
**The Seed Enterprise Investment
Scheme (SEIS): Qualitative
research to explore accessibility,
customer experience and
implementation of the scheme.**

A report prepared by

PACEC

for
HMRC

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Glossary of Terms

Business angels: Individuals, and their syndicates, who provide venture capital by usually investing in early stage and smaller businesses

CAQDAS: Computer-Aided Qualitative Data Analysis Software. A system for organising and analysing qualitative information such as interview transcripts

CGT: Capital Gains Tax

Chartered Institute of Taxation: A professional organisation for accountants and tax advisers

CPD: Continuing Professional Development.

EIS: The Enterprise Investment Scheme for investors and businesses (HMRC)

Equity funding: Finance invested in the shares of a business.

Fame: Originally “Financial Analysis Made Easy”, an external database of company accounting information drawn from Companies House

HMRC: Her Majesty’s Revenue and Customs

ICT: Information and Communication Technology, an abbreviation for the computing and telecoms sector

IP: Intellectual property

Mezzanine finance: A combination of debt and equity finance provided by investors

PACEC: Public and Corporate Economic Consultants Ltd

R&D: Research and Development to explore, and test the feasibility of, for example, new technologies, processes, and products and services

SCEC: Small Companies Enterprise Centre

SEIS: The Seed Enterprise Investment Scheme

VC finance: Venture capital, usually invested in new small or medium sized businesses for equity where the risks are relatively high

VCT: The Venture Capital Trust scheme for investors and businesses (HMRC)

Executive Summary

I Introduction

- I.i In January 2013 HMRC appointed PACEC to carry out research on the Seed Enterprise Investment Scheme (SEIS). The primary aims were to assess, in summary: the early operation and implementation of SEIS; the accessibility of the scheme; awareness of SEIS; how it is communicated to potential users; investment behaviour and whether businesses have sought funding from other sources; and the links between the parties involved in applying for SEIS. The research also sought to provide insights into the participants' aims when they applied for SEIS and the impact of SEIS.
- I.ii The focus of the research was on those who applied to SEIS and were involved in the first few months of the operation of the scheme, from the autumn of 2012 to the end of the calendar year. They may not be typical of those who have applied to the scheme since then.
- I.iii The research covers the following:
- Enterprises who applied to SEIS
 - Investors using SEIS
 - Agents involved in helping to make SEIS applications
 - And eligible enterprises who did not apply to SEIS.
- I.iv Announced by the Government at Budget 2011 and enacted in the Finance Act 2012, with applications first accepted in September 2012, SEIS is designed to help small, early stage UK companies raise finance up to £150,000. Tax relief is available for investments made on or after 6 April 2012.
- I.v SEIS applies to small, start-up companies, specifically those with fewer than 25 employees and assets of up to £200,000, or those who are already trading or seeking to start a new business in eligible trades and sectors.
- I.vi The incentive provided by SEIS is to investors who can invest up to £100,000 per tax year, i.e. income tax relief worth 50 per cent of the amount invested and Capital Gains Tax relief.

II The Methodology and Interview Programme

- II.i The methodology for the study involved a full briefing with the Her Majesty's Revenue & Customs (HMRC) Steering Group, a desk study of relevant reports, and sixty one qualitative in-depth interviews with a representative selection of participants including sixteen agents/intermediaries, fifteen SEIS enterprises, fourteen SEIS investors and sixteen eligible businesses who had not participated in SEIS. Analysis of the results

was facilitated by using transcripts of the interviews and appropriate computer-aided qualitative data analysis software (CAQDAS).

III The Profile of Early Participants in SEIS

III.i In the first few months of the SEIS scheme up to the end of the calendar year 2012 some nineteen agents (mainly accountants) had participated in the scheme along with sixty-four companies and two hundred and fifty-nine investors. The participants were mainly located in London and the South East with a smaller number in the North West (mainly around Manchester). The main characteristics of those involved in early stages of the scheme was as follows:

- the accountants were usually small to medium-sized practices mainly based in London and the South East or in the Manchester area;
- the SEIS enterprises were reasonably innovative, in that the interviews with them indicated that in the main they had undertaken research and development (R&D) and introduced new products and processes in the twelve months prior to the interviews. Some had introduced new processes but very few had registered intellectual (IP) or patents. The main sectors were in online services for retailing, creative industries or software development;
- the investors were mainly self-employed or retired and had made relatively few investments in businesses (in contrast to business angels who usually make several investments).

