



Employment and Investment Incentive Scheme – The New BES

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The new Employment and Investment Incentive Scheme (EIS) is set to replace the Business Expansion Scheme (BES), subject to European Commission approval being obtained. There is no clear date regarding when approval will be granted but, if approved, it will run until the end of 2013.

Overview

Under the new EIS, set out in s30 Finance Act 2011, qualifying investors can avail of a tax deduction for the cost of investing in certain companies. The purpose of the scheme is to promote the creation of jobs and to encourage companies to carry out research and development (R&D) activities, and to this end the new scheme widens the scope of trades that can qualify for the relief. In addition, the lifetime company investment limit has been raised to €10m (€2m under BES) and the cap on the amount that can be raised in any 12-month period has been increased to €2.5m (€1.5m under BES).

In order for the relief to apply, the company must use the funds invested by the qualifying individuals to achieve the following:

- › increase the number of employees and the average emoluments paid by the company during the relevant period **or**
- › increase the amount of expenditure by the company on R&D activities during the relevant period.

Broadly speaking, the relevant period is the period beginning on the date on which the shares are issued, provided that the company was carrying on relevant trading activities (see below) at that time, and ending three years after that date. Otherwise, the relevant period begins on the date that the company commences to carry on relevant trading activities and ends three years after that date.

Qualifying Individuals

Individuals will qualify for EIS relief if they subscribe for eligible shares in a qualifying company (see below). Eligible shares must be new ordinary shares that throughout the period of three years from the date of their issue carry no present or future preferential rights to dividends or to the company's assets on its winding-up. In addition, they must have no present or future preferential right to be redeemed. Eligible shares must be issued on or before 31 December 2013.

The minimum investment that a qualifying individual can make is €250 per year, and the maximum amount qualifying for relief is €150,000 per qualifying individual per year.

Tax relief is given by means of a deduction from the qualifying individual's total income. Individuals will get relief as follows:

- › Thirty forty-firsts of the amount invested will be given as a deduction from the individual's total income in the year in which the eligible shares are issued.
- › And a further eleven forty-firsts of the amount invested may be available as a deduction at the end of the holding period, provided that the company concerned has increased its number of employees and related payroll expense (unless to the extent that there has been a general reduction in the basic pay rate) since the investment was made **or** the company has increased its expenditure on R&D.

Connection with a company

An individual cannot avail of the relief if he or she is connected with the qualifying company at any time during the specified period. The specified period is the period beginning on the incorporation of the company (or, if the company was incorporated more than two years before the date on which the shares were issued, beginning two years before the issue of the shares) and ending three years after the issue of the shares. An individual is connected to a company if the individual (or an associate of the individual) is:

- › a partner of the company or
- › a director or employee of the company or of another company that is a partner of that company who, during the period of three years after the date on which the eligible shares were issued, receives or becomes entitled to receive any payment from the company that is not on an arm's-length basis. Merely being a director or an employee of a company does not deem

an individual (or an associate of the individual) to be connected to the company.

In addition, an individual will be connected to a company if he or she owns (or is entitled to acquire) more than 30% of:

- › the issued share capital of the company,
- › the loan capital and issued share capital of the company,
- › the voting power of the company

or would be entitled to 30% or more of the company's assets in the event of a winding-up.

An individual will also be connected with a company if he or she has control of the company within the meaning of s11 TCA 1997.

Where an individual subscribes for shares in a company with which the individual is not connected and he or she subscribes for the shares as part of any arrangement that provides for another individual to subscribe for shares in another company with which the individual is connected, that individual will be deemed to be connected to the company.

However, an individual will not be deemed to be connected with a company (as above) if, within the period of two years before the date on which the eligible shares are issued (or, if later, the date of incorporation of the company) and three years after the date of the issue of the shares the aggregate of all amounts subscribed for the issued share capital and loan capital of the company does not exceed €500,000

It is important to note that if an individual making an investment in eligible shares at a time when he or she is not connected with the company, the relief will not be withdrawn if the individual subsequently becomes connected with the company.

Withdrawal of relief

There are a number of situations where the relief may be withdrawn, including where the individual disposes of the shares within the specified period. If before three years after the shares are issued an individual disposes of the shares otherwise than by means of a bargain made at arm's length, the individual will not be entitled to any relief in respect of those shares. In any other case, relief in respect of the shares will be reduced by the amount or value of the consideration that the individual receives for those shares.

In addition, where an individual enters into an option or agreement to dispose of the eligible shares at a price other than market value, the individual shall not be entitled to any relief in respect of the shares.

