TrendScout

Your comprehensive guide to

The Enterprise Investment Scheme (EIS) and Seed Enterprise Investment Scheme (SEIS)

2023 - 2024 TAX YEAR

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Welcome to Trendscout!

A **GUIDE** TO THE ENTERPRISE INVESTMENT SCHEME (EIS) AND SEED ENTERPRISE INVESTMENT SCHEME (SEIS)

Explore possibilities

Founded by successful entrepreneur **Ilayda Taze**, Trendscout has brought together an experienced team of equally successful founders and investment professionals. Their combined knowledge and experience are hugely valuable assets when supporting our cohort of startups.

Our EIS portfolios

With Trendscout, investors can become shareholders in over 30 early-stage companies with huge growth possibilities. Unlike some EIS portfolios, which can take up to a year to deploy capital, our investor's funds are deployed immediately.

Sectors

- Artificial Intelligence (AI)
- Delivery Services
- Ecommerce
- Educational Technology (Edtech)
- Financial Technology (Fintech)
- Food And Beverage
- Fraud Detection
- Healthcare Tech
- Online Retail
- Pet Care
- Technology
- Wellbeing

Stage

1. Pre Seed - Solving the problem. Running a successful business is all about producing something that solves a problem.
2. Seed - Development. This is where it starts getting serious.
3. Startup - Entering the market.
4. Growth - Revenue.

Investment Size	Minimum Investment
£150,000 to £2million	£10,000

British Ventures EIS

A test of British's portfolio of companies with big growth ambitions run by exceptional founders.

Univy | GoKo Travels | Igniv | Porter | ElementaryB | LongLive

Sustainable Growth EIS

Portfolio of companies using innovation to address the world's sustainability challenges.

Reknowledge | Unify | Greenbay | Spacebands | SkyFarer | Bullet & Bone

You can find more about us at https://www.trendscoutuk.com/

Glossary

Disclaimer

Investing in unlisted companies, particularly startups and early-stage businesses can be rewarding. However, it also involves a number of risks. This warning is to ensure that you understand the risks involved, but it is not exhaustive and cannot highlight all the risks involved. Investors should conduct a level of their own due diligence and seek third party advice from an appropriately qualified independent financial adviser prior to making any investment in light of their personal circumstances. The information contained herein isn't intended as investment advice or an offer to buy or sell any investment. It's intended as a guide to enable investors to conduct additional research into the potential risks and rewards of investing in SEIS and EIS businesses.

FOREWORD

Over the last 24 years, the Enterprise Investment Scheme (EIS) has helped more than 33,000 businesses raise over £24 billion. EIS's centrality in the equity funding market for SMEs is demonstrated by its resilience in the face of famously volatile governments, which is also a testament to the scheme's importance in helping UK companies grow.

The Chancellor's recent comments that SMEs "are the champions of small enterprises and the entrepreneur", highlight the growing awareness of the EIS industry's core values: SMEs and entrepreneurs are the core of the UK economy.

The EIS fills a gap between needed capital and some of the nation's least developed and most unexplored areas. The good news for investors is that there's an endless supply of high-quality businesses to support. More small businesses than ever before have the desire to scale up and grow quickly.

This guide aims to empower you with the knowledge you'll need to confidently and professionally invest in EIS eligible companies. We hope you find it both helpful and informative. This guide will also provide you with knowledgeable opinions on the relevant issues and challenges you may face while investing in this sector.

Ilayda Taze
Director
Trendscout UK

Please keep in mind that this guide is to provide general information. Professional advice should always be taken.

AN **INTRODUCTION** OF EIS AND SEIS

The Enterprise Investment Scheme (EIS) is a long-running government scheme that aims to encourage investment in smaller businesses by offering valuable tax incentives to those who subscribe to qualifying shares in EIS companies.

The Seed Enterprise Investment Scheme (SEIS) was created in 2011 to complement the EIS. The main difference between the EIS and the SEIS is that the latter is aimed at companies in the early stages of development, whereas the former is aimed at extensive and older businesses (although these are still considered small and young in the UK industry and corporate landscapes).

Both the EIS and SEIS promote early-stage investment in smaller and younger UK businesses that show high growth potential by using investor funds to help finance expansion and development.