These applicants may not be typical of those who applied for SEIS after the end of the calendar year 2012.

IV The Implementation of SEIS and the Application Process

IV.i The participants in SEIS said that most features of the application process, and the information available to them, were generally helpful and useful. The features they highlighted were the application form itself and the associated guidance notes. These positive points were also made about the advance assurance facility, which allowed them to check the eligibility of businesses for SEIS with HMRC prior to a full application. Generally SEIS participants did say that they had experienced a delay between when they were aware of SEIS and when they could apply.

IV.ii By and large, the accountants, in particular, were familiar with other “similar” Government schemes, especially the Enterprise Investment Scheme (EIS), and considered that the SEIS application process, if anything, was slightly simpler.

V SEIS Awareness and Communication

- V.i The SEIS enterprises had generally heard about the scheme through their accountants who were then sometimes involved in making the SEIS applications (both for the advance assurance stage and the full application).
- V.ii There were some differences in the way enterprises, agents and investors had heard about SEIS and how they preferred to be alerted to Government schemes.
- The SEIS enterprises, having heard through their accountants, generally preferred to be alerted to schemes via direct email contact from them (with the inclusion of newsletters).
 - Participating agents had primarily been alerted to SEIS through the Government's budget statement or by the financial press and HMRC website and preferred these means to allow them to be aware of schemes.
 - On the whole, the investors first heard about SEIS via their accountants (through emails and newsletters) and had a preference for this method along with direct emails and newsletters. Some were alerted to SEIS by the business they invested in.
- V.iii The non-SEIS enterprises interviewed were in the vast majority of cases not aware of SEIS. Their preference for being alerted to SEIS and other Government schemes in general was by direct e-mail alerts.

VI Sources of Finance Used by Enterprises

- VI.i On the whole the SEIS enterprises considered that equity funding was more appropriate than debt funding to support their growth activities. Underpinning this, those interviewed were growth orientated and some aimed to achieve significant growth. They were also relatively innovative with a focus on the enhancement of existing products and services and the development of new ones in conjunction with some research and development (R&D), primarily to test feasibility options.
- VI.ii Generally, SEIS enterprises said they had not sought alternative finance to SEIS. Where they had, a minority had sought a bank loan and/or in a few cases business angel or Venture Capital [VC] finance. Some had also approached family and friends. However, the feedback given was that the prospect of being able to obtain a bank loan of a size equivalent to their SEIS investment, or for a lesser amount, was unlikely, primarily as they were very new businesses. Those enterprises that had been offered a bank loan tended not to have taken it up because of the unacceptable conditions attached and the guarantees and securities required.
- VI.iii Mainly, the SEIS enterprises said they preferred equity funding as (in spite of a dilution in their equity holding) it did not have to be "serviced" or repaid as debt finance did. It also tended to be more substantial and provided both day to day

operational and growth/investment finance. Investors could also give useful business advice when they provided equity funding as they had a stake in the business.

VII The Reasons for Participating in SEIS

- VII.i Generally the aims of agents for participating in SEIS were to continue to offer a service for existing business clients with the anticipation of future fees as the businesses grow. For them, SEIS was a suitable investment vehicle given the early stage the SEIS businesses were at and the limited prospects they had of raising finance from elsewhere.
- VII.ii For the SEIS enterprises the main reason for applying to SEIS was to obtain investment finance to allow their businesses to consolidate and grow. By and large they sought to develop their existing and new products and services. A specific financial objective was to obtain equity funds as opposed to debt funding as equity finance, unlike debt, did not have to be repaid, or serviced through charges and interest rate payments.
- VII.iii The main aims of investors for participating in SEIS were to take advantage of the front end tax relief, in particular, that SEIS offered and the Capital Gains Tax (CGT) exemptions from the likely gains in the share value of their SEIS investments as the businesses grew and increased their profitability. Generally the investors also knew the directors of the businesses prior to investing via SEIS and they were attracted to the business ideas. Some may have invested in the business without SEIS but generally they would have invested less.