There may also be a withdrawal of the relief where the individual receives value from the company. If within two years before the issue of the shares (or the date of incorporation of the company, if later) or three years after the issue of the shares an individual receives value from the company, the relief to which the individual was entitled in respect of those shares shall be reduced by the value received from the company. There are a number of situations where an individual will be deemed to have received value from a company. These include (but are not restricted to) where the company:

- › repays, redeems or repurchases any of its share capital or securities that belong to the individual or makes a payment to the individual for giving up his or her rights to same,
- › forgives any liability owing to it by the individual or discharges (or undertakes to discharge) any liability of the individual to a third person,
- › makes a loan or advance to the individual or
- › transfers assets to the individual for no consideration or for consideration that is below market value or acquires an asset from the individual for a consideration that exceeds market value.

Qualifying Companies

In order for a company's shares to qualify for the relief, a number of conditions must be satisfied.

The company must carry on relevant trading activities. The scheme is now open to trades generally, as opposed to under the BES, where the qualifying trades were limited to certain activities including manufacturing, IDA- or Údarás na Gaeltachta-approved services, tourist traffic undertakings, shipping, certain R&D activities, horticulture, music recording and recycling.

However companies carrying on the following cannot qualify for the EIS:

- › dealing in commodities or futures or in shares, securities or other financial assets,
- › financing activities,

- › professional services,
- › dealing in or developing land,
- › occupying woodlands,
- › operating or managing nursing homes or residential care homes,
- › coal, steel or shipping activities,
- › operating or managing hotels, guesthouses, self-catering accommodation etc. (however, certain tourist traffic undertakings will qualify).

In addition, a company must satisfy a number of other conditions in order to qualify for the EIS.

- › The company must be incorporated in the State or in another EEA State.
- › The company, throughout the three-year relevant period, must be an unquoted company that is resident in the State or in another EEA State and must carry on a business in the State through a branch or agency.
- › The company must:
 - › exist wholly for the purpose of carrying on relevant trading activities principally in the State, or
 - › carry on a business that consists wholly of the holding of shares or securities or the making of loans to one or more qualifying subsidiaries, or
 - › carry on a business that consists of both the holding of such shares or securities or the making of such loans and the carrying on of relevant trading activities principally in the State.
- › The company must also be a micro-, small or medium-sized enterprise. The micro- and small enterprises can be located anywhere in Ireland, whereas the medium-sized enterprises must be located in an "Assisted Area" (all areas in Ireland excluding Counties Dublin, Meath, Kildare and Wicklow and Cork city, except for Cork City Docklands). An exception to this is a medium-sized enterprise that is at a stage of development not beyond start-up. Such a medium-sized enterprise can be located anywhere in the State.

	Micro- enterprise	Small enterprise	Medium- sized enterprise
No. of employees	<10	<50	<250
Annual turnover	<€2m	<€10m	<€50m
Annual balance sheet	<€2m	<€10m	<€43m
Location	Anywhere in Ireland	Anywhere in Ireland	“Assisted Area” unless a start-up

Limit on amounts raised

The maximum amount that a company, including any of its associated companies (see below), can raise through the issue of eligible shares during its lifetime is €10m, and the maximum that a company (including any of its associates) can raise through the issue of eligible shares in a 12-month period is €2.5m.

Where the amount received by a company exceeds the €10m limit, the available relief shall be divided between the qualifying individuals in proportion to the amounts that have been subscribed by them for the shares to which their claims relate.

Two companies will be associated with each other if it can reasonably be considered that:

- › both companies are in pursuit of a common purpose,
- › any person or group(s) of persons having a reasonable commonality of identity have or had the means or power, either directly or indirectly, to determine the trading activities carried on by both companies or
- › both companies are under the control of any person or group of persons having a commonality of identity.

Subsidiaries

A qualifying company may, in the relevant period, have one or more subsidiaries provided that the subsidiary is unquoted, is resident

in the State and carries on one or more relevant trades (as detailed above) or the subsidiary exists solely for the purpose of carrying on a trade consisting of the following activities:

- › the purchase of goods or materials for use by the qualifying company or its subsidiaries,
- › the sale of goods or materials produced by the qualifying company or its subsidiaries, or
- › the rendering of services to or on behalf of the qualifying company or its subsidiaries.

In addition:

- › the subsidiary must be a 51% subsidiary of the qualifying company;
- › no other person has control of the subsidiary in accordance with s11 TCA 1997; and
- › no arrangements are in existence whereby the above two conditions would cease.

Summary

The new EIS is a very welcome relief, and its application to a broader number of companies will make it very attractive to both investors and qualifying companies. The scheme is focused on the creation of employment and the carrying out of R&D activities. It is less restrictive than the BES as it is now open to most trades, and thus many trading companies should qualify. In addition, the amount that a company can raise during its lifetime has been greatly increased from €2.5m under the BES to €10m under the new EIS. However, the scheme is treated as a specified relief, which may discourage certain individuals from investing in qualifying companies. It is important to note that introduction of the scheme is subject to EU approval and a commencement order from the Minister for Finance. In addition, the scheme, as set out in Finance Act 2011, comes to an end on 31 December 2013 unless extended.