

# FINANCE ACT 2012

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## EXPLANATORY NOTES

### INTRODUCTION

#### *Section 38 Schedule 6: Seed Enterprise Investment Scheme*

##### Summary

1. [Section 38](#) and Schedule 6 set out the new Seed Enterprise Investment Scheme (SEIS), which is designed to incentivise investment in small, early stage companies.

##### Details of the Schedule

##### **Part 1 of the Schedule**

2. Paragraph 1 of the Schedule introduces a new Part 5A to Income Tax Act 2007 (ITA), containing the rules for the new scheme.

##### *Chapter 1 of New Part 5A of ITA*

3. New section 257A defines SEIS income tax relief and provides that it will apply to shares issued on or after 6 April 2012 and before 6 April 2017. The new scheme is therefore of fixed length, but can be extended by a Treasury order.
4. New section 257AA provides that an investor is eligible for relief in respect of shares issued to him or her where particular requirements are met. There are requirements which apply to the investor, general requirements, and requirements that apply to the issuing company. These requirements are in Chapters 2 – 4 of new Part 5A.
5. New section 257AB provides that the relief is a reduction of income tax calculated as 50 per cent of the amount the investor subscribes for shares, subject to an overall limit of 50 per cent of £100,000 on the amount of relief that can be received in any one year.
6. New section 257AB(5) allows an investment or part of an investment made in one year to be treated as though made in the previous year (but not in the first year that the new scheme operates), subject to the overall limit for a year.
7. New section 257AC defines two periods of time with respect to which many of the SEIS conditions operate. Period A runs from the company's incorporation to the third anniversary of the share issue (defined at new section 257AC(4) as the "termination date"). Period B runs from the issue of the shares to the termination date.
8. New section 257AD is an overview of chapters 5 – 8 of new Part 5A, which deal with the making of claims, withdrawal of relief, and supplementary matters.
9. New section 257AE(1) mentions new Section 150E of the Taxation of Chargeable Gains Act 1992 (TCGA), which provides a relief from capital gains tax (CGT) on gains on shares which qualify for SEIS relief (see paragraphs 93 below).

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10. New section 257AE(2) mentions new Schedule 5BB TCGA, which provides relief from CGT on the disposal of assets where the proceeds are reinvested under SEIS (see paragraphs 97 to 108 below).

### *Chapter 2*

11. New section 257B is an overview of chapter 2 which contains the conditions which apply to the SEIS investor.
12. New section 257BA provides that neither SEIS investors nor their associates may be employees of the company or any qualifying subsidiary in period B (unless also a director).
13. New section 257BB provides that SEIS investors must not during Period A have a “substantial interest” in the company, defined at new section 257BF as having more than a 30 per cent stake in the company through ordinary or issued share capital, voting power or rights on winding up, or as having control of the company.
14. New section 257BC provides that SEIS investors must not subscribe for the shares as part of a wider arrangement which includes somebody else subscribing for shares in a company in which the investor – or anyone else party to the arrangement – has a substantial interest.
15. New section 257BD provides that during Period A there must be no loans to the investor or their associates which are linked to their subscription for shares.
16. New section 257BE requires the subscription for shares to be for genuine commercial reasons, and not as part of a tax avoidance arrangement.
17. New Section 257 BF defines when a person has a “substantial interest” in a company.

### *Chapter 3*

18. New section 257C is an overview of chapter 3 which contains the general requirements under SEIS.
19. New section 257CA sets out the types of shares for which investors can subscribe under the scheme, allowing for shares carrying certain preferential rights to dividends. Shares are still excluded if: they carry preferential rights to assets on winding up; they have any right to be redeemed; the amount and timing of the dividends depend on a decision of the company or any other person; or if they are cumulative. This new definition is the same as that also being introduced for the Enterprise Investment Scheme (EIS).
20. New section 257CA(4) provides that shares must be subscribed for wholly in cash and be fully paid up at the time they are issued.
21. New section 257CB requires that the shares be issued to raise money for a qualifying business activity carried on or to be carried on by the company or by a qualifying 90 per cent subsidiary. Qualifying business activity is as defined at new section 257HG.
22. New section 257CC requires that the money raised from the share issue must be spent by the end of period B, for the purpose of the qualifying business activity for which it was raised.
23. Section 257CC(2) provides that spending money on the acquisition of shares or stock in a company does not of itself amount to spending the money for the purposes of a qualifying business activity.
24. New section 257CD prevents “pre-arranged exits”, which are any arrangements in place (at the time the shares are issued) for the disposal of shares or securities in the company or its assets, or for its activities to cease, or for the investment to be protected from normal commercial risks.

