

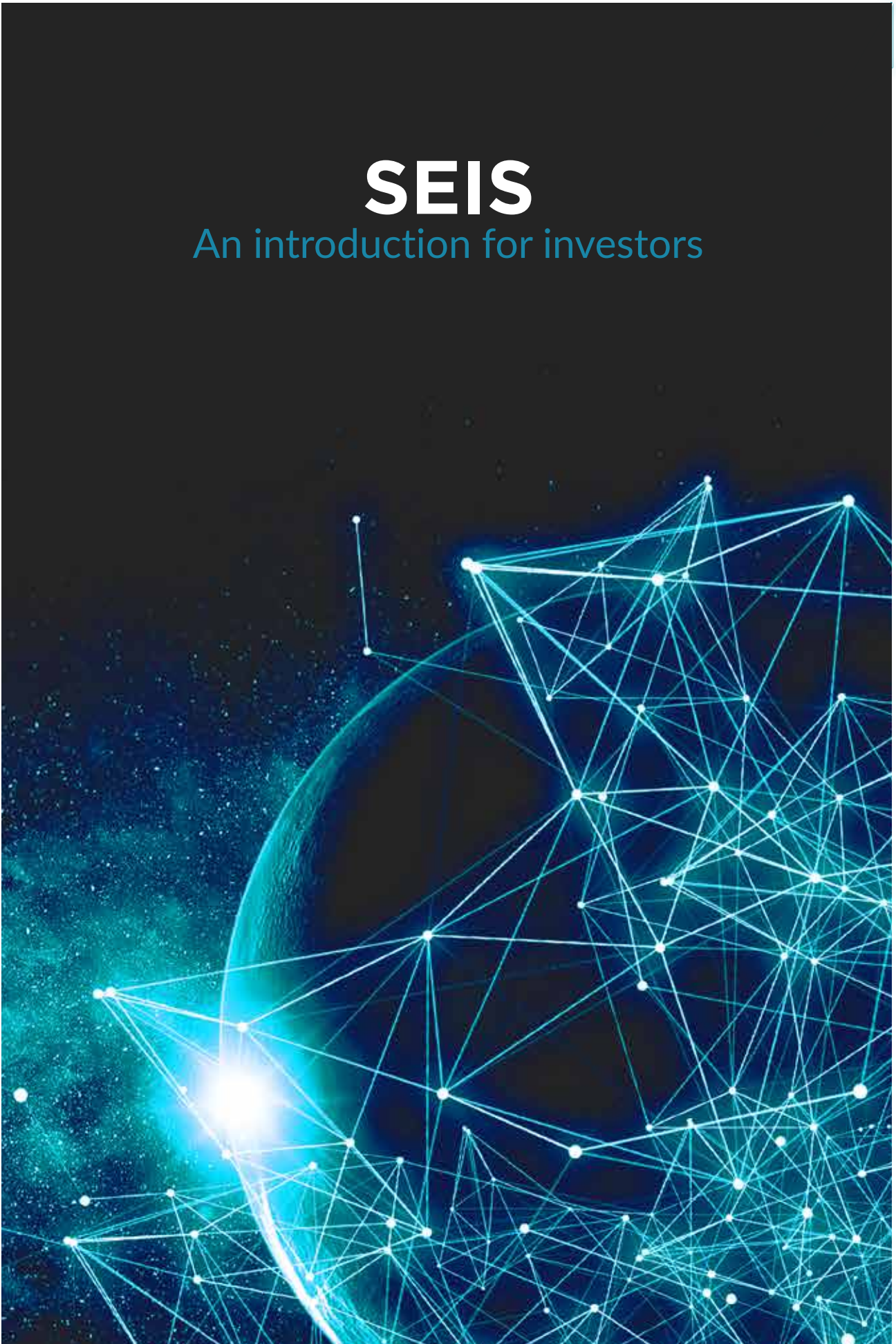


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SEIS
The Seed Enterprise Investment Scheme
An introduction for investors

SEIS

An introduction for investors



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OVERVIEW OF SEIS

The Seed Enterprise Scheme (SEIS) is designed to help smaller companies raise money when they start to trade.

SEIS was introduced on 6 April 2012 and is modelled on the long standing Enterprise Investment Scheme (EIS), but offers more generous tax breaks to incentivise investors to invest in very early-stage companies - with all the additional risk that entails.

At the time of writing, the tax breaks are worth up to 64% of the amount invested, this includes income tax relief and capital gains tax relief.

A summary of the Tax Breaks:

- Income tax relief for the investor of up to 50% of the amount invested;
- Exemption from capital gains tax on the disposal of SEIS shares;
- Losses on disposal of SEIS shares are allowable for capital gains tax purposes;
- Capital gains tax reinvestment relief for chargeable gains reinvested into SEIS shares; and
- No Inheritance tax once the shares have been held for two years.