The UK government provides investors with various significant tax reliefs in exchange for providing capital. This helps investors mitigate investment risks and increase their potential returns.

In light of the numerous tax “loopholes” being closed by the government, it’s essential to remember that the EIS and SEIS are non-aggressive schemes that, importantly, the government continues to support. Investors benefit both small businesses and the economy by investing in EIS and SEIS.

Although they are technically different schemes, this guide uses EIS to refer to both the EIS and SEIS for simplicity, unless the context indicates otherwise.

*The EIS / SEIS figures for funds raised are estimates based on a National Statistics publication produced by HM Revenue and Customs (HMRC) released on May 27, 2021. The statistics include investments up to the 2019/2020 tax year.

COVID-19

The coronavirus pandemic had a significant impact worldwide, and its effects are particularly evident in the EIS industry. Many investors have shied away from risk due to COVID-19, at least in the short term, lowering the funds available to the EIS. Of course, this has happened in various other investment industries as well.

Fortunately, national governments appear to be in a place where they can handle COVID-19 despite the ever-present variants. The vaccination scheme, combined with increased public awareness, hopefully means we are past the worst of it.

We are now as close to normal as we can hope for, particularly as the myriad restrictions have been lifted. This has led to a more optimistic outlook, which, paired with some exciting EIS opportunities on the market, has rekindled interest in the sector.

EIS companies are generally dynamic and innovative by their nature. In this respect, many EIS have adjusted their business models to deal with the challenging markets we've been experiencing and to take advantage of new opportunities brought about by COVID-19.

Furthermore, the wider industry has taken numerous steps to benefit EIS investors in the long run. Although investing in EIS carries risks and rewards like any other investment, what sets it apart is that EIS investors benefit from considerable tax reliefs, which will be discussed in this guide. These tax reliefs can lower the effective net cost of investing while simultaneously providing potential longer-term benefits.

WHY **THERE** ARE 3 WINNERS WITH EIS & SEIS

Winner 1 - The Investor

By investing in EIS and helping small UK businesses, it's only fair that the investor should benefit.

Investors can benefit in several ways, including:

- Investing in small promising companies can provide large potential returns.
- Unlike many traditional systems, EIS investors benefit from a closer relationship with the company they invest in.
- There are numerous valuable tax reliefs available to investors. These can lower the risk of investing in a small business while increasing total earnings.

Winner 2 - The Company

Small businesses have found it increasingly challenging to obtain traditional financing due to stricter lending standards, less support from banks, and

broader limits on other kinds of finance. This means that raising cash, no matter how good the company, has become more difficult than ever.

The EIS offers British businesses a different way to fund their growth. The funds raised can help with most aspects of development, such as creating new businesses, product launches, and entry into new markets. The EIS has contributed to the success of numerous businesses, both small and well known.

Winner 3 - The Country

The benefits EIS provides to the UK economy are why the government offers tax benefits on investments. Surprisingly, many people are unaware of these advantages.

Among the advantages are:

- Raising Income Tax and National Insurance from EIS company employees.
- EIS companies contribute to the Treasury through Corporation Tax, VAT, and other duties.
- Helping the economy grow.
- Helping create new British businesses and job opportunities.

DIFFERENCE **BETWEEN** EIS & SEIS?

The EIS and SEIS have the same aim: to provide a channel for early-stage investments to become high-growth potentials.

Although EIS and SEIS are similar in several ways, the main difference is the conditions for startups interested in participating in either EIS or SEIS.

SEIS is aimed at startups and very early-stage companies.

On the other hand, EIS can be used for more extensive and older businesses (although these are still considered small and young in the UK industry and corporate landscapes).

SEIS Funding Criteria For Companies

Fewer than 25 employees.

Trading for less than 2 years.

Gross assets valued at no more than £200,000.

No previous investment from a Venture Capital Trust under EIS. Subject to the EIS funding limit of £100,000.

The comparable requirements for EIS

Fewer than 250 or 500 employees for 'Knowledge intensive' companies.

Trading for less than 5 years or less than 10 years for 'Knowledge intensive' companies. Typically, those with high research and development costs or requirements.

Gross assets are valued at no more than £15 million.

The maximum lifetime amount that can be raised under SEIS, EIS, and VCT is £12 million or £20 million for Knowledge intensive' companies.