VIII Links Between Agents, SEIS Enterprises, and Investors

- VIII.i For early applicants in the SEIS application process the strongest links were between the agents and the SEIS enterprises on the one hand and the SEIS businesses and the investors on the other. The links between the agents and the investors were generally relatively weak and the two parties were normally introduced to one another through the SEIS enterprises.
- VIII.ii The agents tended to play an important role in making the businesses aware of the SEIS opportunity, persuading the businesses to make an application and organising it for them.
- VIII.iii The agents generally said that they influenced the enterprises' decisions to apply for SEIS through their discussions with them. The SEIS enterprises generally shared this view. They maintained that they usually made the decision to use SEIS to obtain investment and/or worked with their accountant/adviser to reach it. The investors made their decision to invest and apply for SEIS usually in conjunction with the SEIS enterprise and in some cases also in liaison with the accountants.

IX Agent and Investor Behaviour in Relation to Investment

- IX.i In terms of the criteria that agents usually used to identify businesses for potential investment, the focus was on the growth potential of businesses. In general, the agents already knew the SEIS businesses, who by and large were growth businesses and who met the SEIS eligibility criteria. If they sought to identify businesses to invest in they would mainly liaise with their business contacts, review their existing portfolio, and work with business networks.
- IX.ii It was commonplace for the agents to be involved in other Government schemes (especially EIS). In general, they thought that SEIS played a different role in encouraging start-up / early stage investments while EIS could be used for later stage investments.
- IX.iii The criteria investors would use to identify and select a business to invest in were the growth potential, the management team / directors, the value of assets, the opportunity to sell shares and ultimately the ability to exit the business with a reasonable return.
- IX.iv Overwhelmingly the SEIS investors used the scheme because they sought to take advantage of the front end tax relief and the CGT exemptions, and in particular the likely gains in the share value of their SEIS business on disposal of the shares.

X The Impacts that Result from SEIS

- X.i The SEIS enterprises said they had become more favourably inclined to equity funding as a result of SEIS. Equity finance, unlike debt, did not have to be repaid, or serviced through charges and interest rate payments. The agents shared this view.
- X.ii In the view of agents and investors, SEIS had encouraged some investors to be more inclined to equity funding (compared to other investments) which had resulted in a small change to the investment landscape nationally for businesses seeking external funds. The agents and investors considered that seed enterprises' options for gathering larger amounts of growth funding had generally been restricted to banks, business angels, and venture capital funds.
- X.iii Based on the views of SEIS enterprises, the SEIS programme also had some initial impacts on business outputs, such as the ability to recruit people with appropriate skills and purchase equipment, and outcomes, for example, increased turnover. The initial aims of businesses had been to attract funding, consolidate, and grow their businesses as well as developing new products and services. Overall participating businesses said these aims had been wholly satisfied. The investments had consolidated the start-up phase and resulted in early growth for most. Generally, the investments met a funding gap, and improved cash flow and working capital. Others said they had recruited key staff with appropriate skills and strengthened their innovation activities. Existing products and services were refined and developed, the feasibility of ideas tested, and new products and services developed. For some

businesses there had been consequent increases either in turnover, profit margins, and the value of business assets.

- X.iv The SEIS enterprises and their agents considered that by and large the investment they received and the subsequent outputs and outcomes for businesses were unlikely to have occurred without the SEIS scheme. They felt they would not have been able to raise the funding necessary from elsewhere, especially as they did not obtain funding from banks where they tried, or believed they would not be able to.
- X.v Generally, some of the investors thought they would have funded the SEIS enterprises to some extent without SEIS, but possibly not to the same degree. Some funding would have been provided mainly because the investors knew the owners/directors of the enterprises, they liked the business idea(s), and the businesses were often trading in a sector the investors had experience in. Their SEIS investment was not likely to mean that they would not make investments in other businesses but the amount could be smaller.

