HM Revenue & Customs

Enterprise Investment Scheme and Venture Capital Trusts: Simplification

Who is likely to be affected?

Companies raising money under the Enterprise Investment Scheme (EIS) and Venture Capital Trusts (VCTs) and individuals investing under those schemes.

General description of the measure

This measure will amend the EIS to:

- relax the rules defining when a person is connected to a company through an interest in its capital;
- widen the definition of shares which qualify for relief; and,
- remove the £500 minimum investment limit.

It will also remove the £1 million limit on investment by a VCT in a single company (except for companies in a partnership or a joint venture).

Policy objective

The aim of the EIS and VCT schemes is to help smaller, riskier UK companies to compete for equity finance, recognising a market failure in the supply of such finance.

The measure simplifies the rules of the schemes making them easier for companies, VCTs and investors to use.

Background to the measure

The Government announced its intention to consult on simplification of the scheme in Budget 2011; and a consultation document, *Tax-advantaged venture capital schemes: a consultation* was published on the Treasury website on 6 July 2011.

The measure takes account of views expressed in the consultation.

This Tax Information and Impact Note updates and replaces the note published on 6 December 2011.

Detailed proposal

Operative date

The changes to EIS will apply to shares issued on or after 6 April 2012. The change to the VCT scheme will apply to shares issued on or after 1 April 2012.

Current law

The EIS is in Part 5 of the Income Tax Act (ITA) 2007.

Within that part, the rule defining when an individual is "connected" to a company (and so not eligible under EIS for relief on investment in the company) is at section 170 ITA. In particular, it provides that an individual must not possess or be entitled to acquire more than 30 percent of the loan capital and issued share capital of the company (s170(1)(b)).

The rule defining the type of shares which can qualify for relief under the scheme is at section 173 ITA. It provides (at s173(2)) that the shares must not be entitled to any present or future preferential rights to dividends.

The rule relating to the minimum investment limit is at section 157(2) ITA. It provides that to be eligible for EIS relief in respect of an amount subscribed for shares issued by the issuing company in a tax year, the investor must have subscribed at least £500 for shares in that company.

The Venture Capital Trust Scheme is in Part 6 of ITA 2007.

Within that part, the rules defining what investments, by a VCT, in a company, count as "qualifying holdings" are in Chapter 4. In particular, section 287 - the "maximum qualifying investment requirement" - provides that in any period, up to £1million may be invested by a VCT in a company as part of the VCT's qualifying holdings. If the company is a member of a partnership or joint venture, this amount is divided between the members so that the partnership or joint venture as a whole cannot receive more than £1million of investment.

Proposed revisions

Legislation will be introduced in Finance Bill 2012 to:

- disregard loan capital for the purposes of the limit on the proportion of a company's capital which an investor can hold without being treated as "connected";
- allow shares to carry a preferential right to dividends providing their amount and the date that they are payable is not dependent on a decision of the company, the holder or anyone else, and providing that the dividends are not cumulative;
- remove the £500 minimum investment limit; and,
- remove the £1 million limit for VCT investment for companies not in partnership.

Summary of impacts

Exchequer impact (£m)	2012-13	2013-14	2014-15	2015-16	2016-17
	negligible	negligible	negligible	negligible	negligible
	This measure is expected to have a negligible impact on the Exchequer.				
Economic impact	The changes in this measure will make it easier for companies and individuals to benefit under EIS and VCTs and therefore easier for companies to raise equity for investment and growth.				
Impact on individuals and households	Individual investors investing under EIS and VCTs will benefit from these simplifications to the rules of the schemes. The removal of the minimum investment limit will increase the number of investors able to invest small amounts. Around 10,000 individuals invested through EIS in 2008-09, the last year for which figures are available, and around 6,300 through VCTs.				
Equalities impacts	Compared to the self-assessment population, EIS investors tend to be male, located in the South of England and have higher overall income levels. The changes to the schemes are not likely to change that position. From the data available it is reasonable to conclude that these changes will not have any further impact on those groups affected by equality legislation.				

Impact on business including civil society organisations	The simplification proposals set out here are deregulatory overall although the level of any savings will be small. (There may be a one-off administrative impact in familiarisation with the new rules, though this is expected to be negligible.) HM Revenue & Customs operates an advance assurance system for the schemes under which companies can seek advice before making a share offer and this will assist companies in using the new definition of eligible shares. (Shares which would have previously qualified will continue to do so.) The removal of the minimum investment limit may assist companies in attracting investment via alternative sources such as crowdfunding organisations. Around 2,000 companies raise funds under EIS each year and in total around 1,600 through VCTs for all years up to 2007-08.
Operational impact (£m) (HMRC or other)	There will be some small costs in updating forms and guidance.
Other impacts	<u>Small firms impact test</u>: The EIS is designed to incentivise investment in smaller companies. The changes being introduced are based on consultation with this sector and should have a positive effect. <u>Competition assessment:</u> The changes should not have any impact on competition as they do not affect or limit suppliers' ability to compete.

Monitoring and evaluation

Uptake of the reliefs in terms of numbers of investors and investees, amounts of investment and the distribution of levels of investment, are regularly monitored, and published as National Statistics.

Further advice

If you have any queries about this change, please contact Kathryn Robertson on 020 7147 2589 (email: kathryn.robertson@hmrc.gsi.gov.uk) or Des Ryan on 020 7147 0818 (email: des.ryan@ hmrc.gsi.gov.uk).