INVESTOR **TAX BENEFITS** - EIS & SEIS

EIS

30% Initial Income Tax Relief

Effective net cash outlay of 70p in the £1

CGT Freedom

No Capital Gains Tax to pay on any EIS gains after 3 years

CGT Deferral Relief

Potential unlimited indefinite deferral of an existing CGT bill

Loss Relief

Maximum exposure of 38.5p on the £1 for a 45% income taxpayer

Business Relief

Potential inheritance tax saving of 40p on the £1 after 2 years

SEIS

50% Initial Income Tax Relief

Effective net cash outlay of 50p on the £1

CGT Freedom

No Capital Gains Tax to pay on any SEIS gains after 3 years.

CGT Reinvestment Relief

Potential exemption of an existing CGT bill on 50% of the gain to the extent reinvested

Loss Relief

Maximum exposure of 27.5p on the £1 for a 45% income taxpayer (or 13.5% if CGT Reinvestment Relief claimed)

Business Relief

Potential inheritance tax saving of 40p on the £1 after 2 years

TAX **SUMMARY**

Although the EIS grants generous tax reliefs to investors, it's not considered an aggressive tax planning strategy because it is a government scheme. Current legislation provides tax incentives to encourage investment.

The following are the tax benefits offered to investors in companies that qualify for EIS and SEIS:

Income Tax Relief (EIS & SEIS)

EIS - An individual's income tax can be reduced by up to 30% of the amount invested in qualifying EIS shares.

SEIS - An individual's Income Tax liability can be reduced by up to 50% of the amount invested in eligible SEIS shares.

EIS and SEIS - To avoid Income Tax relief being withdrawn, a qualifying investment must be held for at least 3 years from the date of issue (EIS & SEIS) or for 3 years from the beginning of trade if later (EIS).

EIS - There is no minimum subscription per company, and an investor's maximum investment for which they can obtain Income Tax relief in any tax year is £1 million. The maximum is £2 million for Knowledge Intensive companies - see page 20.

SEIS - There is no minimum subscription amount per company, and the highest investment for which an investor can claim Income Tax relief in any tax year is £100,000.

EIS & SEIS - **"Carry Back"** - Individuals may elect for their share subscriptions (up to their maximum annual allowance) to be treated as if they were made in the previous tax year, effectively carrying Income Tax relief back one year. With EIS, up to £2 million can be invested, of which £1 million can be applied to the previous tax year. With SEIS, up to £200,000 can be invested, of which £100,000 can be applied to the previous tax year.

EIS & SEIS - Income Tax relief is restricted to the amount that reduces the individual's taxable income for the year to 'zero'.

CGT Freedom (EIS & SEIS)

No Capital Gains Tax is payable on the disposal of shares after 3 years, or 3 years after commencement of trade provided the initial Income Tax relief was given and not withdrawn on those shares. The shares can be kept for much longer, allowing any CGT free gains to accumulate over a longer period.

CGT Deferral Relief (EIS)

When an investor disposes of an asset that generates a capital gain, the capital gains realized can be deferred for as long as the EIS-qualified shares are held.

The disposal of the asset that generated the deferred gain must have occurred within 36 months of the EIS investment's share issue date or before the first 12 months of the EIS investment's share issue date.

A deferral relief is unlimited, meaning it isn't limited to £1 million per annum and can be claimed by investors whose interest in the company is more than 30%.

CGT Reinvestment Relief (SEIS)

When an investor disposes of an asset that gives rise to a capital gain by investing in SEIS, Reinvestment Relief of 50% of the gain reinvested is available. Eligibility for this relief is the same as for Income Tax relief.

The disposal of the asset that generated the gain being deferred should be in the same year as the Income Tax claim.

Reinvestment relief is limited to a maximum of £100,000 per tax year.

Loss Reduction (EIS & SEIS)

EIS & SEIS - If EIS shares are sold at a loss (after considering Income Tax relief), the loss can be set against the investor's capital gains or income in the year of disposal or the preceding year.

EIS - For losses offset against income, the net effect limits investment exposure to 38.5p on the £1 for a 45% taxpayer if the shares become valueless.

SEIS - For losses offset against income, the net effect is that, if the shares become entirely worthless, the investment exposure is limited to 27.5p on the £1 for a 45% taxpayer. This can be further reduced by up to 14p on the £1 by claiming CGT Reinvestment Relief, limiting the investment exposure to 13.5p on the £1.

