Enterprise Investment Scheme

The use of Enterprise Investment Schemes (EIS) is a highly popular way of investing in a company and gaining tax relief. EIS relief is formed by two components; 30% Income Tax relief for subscription of EIS shares and Reinvestment relief which will defer Capital Gains Tax.

This factsheet discusses Income Tax relief available to investors.

Qualifying Individual

An individual is entitled to claim EIS relief on subscription for qualifying shares in an EIS company, if he is not connected with the company during the designated period of 2 years before the issue to the third anniversary of issue, or if later, the third anniversary of the date the company commenced to trade.

An individual is connected with the company, and ineligible for EIS relief where he is:

- An employee, partner, or director of the issuing company, or any subsidiary of the issuing company, although for these purposes if a director is unpaid, he will qualify for EIS relief.

- Entitled to acquire more than 30% of the voting power of the company.

- Entitled to acquire such rights as would entitle him to more than 30% of the assets of the issuing company or any subsidiary available for distribution to the company's equity holders.

- An individual who has control of the issuing company by means other than through his shareholding in the company.

- An individual who subscribes for shares in the issuing company as part of an arrangement providing for another person to subscribe for shares in another company with which, were that other company an issuing company, the individual would be connected.

In determining whether an individual controls 30% of the ordinary share capital, account must be taken of shares held by connected persons. These include the individual's spouse, parent or grand-parents and direct descendants. For these purposes, brothers, sisters, and other relatives are not taken into account.

EIS Subscriber who becomes a Director

An individual, who is a paid director or employee at the time the shares are issued, is unable to obtain EIS relief as he is connected with the company at that time. If, however, following the subscription he becomes a paid director (but not simply an employee,) then provided that the remuneration paid is at no more than a commercial rate, he will qualify for EIS relief. Where an individual has previously qualified for EIS relief, and has subsequently become a paid director, and then makes a further subscription for qualifying shares within 3 years of the first subscription he will be entitled to EIS relief on the second subscription notwithstanding that at the time of the second subscription he is connected with the company, subject of course to the normal qualifying criteria.

Maximum Investment Amount and Rate of relief

Since 6th April 2008 the maximum investment qualifying for EIS income tax relief has been £500,000 per annum. It is proposed to increase this limit to £1,000,000 with effect from 6th April 2012.

For 2011/12 Income tax relief has been increased to 30% of the amount invested. Previously this was given at the rate of 20%. EIS relief is not available where the investor subscribes less than £500.

Provided the qualifying shares on which EIS income tax relief is obtained are held for a minimum period of 3 years the income tax relief is not withdrawn on their disposal. Gains on the disposal of qualifying shares are not chargeable to CGT at any time after the end of the 3 year qualifying period.

The investor may claim up to 100% of the relief as if the shares had been issued in the previous tax year. Accordingly relief on subscriptions of up to £500,000 during 2010/11 may be carried back to 2009/10.

For shares issued before 6th April 2009, the old rules will continue to apply so that only an investment in the EIS company made within the first 6 months of the tax year may be carried back. This remains restricted to 50% of the amount invested within that period, or a total of £50,000, whichever is the lower.

For both the old and new carry back provisions the restriction that the relief carried back together with the premiums paid in the previous year do not exceed the maximum available relief for that previous year still apply.

Loss Relief against Capital or Income

If a loss arises on disposal of the investment, the loss based on proceeds less cost after deducting EIS relief obtained, is available for set off against other gains in the year. Alternatively, the loss can be set against income of the year of loss, or his income of the preceding year. Finally, if the loss is not used in any of these ways, it may, instead, be carried forward and set against future gains.

Sheltering Gains through EIS Deferment Relief

An EIS investment may also be used to shelter a gain arising on the disposal of other assets. This aspect, EIS deferment relief is discussed in detail in the Tax Planner booklet and is also available to directors of the company who are not eligible to receive Income Tax relief.