A maximum of £150,000 can be raised by a company through SEIS investments although this amount will be increased to £250,000 for the 2023 Tax Year. It is, of course, perfectly possible for a small company to raise more than £150,000 from a single share issue; however only £150,000 of the amount raised can qualify for SEIS.

To qualify for the SEIS scheme, and realise the tax advantages associated with the scheme, there are many complex conditions that need to be met both by the company and the investor, at various stages before, during and after the share issue.

The tax advantages available under SEIS can be withheld or withdrawn from investors if the detailed rules are not followed for at least three years after an investment is made.



THE COMPANY PERSPECTIVE

What companies can qualify

A company seeking to use SEIS must:

- Not have gross assets over £200k (£350k from April 2023) when the shares are issued (for a parent company this is the sum of the gross assets of all members of the group, ignoring rights of shares in or loans to another member);
- Not be a member of a partnership; and
- Have less than 25 full-time equivalent employees in total when the shares are issued.

Throughout the three year period starting with the date of issue of the shares, the company must:

- Have a permanent establishment in the UK;
- Exist for the purpose of carrying out one or more “new qualifying trades”; and
- Be the only party to carry out the activities of the new qualifying trade (unless the trade is acquired by an unconnected party or undertaken by a qualifying 90% subsidiary).

Throughout the period starting with the date of incorporation and ending three years after the date of the share issue, the company must not:

- Be controlled or under the control of another company (ignoring any “off the shelf” period from 2013/14 onwards); or
- Be a party to arrangements that would result in it becoming controlled by another company; or
- Control any other company unless it is a qualifying subsidiary (eg. a 51% subsidiary that is not controlled by any other company).

Failure to comply with these conditions throughout the three year holding period will result in the various tax reliefs being withdrawn.

Companies which at the time of the share issue are trading on a recognised stock exchange or have arrangements in place to become a quoted company (or subsidiary of a quoted company) cannot use SEIS.

Companies that have previously raised money under the EIS or Venture Capital Trust (VCT) schemes cannot use SEIS. However, companies that raise money under SEIS can go on to raise money from EIS or VCT investors.

De Minimis Aid

Any de minimis aid the company has received in the three years prior to the share issue is deducted from the maximum qualifying investment of £150,000 (250,000 from April 2023).

De minimis aid includes not only grants, loans and subsidies, but also training, licences, and other free supplies from local enterprise partnerships or regional development agencies. Normally a company will be informed when they receive de minimis state aid.

TAX RELIEF OVERVIEW

To qualify for the tax advantages available under SEIS, there are conditions that the investor needs to meet and conditions that the company needs to meet. Some of those conditions apply at the time of investment; others must be met during periods before and up to three years after the share issue.



Tax Reliefs - Overview

The tax reliefs available to the investor under SEIS are:

- Income tax relief of up to 50% of the amount invested, for up to £100,000 (£200,000 from April 2023) of qualifying investments annually (income tax relief can also be carried back one tax year);
- Gains on the disposal of SEIS shares after more than three years may be exempt from capital gains tax;
- Losses on the disposal of SEIS shares are allowable for capital gains tax purposes;
- Half of chargeable gains on the disposal of any asset may be reinvested into SEIS shares and attract an exemption of up to 50% of the amount invested; and
- SEIS investments should qualify for inheritance tax once held for two years.

Income Tax Relief

Under SEIS, relief can be claimed by an investor for qualifying investments totalling up to £100,000 (the permitted maximum) in any tax year. There are plans to increase this from the 2023 tax year to £200,000.

The investor can offset up to 50% of the value of the investment(s) up to the permitted maximum against their income tax liability for the tax year in which the investment was made.

The investor can also choose to treat some or all of the investment as being made in the previous tax year for the purposes of income tax relief, and offset 50% of the value of the investment against their income tax liability for the tax year immediately previous to the tax year in which the investment was made.

Relief can only be claimed against the amount of income tax the investor is due to pay in the UK; any unused income tax relief from an SEIS investment cannot be carried forward to future tax years or repaid to the investor.



THE INVESTOR PERSPECTIVE

Example 1 – Income Tax Relief

In 2019/20 Mary expects to have an income tax liability of £40,000.

In March 2020 Mary makes a qualifying SEIS investment of £20,000.

Mary can choose to claim a “tax reducer” of 50% of £20,000 = £10,000.

Mary’s income tax liability is reduced by £10,000 from £40,000 to £30,000.

Mary’s £20,000 SEIS investment has, in effect, cost her only £10,000.