EIS & SEIS - Losses can also be offset against future capital gains at the prevailing rate.

Business Relief - Inheritance Tax (EIS & SEIS)

After two years of holding the investment, shares in qualifying companies will be eligible for Business Relief for Inheritance Tax purposes at rates of up to 100%. This means that any Inheritance Tax liability for such shares is reduced or eliminated entirely.

EIS and SEIS enterprises must meet several conditions to be considered eligible investments. You can read this guide to learn more about the requirements regarding EIS and SEIS.

In addition, the investment must be put to good use in a qualifying trade. Most business practices are admissible, but some are not. If these excluded trades account for more than 20% of its regular operations, it would be ineligible for the scheme.

The following activities are examples of **what is not permitted**:

- Production of coal or steel
- Farming or market gardening
- Forestry
- Legal or financial services such as banking and insurance
- Leasing or property development
- Energy generation
- Exporting electricity
- Managing hotels or nursing homes
- Dealing in futures or securities
- Offering services to a non-qualifying company

INCOME **TAX RELIEF** EXAMPLE

Example - Investing £100,000 in an EIS and an SEIS

	EIS	SEIS
Gross Total Initial Investment	**£100,000**	**£100,000**
Less Income Tax Relief @ 30% or 50%	(£30,000)	(£50,000)
Less Income Tax Relief @ 30% or 50%	£70,000	£50,000

An individual who holds no more than a 30% interest in the company (passes a 30% Interest Test) can reduce their Income Tax liability by up to 30% of the amount invested, provided they hold an EIS qualifying investment for at least 3 years from the date of issue of the shares, or 3 years from the date of commencement of trade (if later). They can lower their Income Tax relief by up to 50% with SEIS under the same conditions. There is no minimum subscription, and the maximum investment in qualifying shares that qualify for EIS Income Tax relief in the current tax year is £1 million.

For Knowledge Intensive companies, the maximum is increased to £2 million. In the current tax year, the maximum investment in SEIS qualifying shares that qualify for Income Tax relief is £100,000. Up to a limit of the investor's Income Tax liability, tax relief is offset in the applicable year of claim. In other words, initial Income Tax Relief can reduce an investor's tax bill to nil.

Subscriptions may be treated as if they were made in the previous tax year provided their total claim, including any amounts already subscribed for in the last tax year, doesn't exceed the annual limits for the tax year in question.

For instance, an investor who has made no EIS investments in a tax year can make EIS subscriptions of up to £2 million in the next tax year and elect to carry back £1 million to the previous tax year to obtain Income Tax relief.

Individuals (including spouses and civil partners separately) are eligible for income tax relief on the total amount subscribed in eligible qualifying company shares. This relief is normally passed on to the investor in a tax rebate or via an adjustment in their PAYE code. The relief may only be claimed once the company has sent the investor Form EIS 3 or SEIS 3.

CGT **(CAPITAL GAINS TAX)**

There is no CGT payable on gains from investments made in an EIS or SEIS company (on which EIS or SEIS Income Tax Relief has been obtained and not withdrawn) where the investments have been held until the later of 3 years from the date of the subscription (EIS and SEIS) or from the date of commencement of the company's trade (EIS). EIS or SEIS Income Tax relief must be granted on shares to qualify for CGT Relief on disposal. If full Income Tax Relief isn't retained, partial CGT Relief on disposal may be available.

Seeing this in Action

A higher rate taxpayer has a £100,000 capital gain on the disposal of their second home. The investor has already used their full annual CGT allowance. They invest £100,000 in EIS and another £100,000 in SEIS. The amount of the gain that can be deferred has no limit and is restricted only by the amount subscribed for EIS qualifying shares in the company. Gains may be deferred until the EIS qualifying shares are disposed of or when other events trigger withdrawal of the deferral relief if earlier. Once the EIS Company shares have been sold, the deferred gain will be subject to CGT in the year of disposal. With SEIS, Reinvestment Relief is available on 50% of the gains. This is not repayable, provided Income Tax relief is not withdrawn.

The example assumes the investor is liable for Capital Gains Tax at the rate of 28%, which is the higher rate of CGT on the sale of residential property that's not the main residence.