XI The Views of Non-SEIS Enterprises

- XI.i The level of awareness of SEIS among non-SEIS enterprises was very low, with only a small number of the interviewees expressing any knowledge of the scheme at all. The few respondents who claimed some awareness of SEIS were asked how they became aware of it. However, they could not recall how they were alerted to the scheme.
- XI.ii Notwithstanding the low level of awareness of SEIS among these enterprises, many of the interviewees thought, nevertheless, that they would be encouraged to take part in Government schemes which provided investment finance, if they were offered the right type of finance with appropriate conditions. Grants were the most attractive form of finance for them as grants did not have to be repaid. Grants were more attractive than loans or equity funding.
- XI.iii Generally the interviewees considered that emails were the most useful way to alert them to new Government initiatives and provide them with information about schemes that are available. However, some also suggested that television promotion and, to some extent, letters and newsletters would be an appropriate means of communicating with them.
- XI.iv On the whole, the non-SEIS enterprises said they were using only a narrow range of sources of finance to support their business. The main ones were the sales and turnover of the business and their own personal savings. On the whole, very few of these enterprises indicated they were likely to consider making a SEIS application in the future as they were not looking for external finance.

1 Introduction

1.1 Introduction

1.1.1 In January 2013 HMRC appointed PACEC to carry out research on the Seed Enterprise Investment Scheme (SEIS). The primary aims were to assess a series of linked issues. In summary, and reflecting the tender brief, they were: the early operation and implementation of SEIS; the accessibility of the scheme, the awareness of SEIS, how it was communicated to potential users; investment behaviour and whether businesses had sought alternative funding, and the links between the SEIS enterprises, investors, and agents when they applied for SEIS. The research also sought to explore the aims of participants when they applied for SEIS and the impact of SEIS on enterprises and investors.

1.1.2 The focus was on those who applied to SEIS and were involved in the first few months of the operation of the scheme, from the autumn of 2012 to the year end. These applicants may not be typical of those who have applied to the scheme since then.

1.2 Background

1.2.1 In the current economic climate, there is a particular policy emphasis on providing stimulus for the UK's small and medium enterprises (SMEs). To address this, the Government announced in the Budget of 2011 that it would bring forward proposals to support investment in smaller, early stage companies. The inclusion of SEIS in the Finance Act 2012 was part of this support.

1.2.2 SEIS was enacted in Finance Act 2012, with tax relief available for investments made on or after 6 April 2012. Application forms were available from September 2012. It was designed to help small, early stage UK companies raise finance of up to £150,000 by offering tax relief to investors. A sister scheme to the Enterprise Investment Scheme (EIS), SEIS differs in its exclusive targeting of start-up companies whose trades are no more than two years old. The SEIS scheme targets these 'seed' enterprises because investors often perceive them to be the riskiest small businesses, and therefore these companies may not receive as much investment as 'larger' small businesses. SEIS complements the existing Enterprise Investment Scheme (EIS), in recognition of the particular difficulties which very early stage companies face in attracting investment, by offering tax relief at a higher rate than that offered by the existing EIS.¹

1.2.3 SEIS applies to small, start-up companies, specifically those with fewer than 25 employees and assets of up to £200,000, or those who are trading or seeking to start a new business in eligible trades or sectors. Key players involved in the SEIS scheme are:

¹ See <http://www.hmrc.gov.uk/seedeis/background.htm>

- Small UK start-up companies who seek investment;
- Investors who take advantage of the tax relief; and
- Agents/intermediaries who may act as a link between the two above groups.

1.2.4 The incentive provided by SEIS is to investors, who can invest up to £100,000 per tax year under the scheme. Specifically, it provides income tax relief worth 50 per cent of the amount invested and Capital Gains Tax (CGT) relief to individual investors with a stake of not more than 30 per cent in such companies, including company directors.

1.2.5 The investors cannot claim their relief until HMRC has first agreed that the company and the investment meet all the qualifying conditions. The company first applies to HMRC; if its application is approved then HMRC authorises it to issue claims forms to its investors. HMRC also operates a non-statutory advance assurance facility which allows companies to give it information in advance of a share issue, about their trade, structure, and eligibility for SEIS, etc. HMRC will then give them a view as to whether it is likely to qualify, so they can provide a degree of comfort to prospective investors. SEIS is administered by two small specialist offices in Cardiff and Maidstone, the Small Companies Enterprise Centre (SCEC). Investor claims are not handled by the SCEC, but by the investors' own tax offices.

