Risk to capital requirement for venture capital schemes: changes in Finance Bill 2017-18

OMB **Personal tax**

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Growing and developing complications for EIS, SEIS and VCTs.

Clause 14 of Finance Bill 2017-18 introduces an additional risk to capital condition in order for investments to qualify for any of the three venture capital reliefs – Enterprise Investment Scheme (EIS), Seed Enterprise Investment Scheme (SEIS) and Venture Capital Trusts Schemes (VCTs).

According to the published Explanatory Note, the purpose of the new condition is 'to prevent investment in companies whose activities are mostly geared towards the preservation of the capital invested rather than the long-term growth and development of the company.'

In relation to each of the three schemes, the new risk to capital condition has two legs. Having regard to all the circumstances existing at the time of the share issue, it must be reasonable to conclude both that the company in which the investment is being made 'has objectives to grow and develop its trade in the long-term' and that there is a significant risk that there will be a loss of capital of an amount greater than the net investment return.

In its written evidence to the Public Bill Committee, the ATT focused on the company objectives leg. ATT notes that it is unclear what the requirement for the company's objectives to grow and develop its trade means in practice.

ATT notes that the company must have objectives to both grow and develop but that neither verb is defined in the legislation. It explores whether there is an intended distinction in meaning between the two verbs and, if so, whether there is a risk that a company's objectives might satisfy one but not both of the 'grow and develop' tests.

The ATT's written evidence observes that the uncertainty of meaning is compounded by the addition of the words 'in the long-term' which introduces an imprecise timescale and also prompts the question as to whether the new condition would be met if the company's objectives were to grow and develop in a more immediate timescale than the long-term.

Specifically within the context of EIS, ATT ask whether the grow and develop test achieves anything given that an existing condition (Income Tax Act 2007 s 174) already requires the shares in respect of which relief is claimed to 'be issued in order to raise money for the purposes of a qualifying business activity so as to promote business growth and development'.

As a subsidiary point, in relation to all three of the venture capital schemes, ATT drew attention to an apparent inconsistency between the commencement provision within Clause 14 and HMRC's draft guidance which simply states that the new condition will apply to all investments made on or after the date of Royal Assent.

Written evidence

The written evidence submitted to the Finance Bill Committee should become available on the Parliamentary website.

It is also available on the ATT website.