	EIS	SEIS
Gross Total Initial Investment	**£100,000**	**£100,000**
Less Income Tax Relief @ 30% or 50%	(£30,000)	(£50,000)
Net Cost of Investment	£70,000	£50,000
Hypothetical Value of Investment after 3 years	£160,000	£160,000
Tax Free Gain	£60,000	£60,000
Total Tax Free Return to Investor (Tax free gain of £60,000 plus Income Tax relief)	£90,000	£110,000

*The hypothetical values are for illustration purposes only

CGT **DEFERRAL RELIEF** & REINVESTMENT RELIEF EXAMPLES

With EIS, CGT on gains realised on different assets can be deferred if investors invest it into EIS qualifying shares.

To qualify for CGT, the investor must subscribe for EIS shares one year before or three years after selling or disposing of their assets that generated the gain being deferred.

It's unnecessary to claim EIS Income Tax relief to obtain deferral relief. A deferral relief is unlimited and can also be claimed by investors (individuals or trustees) whose interest in the company doesn't fail the 30% tests.

If the shares against which the gains are deferred are held until death, the deferred gain is never chargeable, so the deferral is definite.

There are several circumstances in which a chargeable event may occur concerning deferred gain, the result of which is the gains becoming chargeable. Individuals and trustees should seek advice concerning events that could result in the withdrawal of relief.

Investors that invest in SEIS can get Reinvestment Relief on up to 50% of the gain realised from assets. The investor must claim relief against a gain in the same year as Income Tax.

Unlike EIS, where gains are deferred, with Reinvestment Relief, the 50% tax on gains doesn't become repayable in the future.

CGT Investment Deferral Relief Example

	EIS	SEIS
Initial Investment	**£100,000**	**£100,000**
Less Income Tax Relief @ 30% or 50%	(£30,000)	(£50,000)
Capital Gains Deferral Relief (assuming CGT at 28%)**	£28,000	-
Reinvestment Relief (assuming CGT at 28%)**	-	£14,000
Net Cost to Investor	£42,000	£36,000
Shares Sold - Hypothetical Value*		
Hypothetical Sale Value	(£160,000)	(£160,000)
Capital Gain	£60,000	£60,000
Chargeable Capital Gain (tax free if held for more than 3 years)	£0	£0
Deferred Gain Becomes Chargeable	**£100,000**	**-**
Tax payable on deferred gain at 28%**	(£28,000)	Nothing is payable with Reinvestment Relief
Value of EIS deferral relief	Capital gains tax of £28,000 has been deferred. This can potentially be deferred again in new EIS or by for example using future CGT allowances etc.	-
Net Profit on the Net Cost to Investor	**£90,000**	**£124,000**

*The hypothetical values are for illustration purposes only.

** Assumed CGT at the rate of 28%, which is the higher rate of CGT on the sale of residential property that is not the main residence.

LOSS **RELIEF** EXAMPLES

EIS and SEIS shares that are sold at a loss (after taking into account Income Tax relief, which is retained) are eligible for Loss Relief. The loss can be set against an investor's capital gains or income, either in the year of disposal or the previous tax year.

Depending on the investor's marginal income tax rate and if the shares become entirely useless, the net effect is to limit the investment exposure to as much as 38.5% on the £1 for EIS for losses offset against income.

In the same way, with SEIS, the net effect is to limit investment exposure to as little as 27.5% on the £1 or where Reinvestment Relief is claimed, 13.5% on the £1. Losses can also be relieved against capital gains at the prevailing rate of 20% for higher rate taxpayers (28% for UK residential property).

Seeing this in Action

An investor loses money on an EIS and SEIS investment, which are now worth nothing. The loss can be offset against Income Tax for the same year or the prior tax year. Alternatively, it can be offset against capital gains for the same year or carried forward to be offset against future gains, subject to the normal treatment of CGT losses.

Loss relief can reduce the investor's exposure to 38.5% or 27.5% of the original investment if they select to offset the loss against Income Tax due for the current year. This is assuming the investor pays Income Tax at a marginal rate of 45% and has sufficient income to do so. It's assumed that Reinvestment Relief isn't claimed.