1.3 The Research Aims

1.3.1 Through commissioning the research, HMRC sought to extend its knowledge in the key areas shown below. The results will have implications for policy and how SEIS, as a relatively new scheme, is delivered going forward.

- **Operational assessment and applying for SEIS** (including the advance assurance process, documentation, application form and areas for improvement).
- **Awareness of SEIS and communications** (including how businesses, investors and agents first heard about SEIS and their preferred means of communication).
- **Sources of finance used by enterprises** (including whether SEIS enterprises had applied for other sources of funding and their attitudes towards different funding types).
- **Reasons for participating in SEIS** (including the growth ambitions and innovation activities of firms and what investors were looking to achieve).
- **Links between investors, intermediaries and seed enterprises** (including the role of intermediaries in linking investors with seed companies; what links existed prior to and following applications; and influences on the decision to apply for SEIS funding).

- **Investor and agent behaviour in relation to investment** (including how investors and agents select seed enterprises to invest in; the role of SEIS in their investment decisions; and the position of SEIS relative to other schemes in the investment landscape).
- **Awareness of SEIS among non-participating start-ups.**

1.3.2 These questions were central to the methodology used for the research which is set out in the next chapter.

2 The Methodology and Interview Programme

2.1 Methodology

- 2.1.1 There were a number of interrelated steps taken to explore the research issues.
- 2.1.2 At the outset a full briefing was held with HMRC to gain further insights into the SEIS scheme and how it had been delivered. This was followed by a desk study of relevant background information and reports as well as a review of the management information held by HMRC. This showed the characteristics of the participants in SEIS (i.e. the agents, investors, and SEIS enterprises who had successfully made applications).
- 2.1.3 In order to meet the aims of the project the main method used was qualitative interviews with participants in the scheme using a discussion guide. Participants were defined as:
- a The agents or intermediaries (such as accountants) who submitted applications on behalf of companies and investors for SEIS to HMRC
 - b The companies who participated in SEIS following their successful applications, i.e. SEIS enterprises
 - c The investors who invested in SEIS enterprises.
- 2.1.4 Interviews took place with participants who applied to SEIS in the first few months of the scheme from September 2012 up to the end of the 2012 calendar year. These participants may not be typical of those who applied since then.
- 2.1.5 In addition, qualitative interviews were held with other companies who had not applied to SEIS. They were “similar” to SEIS enterprises in that they met the eligibility criteria for the scheme in terms of, for example, their size, period of trading, or were similar in their trades (and industrial sectors), their partnerships, subsidiaries, and whether they had used other schemes. Some filter questions were used at the outset of the interview to ensure they were eligible for SEIS.
- 2.1.6 The interviews were held through a combination of face to face and in-depth telephone methods. The topics were sent in advance to the participants along with letters from HMRC and PACEC outlining the purpose of the study. Each interview followed the discussion guide and was recorded (where there was agreement with the participants) and a transcript produced. The analysis was carried out by careful examination of the interview transcripts, and listening to the recordings of interviews for patterns and commonly-held views, facilitated by appropriate use of computer-aided qualitative data analysis software (CAQDAS). There were telephone follow-ups with some interviewees to clarify some of their answers.
- 2.1.7 The contact information for all the interviews was provided on a confidential basis to PACEC by HMRC. It comprised the names, addresses, telephone numbers (where possible), and geographic location by city and county in the UK, as well as information on gender of the named contacts HMRC provided and the sector or trade

of businesses. It covered applications to SEIS in the first few months from first receipt of applications, i.e. from September 2012 onwards. Applicants were either agents or businesses and in a few cases investors acting for the businesses. The contact information provided sampling frames for the initial applicants from whom a sample was selected which captured the diversity of applicants. This helped ensure a good spread of interviews. The number of contacts provided by HMRC and the interviews achieved are shown below:

Table 2.1 Interviews achieved

Interviewee Group	Achieved Interviews	Face-to-face/ teledepths
Agents/intermediaries	16	5/11
SEIS Businesses	15	4/11
SEIS Investors	14	4/10
Non-SEIS applicants	16	-/16
<i>Total</i>	<i>61</i>	

Source: PACEC

2.1.8 In total there were sixty one interviews. Almost a third of interviews with SEIS participants were carried out face to face and the rest by telephone. The interviews ranged from an average of approximately 45 minutes (with agents) to fifteen to twenty minutes (with non-SEIS applicants). There were some ten to twelve follow-up discussions to clarify some of the comments made in the initial interviews.