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25. New section 257CE requires the issue of shares to be for genuine commercial reasons, and not as part of a tax avoidance arrangement.
26. New section 257CF is the “no disqualifying arrangements” requirement. Arrangements are “disqualifying” if they are entered into with the purpose of ensuring that any of the venture capital scheme tax reliefs are available in respect of the relevant company’s business, and either: all or most of the monies raised under the scheme are paid to or for the benefit of a party to the arrangements; or in the absence of the arrangements, it would be reasonable to expect that the business would be carried on as part of another business by a person who is a party to the arrangements, or a person connected with such a party. This is the same requirement that is being introduced for the EIS and VCT schemes.

#### *Chapter 4*

27. New section 257D is an overview of chapter 4 which contains the conditions that apply to the company.
28. New section 257DA is the “trading requirement”, requiring that the company’s main purpose throughout period B must be to carry on a new qualifying trade or trades. Alternatively if it is the parent company of a group, the business of the group must not consist wholly or as to a substantial part in carrying on non-qualifying activities.
29. Section 257DA(3) provides that if a company intends in the future to have qualifying subsidiaries which will carry on new qualifying trades, then it is treated as a parent company for the purposes of the trading requirement.
30. Sections 257DA(4) and (5) describe how “the business of the group” is to be defined: the activities of the group are to be looked at together as though carried on as one business.
31. Section 257DA(6) provides that certain intra-group transactions are to be ignored in considering what the business of the group involves.
32. New section 257DB provides that the purpose of existence test is not breached due to anything that happens because of the company or a subsidiary being in administration or receivership, or being dissolved or wound up, provided that this is done for genuine commercial reasons and not as part of a tax avoidance arrangement.
33. New section 257DC provides that throughout Period B, the new qualifying trade and any preparation work or research and development leading to it, must be carried on by the issuing company itself or by a qualifying 90 per cent subsidiary.
34. New sections 257DC(4) to (6) provide that this requirement is not breached due to the new qualifying trade being taken over by an unconnected person because of the company or a qualifying 90 per cent subsidiary being in administration or receivership, or being dissolved or wound up, provided that this is done for genuine commercial reasons and not as part of a tax avoidance arrangement.
35. New section 257DD requires the company to have a permanent establishment in the UK throughout period B.
36. New section 257DE requires the company not to be “in difficulty” at the beginning of period B. This means it must not be a “firm in difficulty” under European Commission guidelines.
37. New section 257DF requires the company to be “unquoted” at the beginning of period B and provides that there must be no arrangements at that time for it to cease to be unquoted.
38. A company is “unquoted” if its securities are not marketed to the general public – defined in new section 257DF(3) as being listed on a recognised stock exchange, listed

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on a designated exchange outside the UK, or dealt with, outside the UK, by any such means as may be designated.