Example 2 – With Carry-Back and Unused Relief

In 2018/ 19 Joe had an income tax liability of £35,000.

In 2019/ 20 Joe expects his income tax liability to be rather lower, around £25,000.

Joe decides to make a series of qualifying SEIS investments totalling £130,000 which he completes between December 2019 and February 2020 (ie. In the 2019/20 tax year).

Joe made no qualifying SEIS investments in the previous (2018/19) tax year.

The maximum investment that Joe can claim SEIS relief on in relation to any one tax year is £100,000.

However, Joe can claim to treat a proportion of his SEIS investments as being made in the previous tax year, where it is beneficial to do so.

Joe can (for example) claim to treat £70,000 of his £130,000 2019/20 SEIS investments as having been made in the previous tax year, 2018/19. He can then claim a tax reducer of $50\% \times £70,000 = £35,000$ against his 2018/19 tax bill.

Joe can also claim a tax reducer for the balance of his 2019/20 SEIS investments, £60,000, against his 2019/20 tax bill. That would be a reducer of $50\% \times £60,000 = £30,000$.

After his claims to SEIS income tax relief his tax liabilities would then be:

2018/19: £35,000 - £35,000 = £nil

2019/20: £25,000 - £25,000* = £nil

* for 2019/20, Joe is entitled to a tax reducer of up to £30,000, however his 19/20 tax bill is only £25,000, so the balance, £5,000, is lost – it cannot be carried forward to the next tax year or repaid to Joe by HMRC.

Making a claim to Income Tax Relief

Entitlement to SEIS income tax relief is not automatic; a claim must be made, and to be able to claim the investor must have received form SEIS 3 from the company. The claim is made by entering onto the investor’s tax return the amount subscribed – limited to the permitted maximum – and details of the investment (company name, total amount subscribed, date of issue, name of the HMRC office authorising the SEIS 3, and the HMRC reference).

A claim to carry back the relief to the previous tax year can be made on the investor’s tax return for that earlier year, or, if the tax return has already been filed, by writing to HMRC with full details of the claim and a calculation of the tax repayment due.

THE INVESTOR PERSPECTIVE



Capital Gains Tax Reinvestment Relief

Under SEIS, the investor can also claim relief against capital gains tax.

An investor who makes a capital gain on the sale of any asset and makes a qualifying SEIS investment in the same tax year can claim relief from capital gains tax. Relief is available for 50% of the gain invested into SEIS shares, on a qualifying investment up to £100,000 (£200,000 from April 2023). In other words up to £50,000 of chargeable gains can be relieved in any one tax year.

Reinvestment relief is available in addition to, and not instead of, income tax relief, so both reliefs can be claimed in respect of the same SEIS investment.

The asset does not have to be sold before the SEIS investment is made, but if it is, it must be sold in the same tax year that the SEIS investment is treated as being made for income tax relief purposes.

It is not possible to claim income tax relief and capital gains tax relief for the same investment in different tax years, so if a carry-back claim is made for income tax relief, then capital gains tax reinvestment relief can be claimed only in respect of a disposal arising in the earlier tax year.

Where a carry-back claim is made for income tax relief, it is understood that HMRC will accept a claim to capital gains tax reinvestment relief in relation to a chargeable gain arising in the earlier year - even though this appears to contravene the legislation. Caution is advised when making such a claim.

Example 1 – Reinvestment Relief

Fred sells a residential property in March 2020 giving rise to a chargeable gain of £140,000. In the same tax year he subscribes for £100,000 of SEIS shares. Fred can claim reinvestment relief of £50,000 and his chargeable gain is then reduced to £90,000.

Example 2 – Reinvestment Relief (limited to 50% of gain)

Sally sells a painting in December 2019 realising a chargeable gain of £30,000. The same tax year she subscribes for £40,000 of SEIS shares. Sally can claim reinvestment relief of £15,000 and her chargeable gain is then reduced to £15,000.

Capital gains tax exemption on sale of SEIS shares

Gains on the sale of SEIS qualifying shares are exempt from capital gains tax provided that:

- The investor received income tax relief on the investment that was not subsequently withdrawn or reduced; and
- The shares were held for at least three years prior to disposal.

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Loss Relief

If SEIS shares are sold at a loss, the loss amount, net of any income tax relief already given and not withdrawn, can be offset against taxable income for the tax year in which the shares were sold – or the tax year before.

Example 1

In March 2020 Joanna sells some SEIS shares for £20,000. She had bought them for £50,000 four years ago and obtained income tax relief of £25,000 at the time which was not subsequently withdrawn.