2.1.9 The number of contacts for agents provided by HMRC was relatively small (i.e. 19). Hence PACEC used a “snowballing” approach to gain further potential contacts to interview from the agents and companies interviewed.

2.2 Characteristics of the Interviewees

- a Agents/Intermediaries: mainly small to medium sized accountancy firms who provided investment advice to businesses and individual investors. The majority were based in London and the South East with a smaller number around Manchester. Most of their business clients were start-ups, sole traders, and SMEs (reflecting the national business population). Generally they did not specialise in specific sectors. Where they did, the sectors included creative industries and information/communication technology businesses. The investors they usually acted for tended to be small investors (with few investments) although there were some high net worth individuals who were business angels (with more and larger investments).

In terms of SEIS applications, generally the agents had submitted between two and three (with a few submitting more than five). A small number of agents had more applications “in the pipeline”, and for two of these agents up to fifteen. Most applications were made in the autumn of 2012.

- b SEIS Enterprises: mainly start-up and micro companies with fewer than five employees who were independent businesses trading for less than two years. They tended to be located in London and the South East or the North West, in the Manchester area (as with the agents). The aims of the companies were generally to grow rapidly with some seeking to grow moderately. The businesses were, on the whole, reasonably innovative companies and had carried out R&D and introduced new products and services (just prior to applying for SEIS or since then). The main sectors were online services for retailing and creative industries including graphics and film, advertising and software.

Most of the SEIS applications had been made in late 2012. The median investment was £60,000, in the range of £25,000 to £150,000.

- c The Investors: They were usually resident in London and the South East or the North West (as with agents and SEIS enterprises). They were predominantly men over fifty years of age. They were self-employed, retired, or employees in that order. They had invested in the SEIS businesses at the end of 2012 when some of the businesses were no more than a few months old.

The investors in SEIS were generally individuals who made relatively few investments (rather than business angels), and some were relatively high net worth individuals.

They considered that the aim of the businesses they invested in was to grow either rapidly or moderately. They were thought to be innovative companies in that around half had carried out R&D and had introduced new products or services, or intended to. The latter was a key stimulant for their investments.

The range of investment was £7,000 to £100,000 with a median of £25,000.

Most investors had some form of involvement with the businesses as non executive directors or advisers (in some way). Others had little involvement although in some cases they knew the directors of the businesses quite well.

- d Non-SEIS Enterprises. These businesses were generally micro and small firms trading for less than 2 years and located across Great Britain but primarily in London and the South East and the Midlands/North West (reflecting the national distribution of businesses in Great Britain). The growth aims of these businesses were largely to stay the same size, and very few sought to grow more than moderately. They tended to be less innovative than the SEIS enterprises, did not carry out R&D, and a minority had introduced new products or processes in the last twelve months prior to the interview.

2.2.2 The discussion guide topics used for the interviews are shown in Appendix A.

- 2.2.3 The analysis which follows focuses on the expertise of the interviewees in terms of their involvement in SEIS and their views on the scheme. The results for agents, SEIS enterprises and investors are grouped together in Chapters 4 to 9 as they usually liaised with one another to make the SEIS applications. For non-SEIS enterprises the main issue explored was whether they had heard of SEIS and what the best ways were of advising them on Government schemes. See Chapter 10.

3 The Profile of Early Participants in SEIS

3.1 Introduction

3.1.1 This chapter summarises the profile of those involved in making SEIS applications between the start of the scheme and the end of the 2012 calendar year. As HMRC provided PACEC with information on all these early SEIS ‘participants’, the purpose of this chapter is to describe the overall characteristics of this group rather than just those interviewed as part of this study. It covers:

- Agents involved in early SEIS applications
- Early SEIS enterprises
- Early SEIS investors
- Early SEIS-eligible companies

3.1.2 These applications may not be typical of those who applied following the first few months of SEIS up to the end of 2012.