39. New sections 257DF(4) and (5) provide for the Commissioners of HMRC to make the designations referred to in new section 257DF(3).
40. New section 257DG contains the control and independence requirement:
  - The control part of the requirement is that the company may not, in period A, control (whether on its own or together with any person connected with it) any other company which is not a qualifying subsidiary. There must be no arrangements in existence by virtue of which the company could fail to meet this requirement.
  - The independence part of the requirement is that the company may not, in period A, be under the control of any other company – either alone or with any connected person – and nor must there be any arrangements for this to happen (whether in period A or outside it). It may not, therefore, be a subsidiary in period A.
41. New section 257DH requires that neither the company nor any qualifying 90 per cent subsidiary may be a member of either a partnership or a limited liability partnership (or any foreign equivalent) at any time in period A.
42. New section 257DI is the gross assets requirement. Immediately before the shares are issued, the total value of the company's assets (or of the group assets where the company is a parent company), must not exceed £200,000.
43. New section 257DJ is the number of employees requirement. At the time the shares are issued, the company together with any subsidiaries must have fewer than 25 full time equivalent employees.
44. New section 257DK provides that neither the company nor any qualifying subsidiary may have previously raised money under either the EIS or VCT schemes.
45. New section 257DL ensures that any investment under SEIS is kept within the limits which allow SEIS to be regarded under EU regulations as providing *de minimis* and therefore non-notifiable State aid.
46. New section 257DL(1) provides that the amount of all SEIS investment, together with any other *de minimis* State aid received by the company in the 3 years to the date of the latest SEIS investment, must not exceed £150,000.
47. New sections 257DL(4) to (6) apply so that where a share issue takes above £150,000 the total aid received by the company in the 3 years to the date of investment, the investment in the share issue is apportioned so that relief is given only on the proportion of the investment which doesn't exceed the £150,000 limit.

## **Chapter 5**

48. New section 257E contains rules setting out how relief given to an individual is to be attributed to shares for which the individual has subscribed.
49. New section 257EA provides that SEIS relief can not be claimed more than five years after the SA filing deadline for the year in which the shares are issued.
50. New section 257EB provides that the investor can only claim relief if he or she has a compliance certificate from the company for the shares.
51. New section 257EC defines a compliance certificate. This is a certificate issued by the company stating that the shares meet the requirements for SEIS relief (excluding those requirements that are dependent on the investor).

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52. New section 257EC(2) provides that a certificate cannot be issued until the company has supplied a compliance statement to HM Revenues & Customs (HMRC) and new section 257EC(3) that it must have authority from HMRC to issue a certificate.
53. New section 257ED defines a compliance statement. This is a statement to the effect that at the time the statement is made, the requirements for SEIS are met or have been met (excluding those requirements that are dependent on the investor).
54. New section 257ED(3) provides that the company may not make a compliance statement until either it has traded for at least four months, or at least 70 per cent of the money raised by the share issue has been spent for the purposes of the qualifying business activity for which it was raised.
55. New section 257EE provides for an appeal against a decision by HMRC not to authorise a compliance certificate.
56. New section 257EF prescribes a maximum penalty of up to £3,000 where a company negligently or fraudulently issues a certificate or statement or issues one in breach of the conditions in new section 257EC.
57. New section 257EG allows the Treasury, by order, to amend new sections 257EC and 257ED. This is intended to allow changes in the administrative processes without the need for primary legislation.

## **Chapter 6**

58. New section 257F is an overview of chapter 6 which contains provisions dealing with the withdrawal of relief given for SEIS shares (“relevant shares”). Many of the provisions in chapter 6 are counterparts to conditions contained in the preceding chapters, setting out what happens when those conditions are breached.
59. New section 257FA withdraws relief where, before the end of period B, the investor disposes of shares for which SEIS relief has been given. In particular, it contains computational rules setting out how much relief is to be withdrawn.
60. New section 257FA(6) ensures that the death of an investor does not trigger the withdrawal of any relief given.
61. New section 257FB supplements those rules for cases where full relief was not obtained.
62. New sections 257FC and 257FD withdraw relief where the investor holds a call or put option in relation to the relevant shares.
63. New section 257FE withdraws relief where during period A the investor receives any value from the company relating to the relevant shares.
64. New section 257FF provides that relief is not withdrawn where the value received is insignificant (defined in new section 257FG).
65. New section 257FG defines insignificant as an amount that does not exceed £1,000, or if it does exceed that amount is insignificant compared to the amount subscribed for the shares.
66. New section 257FH defines a number of different circumstances in which value is received. These cover various ways in which the company might make payments to the investor. A number of circumstances are excluded – for example where the investor is a director of the company and is reimbursed expenses incurred in performance of his or her duties.
67. New section 257FI defines the amount of value received in the various cases described by new section 257FH.