Example - Loss Relief against Income Tax - EIS & SEIS

	EIS	SEIS
Gross Total Initial Investment	**£100,000**	**£100,000**
Less Income Tax Relief at 30% or 50%	(£30,000)	£50,000
Net Cash Outlay for Investment	£70,000	£50,000
Net Loss if Investment fell to £0	(£70,000)	(£50,000)
Loss Relief against income at 45%	£31,500	£22,500
Net loss	£38,500	£27,500
Percentage of original outlay	38.5%	27.5%

Example - Loss Relief against Capital Gains Tax - EIS & SEIS

Suppose the loss is offset against capital gains tax and the investor has enough gains to offset the loss. It can then be claimed against capital gains for the current year or carried over and relieved against future capital gains. Capital gains tax is currently set at 20% (or 28% for UK residential property) for higher-rate taxpayers.

	EIS	SEIS
Gross Total Initial Investment	**£100,000**	**£100,000**
Less Income Tax Relief at 30%	(£30,000)	(£50,000)
Net Cash Outlay for Investment	£70,000	£50,000
If investment fell to £0 net loss relief at 28%	(£19,600)	(£14,000)
Net Loss	(£50,400)	(£36,000)
Percentage of original outlay	50.4%	36%

Thus, an individual with income subject to higher income tax rates will choose to balance the loss against income rather than capital gains if possible.

BUSINESS **RELIEF** (INHERITANCE TAX) EXAMPLE

For Inheritance Tax purposes, shares in EIS and SEIS qualifying companies are usually eligible for Business Relief. After 2 years of holding such an investment, relief can be up to 100%, indicating that any liability to Inheritance Tax is reduced or eliminated in respect of such shares. Example: An investor who has already used their full Inheritance Tax nil rate band invests £100,000 in cash and EIS and SEIS investments.

The example compares an EIS investment of £100,000, a SEIS investment of £100,000, and a cash holding of £100,000. It assumes that the investor is a higher rate taxpayer who has already fully used their Inheritance Tax nil rate band, and that all other allowances have been used.

If the shares have been held for at least 2 years before death, the investment may be eligible for Business Relief for Inheritance Tax purposes at up to 100%. With the other benefits of the EIS and SEIS, the investment's effective cost may be considerably reduced.

Initial Investment	Holding of cash	EIS investment	SEIS investment
Total Gross Initial Investment	£100,000	£100,000	£100,000
Less income tax relief @ 30% or 50%	-	(£30,000)	(£50,000)
Net Cash Outlay for Investment	£100,000	£70,000	£50,000
Hypothetical value of cash and cash from the EIS / SEIS tax relief	£100,000	£30,000	£50,000
Hypothetical value of EIS / SEIS investment*	-	£100,000	£100,000
Less IHT on cash balance	(£40,000)	(£12,000)	(£20,000)
Total Value left to Estate	£60,000	£118,000	£130,000

*The hypothetical values are solely for illustration purposes only.

HOW **TO** INVEST IN EIS

There are several ways to invest in EIS. The approach taken will be determined by the investor's existing knowledge of EIS, risk profile, and desired level of advice. The main options are shown below.

1. Through a Financial Advisor, Wealth Manager, or other Professional Advisors

This is an excellent option for someone who wants professional counsel on their overall financial situation. It's also appropriate where specific recommendations and advice are required for EIS funds, portfolios, or companies.

2. Working with an EIS Investment Manager directly

This is typical if an investor already has a relationship with a manager or likes a manager's style or approach. It's also an excellent alternative for those who believe they're sophisticated and experienced enough to not require professional advice. This option typically gives investors the advantage of investing in a diversified portfolio.

3. Purchasing EIS Qualifying Company Shares Directly

This is an approach usually taken by 'Business Angels', or those that consider themselves seasoned entrepreneurs and serial investors. They sometimes also provide expertise and contacts as well as investment capital. Anyone may adopt this option within the network of the company owners raising funding through EIS. Also, individuals who prefer to know exactly where their money is going and perhaps have their portfolio of EIS companies may take this approach.

4. Through a Crowdfunding or Investment Platform

In addition to – or instead of – existing distribution channels, EIS qualifying companies are increasingly looking to raise money directly on investment platforms. These platforms have seen considerable progress recently, which, combined with accessible information, has resulted in this becoming a more popular choice for sophisticated/experienced investors looking to invest in single company EIS. Also, platforms are becoming more popular with investors who would've previously invested directly into an EIS company. Depending on the route investors pick, varying levels of assistance will be available, but all options will follow the same core underlying method laid out by **HMRC**.