3.2 Agents

3.2.1 The HMRC contact list included information on 19 agents involved in SEIS applications. The agents were typically accountancy and financial services firms. They were located primarily in London and the South East and around the Manchester area, as set out in full in Table 3.1 below.

Table 3.1 Agents by location

	Agents	
	Number of agents	Percentage of total
(unknown)	1	5%
East Midlands	0	0%
East of England	1	5%
London	3	16%
North East England	1	5%
North West England	4	21%
Scotland	0	0%
South East England	6	32%
South West England	1	5%
Wales	0	0%
West Midlands	1	5%
Yorkshire and the Humber	1	5%
<i>Grand Total</i>	<i>19</i>	<i>100%</i>

Source: HMRC, PACEC

3.2.2 In the course of the interviews with SEIS companies and investors, PACEC was given contact details for more agents. Their characteristics were similar to those on the HMRC list, i.e. accountants mainly in London and the South East.

3.3 SEIS enterprises

3.3.1 The HMRC contact list included 64 companies. The information provided with the companies included the following:

- Company name, address, and contact details
- Details of trade (descriptive text)
- Information from registered accounts – on turnover, assets, and profits, etc.
- The Standard Industrial Classification code

3.3.2 Address information was available for all businesses. It was provided by Government Office Region. The breakdown is shown below in Table 3.2. Half of the companies are located in London or South East England.

Table 3.2 Early SEIS enterprises by location

	SEIS companies	
	Number of companies	Percentage of total
(unknown)	1	
East Midlands	1	2%
East of England	6	9%
London	20	31%
North East England	3	5%
North West England	7	11%
Scotland	1	2%
South East England	13	20%
South West England	5	8%
Wales	-	-
West Midlands	3	5%
Yorkshire and the Humber	4	6%
<i>Grand Total</i>	<i>64</i>	<i>100%</i>

Source: HMRC, PACEC

3.4 Investors

3.4.1 The SEIS information provided by HMRC contained at least one investor for each of the 64 companies above. The number of investors per company varied considerably, from just one (in 21 cases) to as many as 17 (in 2 cases). In total, the early applications to the SEIS provided 259 investors contacts.

3.4.2 The HMRC information derived from the application form was limited to name and address only. The investors were characterised by Government Office Region in the

same way as the SEIS companies (see Table 3.3 below). Just as was found to be the case with the SEIS companies, there is a strong bias towards London and the South East; 58% of early investors were to be found in these two regions, with 13% in the North West (around the Manchester area).

Table 3.3 Early SEIS investors by location

	SEIS investors	
	Number of investors	Percentage of total
(unknown)	1	
East Midlands	9	3%
East of England	9	3%
London	79	31%
North East England	10	4%
North West England	34	13%
Scotland	7	3%
South East England	70	27%
South West England	14	5%
Wales	2	1%
West Midlands	10	4%
Yorkshire and the Humber	15	6%
<i>Grand Total</i>	259	100%

Source: HMRC, PACEC

3.5 SEIS-eligible businesses

- 3.5.1 HMRC provided contact details for 385 companies which were likely to be eligible for SEIS, based on data from HMRC's internal corporation tax database and Fame (originally Financial Analysis Made Easy), an external database of UK and Irish company accounts.
- 3.5.2 A set of filter questions was used at the start of the interview to ensure these companies were eligible for SEIS investments, as not all the eligibility criteria could be applied in the HMRC list provided. The filter questions were designed to match the eligibility criteria and included: for example the period of trading, size and age, whether companies were a member of a partnership, whether they had control of other companies which were not qualifying subsidiaries, and involvement in other schemes.
- 3.5.3 The HMRC data by industry were not available for all companies, and the classification scheme used (Trade Classification Number) was viewed as potentially not robust enough for classification. The data showed companies by region in the same manner as the SEIS companies and investors. Although there were only a small number of early SEIS applicants, the early indicators suggest a greater proportion of early applicants from London and the South East than the overall profile

of potentially eligible companies and fewer from the East Midlands, Scotland, and Wales. See Table 3.4.

