

Investor Guide to the Seed Enterprise Investment Scheme

Up to 64% tax relief for investment in seed stage companies

In response to the need for investment in the UK's start-up business sector, the Government has introduced a new scheme to encourage people to invest in seed stage companies. Whilst there are inherent risks in investing in start-ups, the tax reliefs offered are generous. The new scheme came into effect on 6 April 2012.

Summary

The new scheme is largely modelled on the long standing Enterprise Investment Scheme (EIS), but offers enhanced tax reliefs for investment in smaller companies.

Importantly, tax relief will be available to directors investing in their own companies, subject only to the "30% Test" - they must not hold more than 30% of the ordinary share capital, issued share capital or voting rights in the company.

Additionally, in line with changes to the EIS, shares with preferential rights to dividends will qualify for SEIS relief providing their amount and date of payment is not dependent on a decision by the company, the shareholder or any other person and providing the dividends are not cumulative.

The Tax Reliefs

Income Tax relief is available at 50%, and the scheme offers 50% exemption from Capital Gains Tax, on up to £100,000 of investment.

The total tax reliefs can amount to 64% of the sum invested:-

SEIS cash subscription	£100,000
Income Tax relief at 50%	£(50,000)
CGT re-investment relief at 14%	<u>£(14,000)</u>
Net cost of investment	<u>£36,000</u>

Inheritance tax relief could add another £40,000 of tax savings.

Income Tax Relief

An investor who subscribes in cash for ordinary shares in an SEIS qualifying company can obtain income tax relief of 50 per cent on investments of up to £100,000 each year, provided they have paid sufficient tax.

Carry back provisions allow investments to be treated as made in the previous tax year.

If the shares are disposed of, or the company ceases to qualify, within three years, the income tax relief will be clawed back.

Capital Gains Tax Re-investment Relief

Investors can claim relief against Capital Gains Tax on if the gain is reinvested in a qualifying SEIS company.

Up to 50% of the reinvested gain will be exempt, giving an effective rate of relief of 14%

Note that it is not possible to claim income tax and capital gains tax relief for the same investment in different tax years.

Capital Gains Tax Exemptions

Additionally, provided the shares have been held for at least three years and SEIS income tax relief has been given and not withdrawn, any gain on the disposal of the SEIS shares will be exempt from Capital Gains Tax.

Inheritance Tax Exemption

Provided the SEIS shares have been held for two years they will qualify for Business Property Relief and therefore will be exempt from Inheritance tax.

Seed Investment Enterprise Companies

There are a number of conditions that a company must fulfil in order to qualify under the Seed Enterprise Investment Scheme. These largely mirror the rules for Enterprise Investment Scheme companies, except that SEIS companies must:

- have fewer than 25 employees;
- have gross assets of less than £200,000;
- have been trading for less than 2 years;
- must carry on a genuine new trade;
- not have raised any money under the EIS or VCT schemes.

The company or its subsidiary must carry on a qualifying trade which excludes certain financial and so-called 'passive' activities such as hiring plant, letting property and receiving royalties.

Additionally, certain land-backed trades such as operating hotels, nursing homes, farming, forestry and property development do not qualify, nor do shipbuilding, coal mining, steel production, or legal and accounting services.

The amount a company can raise through SEIS funding is limited to £150,000. The limit is disappointingly low, but was set at this level, we understand, in order to avoid the need for EU State Aid approval.

Risk

Investors considering investing in SEIS Companies must remember that the tax reliefs are only available because investing in this type of business is perceived as high risk.

Additionally, shares in unquoted companies can be difficult to sell, should you wish, or need, to liquidate your investment.

How do I find a SEIS company to invest in?

The SEIS is a new scheme, and the market is rapidly developing. Finding the right company to invest in is likely to be problematic for investors unless you are an active business angel.

We cannot recommend any individual Funds or companies, but a number of options exist for investors who are happy to make their own minds up as to where to invest their money.

Local Business Angel groups may well have investment opportunities and there are SEIS Funds advertising on the internet. Universities are sometimes able to offer investment opportunities in spin-out companies and one, Cambridge, now has its own SEIS Fund. There are also websites which act as a marketplace where companies seeking investment advertise for investors.

You should consult your financial adviser before making an SEIS investment.

Key contacts

Please contact any of the names below or your usual BDO contact for more information or to arrange a complimentary no obligation meeting.

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How can we help? BDO's Venture Capital Tax specialists provide a full range of expertise, covering both tax reliefs for investors and guidance to companies seeking investment. For more information, please contact your usual BDO contact or one of the following:

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