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68. New sections 257FJ – 257FO contain supplementary provisions concerning the receipt of value in particular circumstances.
69. New section 257FP withdraws relief where, during period A, the company or any qualifying subsidiary takes over the trade or assets previously used by another person in their trade, and the investor either had or has more than a half share in the trade, or controls or has controlled the issuing company and controls or has controlled the company which previously carried on the trade.
70. New section 257FQ withdraws relief if the company acquires all the issued share capital of another company in period A, and the investor is a person or one of a group of persons, who control(s) both companies.
71. New section 257FR withdraws relief given where, at some later date, it is found not to have been due.

### **Chapter 7**

72. New section 257G provides for relief to be withdrawn or reduced by making an assessment.
73. New section 257GB sets a time limit for any such assessment, which must be made within six years of the end of whichever is the later of the tax year in which period B ends, or the tax year in which the event causing the withdrawal or reduction occurs.
74. New section 257GC sets out cases where no such assessment may be made.
75. New section 257GD provides that when an assessment is made under new section 257G to withdraw relief as prescribed by particular provisions of chapters 2, 4 and 5, interest is to be charged from 31 January following the tax year in which the assessment is made.
76. New section 257GE requires the investor to notify HMRC if he or she ceases to be a qualifying investor, or if relief should be withdrawn for one of a number of specified reasons and new section 257 DF places a similar requirement on the company.
77. New section 257GG gives HMRC power to require information where either new section 257GE or new section 257GF applies or could have applied.
78. New section 257GH gives HMRC a power to require information in other cases, specifying from whom information may be required in various different circumstances.
79. New section 257GI allows HMRC to disclose to a company that SEIS relief has been obtained in respect of its shares.

### **Chapter 8**

80. New section 257H allows for transfers of shares between spouses or civil partners not to be treated as a disposal. The SEIS relief remains attributable to the shares until a disposal or other relevant event by the spouse or civil partner to whom they were transferred.
81. New section 257HA sets out rules determining which shares are treated as having been disposed of under either new section 257FA or 257H.
82. New section 257HB provides for the continuity of SEIS relief where a new holding company is inserted above a company which has issued shares to which SEIS relief is attributable, resulting in shareholders exchanging their original shares for shares in the new holding company.
83. Providing that certain conditions as specified by section 257HB(2) are met, new section 257HB(3) provides that the original shares are not treated as disposed of, and that the relief which was attributed to them is instead attributed to the shares in the new holding company.



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84. New sections 257HC and 257HD ensure that in other respects, the SEIS legislation applies in respect of the new shares as it would have done in respect of the old shares.
85. New section 257HE contains provisions applying to nominees and bare trustees.
86. New section 257HF defines a “new qualifying trade” as being one which has not been carried on by either the company or by any other person for longer than two years at the date of issue of the shares; and neither the company nor any qualifying subsidiary had carried on any other trade before the company in question began to carry on the new trade.
87. New section 257HG defines “qualifying business activity” as either carrying on, or preparing to carry on, a new qualifying trade, or carrying on research and development from which a new qualifying trade will be developed (or which will benefit a new qualifying trade). For a business activity to be “qualifying” it must be carried on by either the issuing company or by a qualifying 90 per cent subsidiary.
88. New sections 257HH and 257HI define the terms “disposal of shares” and “issue of shares”.
89. New section 257HJ contains a number of definitions of terms used elsewhere in part 5A.