INVESTING **IN** EIS - BENEFITS OF INVESTING THROUGH A CROWDFUNDING OR INVESTMENT PLATFORM

Profitable investments

Crowdfunding is a great place to start if you want to use your money, whether individually or for a retirement plan, but don't have that much to invest. Investors frequently seek out prospects with lower costs and more considerable benefits. The potential of the crowdfunding market is enormous, with several unique initiatives that have successfully concluded with satisfying early investment returns.

An Easy Start

Thanks to accessible crowdfunding platforms for buyers, the entire transaction takes little time and requires little or no commitment. It's also unnecessary to have 'the right connection or contacts.' All fundraising campaigns are public and accessible with a few clicks.

Opportunities for small investments

No matter how much money you have, there are always options for you to become a backer. Minimum limits are imposed by crowdfunding sites that are open to practically everyone, with thresholds depending on the platform's business model.

Tax Incentives

Crowdfunding investors benefit from lowering their tax burden. Because the regulatory framework in this industry is still developing, supporters must follow the same rules as stock market transactions. Investors must record any profit or loss they earn after selling a share in the company. For example, because the benefit may be withdrawn entirely from the portfolio, small companies and individual investors may be exempt from paying investment capital gain taxes, as the gain might be entirely excluded from the capital.

Helping Hand for innovative startups

Existing brands, as well as unknown startups, use crowdfunding sites to get funding because it offers an incredibly cost-effective way to raise capital. The crowdfunding community is also a terrific place to test product ideas, create pre-sale promotions, and get feedback from customers. As a result, there is great potential to assist businesses that investors admire. In exchange for the assistance provided, supporters have the opportunity to expand their network of connections. With this in mind, the ideological component of crowdsourcing may be more important to investors than the financial aspect alone. You can read this article for more information about investing on crowdfunding platforms.

KNOWLEDGE **INTENSIVE** COMPANIES

The EIS rules are different when applied to investments in companies classified as 'Knowledge Intensive.' as discussed earlier in this guide.

Knowledge Intensive companies are eligible for EIS if they have fewer than 500 employees (compared to fewer than 250 for other companies) and have been trading for less than 10 years (compared to less than 7 years for other companies). They're also allowed to receive up to £20 million in lifetime funding through SEIS, EIS and VCTs (compared to up to £12 million for other firms). These distinctions indicate that Knowledge Intensive companies may play a beneficial role in growing the UK economy and, as such, deserve special attention. The doubling of the individual investment and annual total investment limit is based on the same reasoning.

It's essential to understand how a company qualifies as Knowledge Intensive in the eyes of HMT and HMRC. In addition to the stipulations mentioned above, official guidance, as described in HMRC's Venture Capital Schemes Manual published at the end of 2017: & VCTs (compared to up to £12 million for other firms), is as follows:

Operating costs

At least one of the following conditions must be met:

- The company must have spent at least 15% of its relevant operating costs on research and development or innovation in 1 of the 3 relevant years preceding the date of the investment.
- In each of the 3 years leading up to the investment, the company must have spent at least 10% of its relevant operational costs on research and development or innovation.

Skilled employees or innovation

At least one of the following conditions must be met:

- At the time of the investment and for the next 3 years, a minimum of 20% of the company's fulltime employees must be classified as skilled employees.
- During the investment, the company should be engaged in work to create intellectual property (IP). Within 10 years, most of the company's business activities should consist of IP exploitation, businesses that utilise the IP, or both.

These rules are not overly complicated or prohibitive; some are generous. For example, the threshold for skilled employees has been set low to avoid complex regulations for businesses that may hire people who lack a certain degree of certification but are experienced and expert researchers. This once again demonstrates the government's commitment to EIS. Also, we can expect even more flexibility in the near future, which is encouraging. HMT has stated that it will consult on a 'new Knowledge Intensive approved fund structure' to provide additional incentives to attract investment.

The Patient Capital Review

Back in 2016, the Prime Minister announced the Patient Capital Review to determine how best to assist the UK's fledgling innovative companies to obtain the funds they need to scale. The term 'patient capital' is used to describe investments made with no expectation of immediate profit, with the idea that such investments should underpin the long-term development of the country's most promising businesses.