Joanna's loss is calculated as the loss on sale, £30,000, less the income tax received and not withdrawn, £25,000, ie. £5,000. She can claim to offset the loss of £5,000 against her taxable income for 2019/20 – or the previous tax year 2018/19.

Inheritance Tax Relief

Provided SEIS shares are held for at least two years they will normally qualify for inheritance tax business property relief and therefore be exempt from inheritance tax.

Interaction with tax relief for investments in other venture capital schemes

Investors can invest in different companies through different venture capital schemes (eg. EIS, VCT) in any tax year and receive the appropriate reliefs, provided the qualifying conditions under those schemes are met.

Income tax relief for SEIS investments is given in priority to that for investments in VCTs and EIS.

Qualifying Investors

To be a qualifying investor:

- For a three year period starting from the date of the share issue, neither the investor nor their “associates” may be employees of the company (directors are not employees for this purpose);
- For a period starting with the date of incorporation of the company and ending three years after the date of the share issue, the investor may not have a “substantial interest” in the company; and
- For a period starting with the date of incorporation of the company and ending three years after the date of the share issue, neither the investor nor their associates may receive a loan as a result of the investment.

And in addition:

- The investor may not subscribe for the shares as part of a reciprocal arrangement whereby another person subscribes for shares in a company that he has a substantial interest in; and
- The investor must not have a tax avoidance motive.

“Associates” include:

- Parents, grandparents and great-grandparents;
- Children, grandchildren and great-grandchildren;
- Spouses and civil partners;

THE INVESTOR PERSPECTIVE

- Business partners; and
- Trustees of settlements where the investor is a settlor or beneficiary.

Siblings are not considered to be associates for the purposes of SEIS.

A “substantial interest” exists where the investor holds an effective 30% holding of the ordinary share capital, issued share capital, or voting power of the company or a 51% subsidiary, or a right to receive more than 30% of the assets of the company or subsidiary in the event of a winding up. Effective holdings include those which the investor enjoys as a result of holdings through companies.

SEIS is available to directors investing in their own companies, even if they are paid for their services, subject to the substantial interest test described above.

The substantial interest test is a “once and for all test” – an investor who fails the test cannot qualify for SEIS in relation to the same company at a later date, even if a new share issue dilutes their holding below 30%.

There is an exception to the substantial interest test – an individual is not disqualified if they hold more than 30% at a time when the company has not issued any shares other than subscriber shares, and the company has not yet begun to trade or make preparations for carrying on any trade or business.

Qualifying Shares

The shares must be subscribed for wholly in cash and be fully paid-up at the time of issue.

Throughout the three year period from the date of issue, the shares must be full risk, ordinary shares which are not redeemable and carry no special rights to dividends or assets on a winding up.

The money raised by the share issue must be used for a qualifying business activity and all spent for that purpose within three years of the share issue (insignificant amounts unspent, or spent for another purpose may be ignored).

When the shares are issued, there can be no arrangements in place:

- To protect the investor’s investment;
- To sell the shares at the end of, or during the three year period; or
- To structure the company’s activities to benefit the investor in a way not intended by the SEIS scheme.

An investor can transfer their SEIS shares to a spouse or civil partner who is then treated as being the investor for the purposes of determining whether the SEIS conditions are met on an ongoing basis.



**HM Revenue
& Customs**

THE INVESTOR PERSPECTIVE

Selling SEIS Shares and Clawback

An investor needs to keep their whole investment in the SEIS qualifying company for at least three years to be able to claim the full tax reliefs available.

The investor will lose tax relief (via “clawback”) if during the three year period:

- They sell some or all of the shares;
- They form a connection with the company;
- They receive money or other assets from the company or unusually high interest on a loan to them; or
- The company ceases to meet the conditions of the SEIS scheme.

HMRC must be told within 60 days of any of the above events occurring.

Time limit to claim SEIS Relief

Relief may be claimed up to five years after 31 January immediately following the tax year in which the investment was made.

Example 1 – Time Limit

Mike makes an SEIS qualifying investment on 30 April 2020.

He has until 31 January 2027 to claim relief under SEIS.

The tax year of investment is 2020/21. 31 January immediately following this tax year is 31 January 2022. Five years from this date takes us to 31 January 2027.

How to claim SEIS Relief

The company will send the investor a compliance certificate that explains the conditions of the SEIS scheme have been met and how long the shares need to be held for. It's called an SEIS 3. Relief under SEIS cannot be claimed until this certificate is received.

Investors wanting to make a claim in respect of the current tax year may:

- Request a change to their PAYE tax code; or
- Make an adjustment to any Self Assessment Payment on Account that is due.

A claim for carry-back against the income tax liability of the prior tax year can be made on the investor's Self Assessment return.





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