## **Part 2 of the Schedule**

90. **Part 2** provides for relief for capital gains.
91. Paragraph 2 provides for the Taxation of Chargeable Gains Act 1992 (TCGA) to be amended.
92. Paragraph 3 inserts new sections 150E and 150F into the TCGA.
93. New section 150E mirrors existing section 150A TCGA that applies to EIS shares. Section 150E reduces the consideration taken into account for capital gains tax on a disposal of shares by the amount of the SEIS relief attributable to those shares. It reduces or eliminates any chargeable gain on a disposal of shares to which SEIS relief is attributable and provides rules that permit those shares to be identified.
94. New section 150F mirrors existing section 150B TCGA that applies to EIS shares. It modifies the effect of new section 150E to limit the reduction in any chargeable gain on the disposal of shares to which SEIS relief is attributable to the extent that value is received and the SEIS relief reduced in consequence.
95. Paragraph 4 of the Schedule inserts a new section 150G into the TCGA. Section 150G introduces Schedule 5BB to the TCGA, which provides the SEIS re-investment relief.
96. Paragraph 5 inserts new Schedule 5BB into the TCGA – see paragraphs 97 to 108 below.

### ***New Schedule 5BB TCGA***

97. Paragraph 1 of Schedule 5BB sets out the conditions for relief and the amount of relief available.
98. Paragraph 1(2) to (4) sets out three conditions for relief:
  - a. An individual must realise a gain on a disposal of an asset in the tax year 2012-13.
  - b. The individual must make an investment that qualifies for SEIS relief from income tax, and claim that relief.
  - c. The individual must claim SEIS re-investment relief in respect of the amount on which the SEIS relief is claimed.
99. Paragraphs 1(5) to (7) sets out the amount of SEIS re-investment relief. Paragraph 1(5) sets the amount on which SEIS relief is claimed (“the SEIS expenditure”) against the

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gain on the disposal of the asset. Paragraph 1(6) provides that the amount of the gain that has the SEIS expenditure set against it is not liable to CGT. Paragraph 1(7)(a) restricts the SEIS expenditure on which relief may be claimed to the extent it has already been used to claim to other SEIS reinvestment relief or to EIS deferral relief. Paragraph 1(7)(b) ensures SEIS re-investment relief is not given against any part of the gain that has already been covered by other SEIS re-investment relief or by EIS deferral relief

100. Paragraph 2 of Schedule 5BB restricts the amount of SEIS re-investment relief that is given under paragraph 1 in two circumstances.
101. Paragraph 2(1) and (2) applies where the amount invested under SEIS exceeds the maximum amount of £100,000 on which an individual can obtain income tax relief in any one tax year. In this circumstance the SEIS re-investment relief is capped at the amount on which SEIS relief is due, applying the formula in sub-paragraph (2).
102. Paragraph 2(3) and (4) applies where SEIS relief is restricted before the claim to SEIS re-investment relief is made. In this case the maximum amount on which SEIS re-investment relief can be claimed is restricted by a similar amount, under the formula in sub-paragraph (4).
103. Paragraph 2(5) gives the order in which the two restrictions in paragraph 2 are to be applied in cases where they both apply.
104. Paragraph 3 of Schedule 5BB sets the time limit for claiming SEIS re-investment relief as the same as the limit that applies for claims to SEIS relief. The paragraph also makes clear that claims to SEIS re-investment relief may be made before effect is given to the claim for SEIS relief on which the SEIS re-investment relief claim depends.
105. Paragraph 4 of Schedule 5BB treats the amount on which SEIS re-investment relief is given as spread ('attributed') equally across all the shares in respect of which the claim to relief is made. This is required in order to be able to recover the correct amount of relief, should this become necessary, under paragraph 5 or 6 of Schedule 5BB (see below).
106. Paragraph 5 of Schedule 5BB applies where the SEIS relief attributed to shares is withdrawn or reduced so that the SEIS re-investment relief attributed is also withdrawn or reduced in the same proportion. For example, if the SEIS relief were reduced by 60 per cent the SEIS re-investment relief will also be reduced by 60 per cent. Where this happens paragraph 5(2) makes the individual who made the investment liable to CGT for the tax year 2012-13 on a chargeable gain of the appropriate amount. Where paragraph 5 applies to reduce the amount of SEIS re-investment relief attributable to the shares in question, sub-paragraphs (4) and (5) reduce the amount of SEIS re-investment relief remaining attributable to the shares by a corresponding amount.
107. Paragraph 6 of Schedule 5BB modifies the effect of paragraph 5 in cases where the investor in shares to which SEIS re-investment relief is attributable transfers some or all of the shares to their husband or wife or civil partner, and that transfer does not itself lead to relief being withdrawn. Where SEIS re-investment relief is withdrawn or reduced after the transfer, a gain is charged to CGT on the transferee spouse or civil partner in respect of the shares which they hold, and the amount of the gain charged on the original investor is based on only the shares they still hold.
108. Paragraphs 7 and 8 of Schedule 5BB make supplementary provision. Paragraph 7(1) permits all necessary adjustments to be made to give effect to claims or charges under the Schedule, notwithstanding the normal time limits for amending or making assessments to CGT. Paragraph 7(2) provides that when an assessment under paragraphs 5 or 6 to withdraw re-investment relief, interest is to be charged from 31 January following the tax year in which the assessment is made. Paragraph 8 defines various terms in Schedule 5BB.



