance Assurance for confidence that Investors will obtain EIS Relief as intended

Qualifying Trade

- List of excluded activities is shorter than you would assume but includes:
- Lending or provision of finance
- Receiving licence or royalty revenue, unless as outlined below
- Included activities, including but not limited to:
- Video games, TV, film and animation development and production
- Music recording
- Ancillary trades in creative sectors
- If receiving license or royalty revenue, it must be from IP that the company has created

Regulatory Requirements

- Complex regulatory issues for public offerings / sophisticated investor offerings / friends & family offerings
- Essential that professional advice is sought so that promoters are protected from significant exposure.

Interaction with other sources of finance

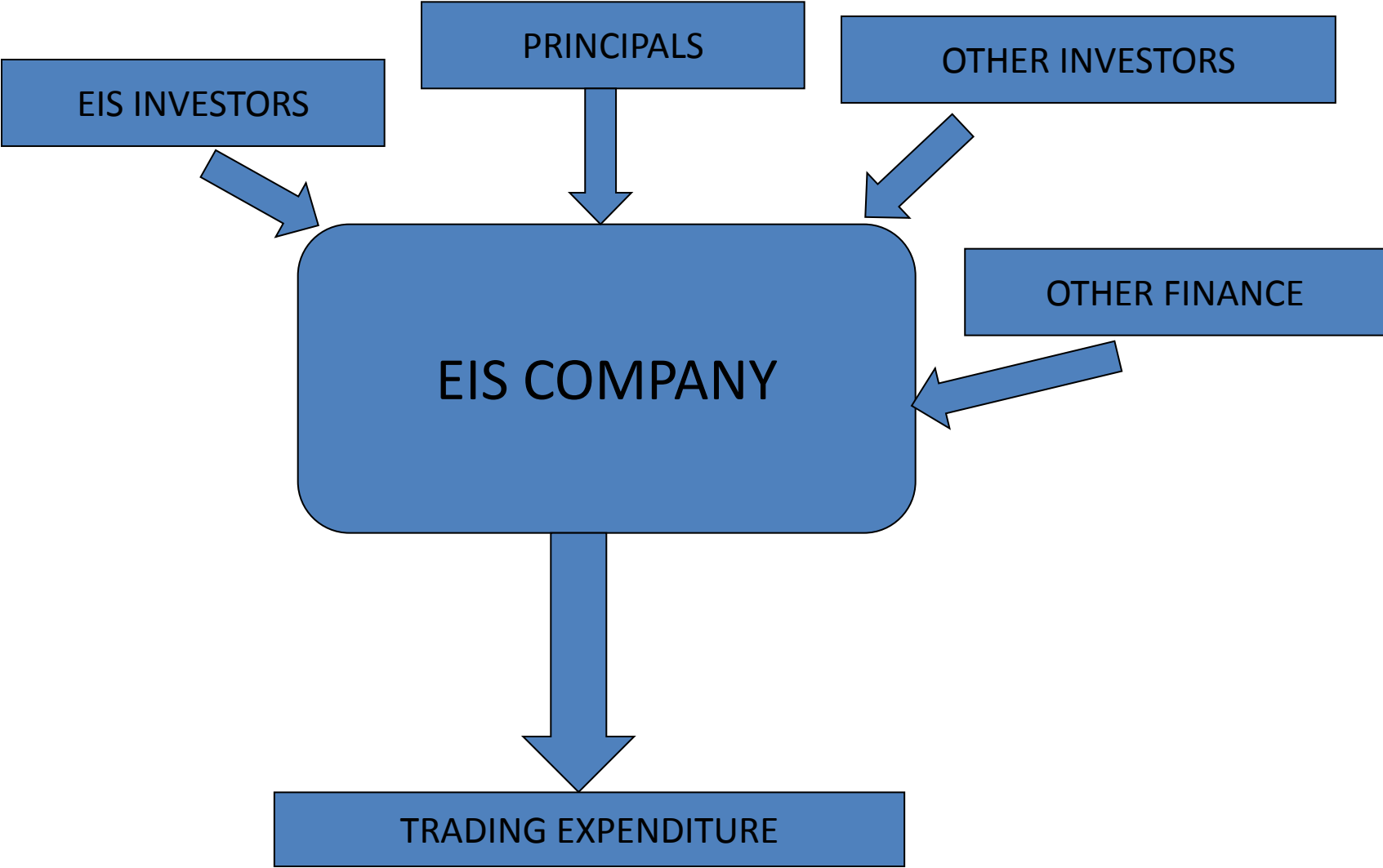
EIS is flexible – subject to the Gross Asset test, can be used in conjunction with:

- Bank and other borrowing
- Most development and production

incentives such as the UK's video games tax credit

- Commissioning deals and pre-sales
- Equity Investment

Basic Structure



Enterprise Investment Scheme- End

Nigel Burke

November 2014

Seed Enterprise Investment Scheme

Nigel Burke

November 2014

Overview

- Broadly operates in the same way as EIS
- For smaller scale fundraising
- Introduced 2012
- Pre approval Mechanism – “Advanced Assurance”

What SEIS offers the Investor

- Income Tax : 50% relief up to £100,000 invested in shares
- Capital Gains Tax : gains on disposal of shares exempt
- Capital Gains Tax : gains on the disposal of any asset, if invested in SEIS shares, can be extinguished by 50% of gain if gain in 2013/14 or 2014/15.
- Loss Relief : if shareholder incurs a Capital Loss, that Loss (less the I.T Relief) can potentially be offset against income.

Downside Mitigation

Can reduce a 45% Taxpayer's exposure to 27.5% in the event of shares becoming valueless.

	40% Taxpayer £	45% Taxpayer £
Initial Investment in Ordinary Shares	(100,000)	(100,000)
Income Tax Relief at 50%	50,000	50,000
Net cost of Initial Investment	<u>(50,000)</u>	<u>(50,000)</u>
If Shares then become Valueless		
Income tax Relief for Capital Loss	20,000	22,500
Loss to Investor after Tax Relief	<u>(30,000)</u>	<u>(27,500)</u>
	30.00%	27.50%

Downside Mitigation

Can reduce a 45% Taxpayer's exposure to 13.5% if 2013/14 or 2014/15 Capital Gains are invested.

	2013/14 or 2014/15 Gain £100,000 45% Taxpayer £
Initial Investment in Ordinary Shares	(100,000)
Income Tax Relief at 50%	50,000
Net cost of Initial Investment	<u>(50,000)</u>
Capital Gains Tax Extinguished	14,000
If Shares then become Valueless	
Income tax Relief for Capital Loss	22,500
Loss to Investor after Tax Relief	<u>(13,500)</u>
	<u><u>13.50%</u></u>

Conditions for the Investor

- Less than 30% restriction remains
- Other conditions for connection with company less restrictive than EIS
- Maximum £100,000 investment in SEIS per annum
- No returns of capital for 3 years etc.

Restrictions on the EIS Company

- The company can raise a maximum of £150,000 from SEIS in its life.
- Gross Assets must not exceed £200,000 before SEIS.
- Company trading for less than 2 years.
- Company can do an EIS once 70% of SEIS funds spent.

Seed Enterprise Investment Scheme- End

Nigel Burke

November 2014