SOPS Connect Limited – The Enterprise Investment Scheme (EIS)

SOPS Connect Limited received 'Advance Assurance' from HMRC on January 29th, 2021. The letter is available on request and means that we can provide UK tax payers with a range of tax reliefs and benefits to improve their return and reduce investment risk.

What is EIS?

The Enterprise Investment Scheme offers several different forms of tax relief to investors who invest money into eligible companies such as SOPS Connect Ltd. Briefly, EIS offers tax benefits in the following ways:

- 30% relief on Income
- Exemption from CGT on any gains after three years from the investment
- Capital Gains Tax deferral when gains are reinvested in other EIS eligible companies
- Loss relief when EIS shares are disposed of at a loss, either by being set against the investor's capital gains or set against the income tax bill in the year of disposal
- Carry-back: applying tax relief to a previous year
- Reduction or elimination of Inheritance Tax on eligible EIS shares held for two years.

EIS rules

Investors in SOPS Connect will receive an ordinary share certificate and the company will handle the application for the EIS certificates which take a month or two to arrive following the investment.:

- In each tax year, you may only invest a maximum of £1 million in qualifying companies (the number of qualifying companies is not limited)
- The investor must hold the shares for at least three years
- The investor may not carry-forward their EIS tax relief
- The claimant must be a UK taxpayer
- The investor must not be connected to the EIS company, either as an employee, partner, or remunerated director
- The shares must be paid for in full, in cash, by the date of issue
- The shares bought by the investor must be new shares which are not on the market.

How does EIS work?

We'll now take a closer look at each of these tax reliefs, how they work and at the qualifying conditions specific to each form.

Income Tax relief

One of the main tax reliefs offered under EIS is income tax relief. Investors can claim 30% of their initial investment back as income tax relief. The relief works by reducing the investor's income tax bill, knocking off an amount equivalent to 30% of the EIS eligible investment.

For example, if you invest £100,000 in a company which is eligible for EIS, you can claim £30,000 back in income tax relief in the year you made your investment. With an annual £1 million limit per investor, this means that you can knock up to £300,000 off your income tax bill!

Capital Gains Tax exemption

All financial gains above £6,000 (with the main exceptions being your car or your main home) are subject to Capital Gains Tax. CGT is a tax on the profits you make from selling any assets. The amount you pay is determined by your tax band and can be anywhere from 10% to 28%. Most investors will be looking at paying at least 20% CGT on their gains.

EIS offers CGT exemption on any gains made from invested shares. Provided that the shares are held for at least three years after investment, any gains made on these shares may be exempt from Capital Gains Tax under this scheme. This means that if you invested £10,000 in EIS shares and then decide to sell them after three years for £40,000, you can keep the full £30,000 profit without paying any Capital Gains Tax. In this example, you'd have saved £8,400.

Capital Gains Tax deferral

EIS offers a second relief affecting Capital Gains Tax. This relief allows investors to defer paying Capital Gains Tax on any asset if the gain from the disposal of that asset is used to invest in shares in another EIS qualifying company. As such, CGT deferral aims to encourage further investment under the EIS scheme. To be eligible for CGT deferral, gains from the disposal of EIS shares must have been made within the twelve months before the EIS investment or within three years after. The relief is limited to the amount invested in the EIS company.

EIS loss relief

This risk of investing in shares is made far more appealing through the availability of loss relief for EIS investors. This form of relief can reduce the impact of losses made on investing in EIS companies.

By claiming loss relief, investors can offset any losses made on an EIS company with two possible options. The investor may either offset the loss against their income tax bill or their capital gains tax bill.

To qualify for loss relief, the value of an investment at the point of sale must be less than what is known as its effective cost. The effective cost is the sum invested less whatever the investor has previously claimed in income tax relief.

Calculating loss relief against income

The amount you can offset against any income tax bill is calculated by multiplying the value of the effective loss by the investor's marginal rate of income tax. The effective loss is the effective cost, minus the sale price.

To give you an example: for an investment with an effective cost of £15,000, which is later sold for £5,000, the effective loss would be £10,000. Assuming the additional rate of marginal tax is 45%, which is the amount applicable to most investors, the amount the investor can claim as loss relief is £10,000 x 45%, which gives £4,500 of tax relief.

Calculating loss relief against CGT

For some investors, it is more tax-efficient to offset their loss against their Capital Gains Tax bill instead. To work out the available tax relief for this route, you multiply the effective loss (as above, the effective cost less the sale price) by your CGT rate. For EIS shares bought for an effective cost of £18,000 and later sold for £3,000, the effective loss equates to £15,000. With a CGT rate of 28%, the loss relief available would be £4,200.

To claim for loss relief, you need to complete the SA108 form as part of your self-assessment tax return. You can find this form on the HMRC website.

The directors of SOPS Connect believe that EIS is highly advantageous for the company and its new investors. We welcome you to contact us with your investment enquiry.