THE **FUNDAMENTALS** OF RISK IN EIS

When considering investing in EIS, remember that they are higher-risk investments. This fact was reinforced by a principles-based test for EIS, introduced by the Finance Bill 2017-2018. The "risk-to-capital conditions" must now be met to ensure that "tax-motivated investments, where the tax relief offers a large part of the return for an investor with low risk to the investor's capital, will not be eligible for relief", according to HM Treasury.

To be eligible for the scheme, an investment should meet the following criteria:

- The company where the investment is made should have objectives for long-term growth and development goals.
- The investment must include a significant risk that investors will lose more capital than they gain as a return (including any tax relief).

Systemic risk

The possibility of a market or sector collapsing is known as systemic risk. EIS portfolio companies tend to have lower systemic risk. Because most are unlisted and due to the long- term nature of the investment, they are less susceptible to market emotional highs and lows.

Liquidity

EIS investors must invest for three years to enjoy the tax benefits. Some EIS investments may take significantly longer to attain a good exit because most EIS companies are not publicly traded, making it difficult to liquidate quickly. So, before investing, an investor should carefully examine the likelihood of needing the funds before the investments mature.

Eligibility

An investment manager or adviser will most likely require assurance that a company is eligible for EIS before considering it for investment. An investee company can apply to HMRC for 'Advance Assurance,' which is an indication that, based on the information submitted to HMRC, it meets the EIS qualifying criteria. More information on Advance Assurance can be found below

Advance Assurance

Investors should consider EIS where companies have obtained Advance Assurance to minimise Eligibility Risk.

HMRC provides a free service to companies that want to raise money through EIS or SEIS. They give an opinion on whether the company's proposed share issuance will qualify for the EIS/SEIS tax reliefs once it submits an application. As a result, Advance Assurance gives investors peace of mind that their investment will qualify for EIS tax benefits.

TAX **RELIEF** AND THE INVESTMENT PROCESS

A typical timeline for an EIS or SEIS investor in a single company is outlined below. The timeline shows the various stages involved and the order in which they occur.

The process for a fund or portfolio is the same. The main difference is that the investor would usually subscribe to the fund, and the manager would invest in the EIS companies. The manager would then issue EIS 3 certificates to the investor for each EIS company in which the fund invests.

TYPICAL **EIS AND SEIS** TIMELINE

- The EIS or SEIS Company is Established (or already trading)
- Investor Subscribes for Qualifying Shares in the EIS or SEIS Company
- Company Share Certificates Issued
- The EIS Company Submits an EIS 1 or SEIS 1 Form to HMRC
  (The company can't file the EIS 1 or SEIS 1 Form until it has carried on a qualifying trade or activity for at least 4 months, or has spent at least 70% of the money raised in the case of SEIS.)
- HMRC Issues an EIS 2 or SEIS 2 Form to the Company
- An EIS 3 or SEIS 3 Form is Issued to the Investor
- The Investor completes Form EIS 3 or SEIS 3 and claims Tax Relief

HOW **TO** CLAIM EIS / SEIS RELIEF

An investor must fill out Form EIS 3 / SEIS 3 and send it to HMRC to obtain tax relief. Investors can use the tax relief in a variety of ways, such as:

- An adjustment to their PAYE code
- A tax repayment
- Agreeing to offset the relief against any outstanding tax liabilities

There are additional rules for Capital Gains tax. Investors should seek expert advice on the most effective strategy to obtain tax relief in their specific circumstances.

INTERESTED? **TALK TO OUR TEAM**

To find more about EIS and SEIS, please visit **https://www.trendscoutuk.com/** You can also email us at **team@trendscoutuk.com** or call us on **+44203 3724223**.

We specialise in the government initiatives of EIS and SEIS.

We connect angel investors and founders in the heart of London, building strategic collaborations that generate profit and growth.

We have over **30 years of business experience** and a network of innovative entrepreneurs and investors, enabling us to recognize upcoming prospects before they hit the masses.

By the numbers

4,500

Platform Investors

£5 Million

Successfully Connected on the Platform

£20 Million

Raised by Trendscout Portfolio Companies

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