### **Part 3 of the Schedule**

109. Part 3 makes consequential amendments to ITA (and in particular to the existing EIS and VCT rules in Parts 5 and 6 of that Act) and to the TCGA 1992.
110. Paragraph 7 of the schedule amends the overview of ITA, adding a reference to the new Part 5A.
111. Paragraphs 8 and 9 amend sections 26 and 27, which form part of the computational rules for income tax liability, to add SEIS relief.
112. Paragraph 10 amends section 169, which deals with the EIS rules on directors and the circumstances in which they may qualify for relief in respect of an investment in shares. The rules are amended to allow a paid director to qualify for EIS relief where the relevant investment was made before the end of the qualifying holding period for a holding of SEIS shares which attracted relief.
113. Paragraph 12 amends the EIS rules so that any SEIS investment received by a company in the 12 months to the date of issue of EIS shares, is taken into account in determining the maximum amount of investment which will attract tax relief in that 12 month period.
114. Paragraphs 11 and 13 amend the EIS rules to add a new requirement, that before a company can issue shares qualifying under EIS it must have spent at least 70 per cent of any money raised under SEIS.
115. Paragraph 14 amends the EIS rule determining identification of shares on a disposal, to include those which have attracted SEIS relief.
116. Paragraph 16 amends the VCT rules so that any SEIS investment received by a company in the 12 months to the date of any investment by a VCT, is taken into account in determining whether a holding will form part of a VCT's qualifying holdings.
117. Paragraphs 15 and 17 amend the VCT rules to add a new requirement, that before a company may receive a VCT investment it must have spent at least 70 per cent of any money raised under SEIS.
118. Paragraph 18 introduces amendments to the TCGA.
119. Paragraphs 19 and 20 make amendments to the rules which determine how any gain or loss on disposal of shares which have attracted EIS relief, is to be calculated. These amendments arise as a consequence of other changes in the Schedule and do not materially alter the rules.
120. Paragraph 21 amends Schedule 5B TCGA. Schedule 5B allows individuals to defer the time at which gains on disposals of assets become liable to CGT where they invest in shares under the terms of the main EIS. The amendments made by paragraph 21 ensure that both EIS deferral and SEIS re-investment relief cannot be claimed in respect of the same expenditure.
121. Paragraph 22 amends section 98 of the Taxes Management Act (TMA) 1970 to include the information obligations provided for by sections 257GE, 257GF, 257GG and 257GH. Section 98 lists those information obligations which may carry a penalty if not complied with.

### **Background Note**

122. The Chancellor announced at Budget 2011 that the Government would bring forward proposals for support for investment in small, early stage companies, in addition to that provided by the EIS and Venture Capital Trusts (VCT) scheme.
123. A consultation document, "Tax-advantaged venture capital schemes: a consultation" was published on the Treasury website on 6 July 2011 setting out proposals and seeking views on a number of design issues.

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124. Views expressed in response to the consultation have been taken into account in developing the new SEIS relief. The Government's response to the consultation was published on 6 December 2011 and is available on the HMT website.
125. The Government announced the proposal to introduce SEIS re-investment relief in the autumn statement 2011. HMRC issued a Technical Note outlining the scope of the relief on 6 December 2011 and draft legislation was published on 31 January 2012.