Table 3.4 Comparison of SEIS and non-SEIS samples

	Company details				
	SEIS		Non-SEIS		SEIS/ Non-SEIS ratio
	No	%	No	%	
(unknown)	1		3		-
East Midlands	1	2%	27	7%	0.22
East of England	6	9%	38	10%	0.95
London	20	31%	88	23%	1.37
North East England	3	5%	8	2%	2.26
North West England	7	11%	53	14%	0.79
Scotland	1	2%	20	5%	0.30
South East England	13	20%	57	15%	1.37
South West England	5	8%	25	6%	1.20
Wales	-	-	13	3%	0.00
West Midlands	3	5%	27	7%	0.67
Yorkshire and the Humber	4	6%	26	7%	0.93
<i>Total</i>	<i>64</i>	<i>100%</i>	<i>385</i>	<i>100%</i>	<i>1.00</i>

Source: HMRC, PACEC

4 Awareness of SEIS and Communication

4.1 Introduction

4.1.1 This chapter describes how the early applicants became aware of SEIS. However, their views may not be typical of other businesses that have applied to SEIS since the end of 2012 or the wider population of firms.

4.1.2 The research questions also covered how participants preferred to be alerted to Government schemes (similar to SEIS) and whether these methods reflected those that alerted them to SEIS. The views of the agents, SEIS enterprises, and the investors are reported on separately below with similar, or different, views and findings drawn out where appropriate.

4.2 The Agents/Intermediaries

4.2.1 The majority of agents (mainly accountants and tax advisers, with some solicitors) had been alerted to SEIS by the budget statement of April 2011, together with subsequent coverage in the financial press. Further information was provided relatively quickly through the professional bodies and their newsletters as e-mails and training organisations that agents used for continuing professional development. Some of the accountants provided summaries and updates of the budget details soon after the statement, and circulated them to their clients (i.e. businesses and investors).

4.2.2 It was noted that agents referred to SEIS in different ways, i.e. mainly the full name of the scheme, the SEIS acronym, or the “seed scheme”. Some of the views expressed on how agents heard of SEIS were:–

- *“Well it was probably through the budget. I am pretty sure it was that... the budget announcement and you thought ‘hang on what’s going on here - that sounds a bit interesting’ and then we followed it up.”* (Agent)
- *“We are a member of the Institute of Chartered Accountants so... they will put out these things by e-mail – which is the best thing. Also the taxation/ accounting press will drop on to these things and of course anything that is coming out in the Budget we get. That is square in front of us.”* (Agent)

4.2.3 The SEIS agents generally sought further information following the budget announcement, primarily from HMRC by telephone or e-mail or via the HMRC website. However, the agents commented that although SEIS was announced to go ahead in March/April 2012, with some information on the HMRC website, it was not possible to apply until the autumn, which delayed the applications.

4.2.4 The majority of agents said they tended to follow the Government’s announcements very closely and on a regular basis to keep up with changes. They also had a

preference for direct electronic alerts from departments making the announcements. Hence this was their preferred means of being alerted to new schemes and changes and in particular the budget announcements which they often watched or listened to. In addition, for more detailed information on schemes they had a preference for newsletters and magazines from professional bodies (e.g. the Chartered Institute of Taxation) and the continuing professional development (CPD) and “training” organisations they used on a regular basis. The points made on the best ways to inform them were:–

- *“The best way is through email, and the budget announcements. Going to the HMRC website from there. Email is good. We knew the EIS scheme already, and we could see SEIS was an enhanced version, with very familiar requirements anyway. The best way to alert us is by e-mail.”* (Agent)
- *“Yes the professional bodies and professional press. I think the Revenue is much much better in the last two years about engaging accountants, if not entirely on their side or playing the same game.”* (Agent)

4.3 The SEIS Enterprises

4.3.1 The SEIS enterprises generally were made aware of SEIS through their accountants (who usually work with small businesses) who then went on to make the SEIS application. Some may have helped to set up the company, or they may have advised other businesses the SEIS directors were involved in. The enterprises had also been alerted, in their view, by the financial press at the time of the 2011 budget announcement and implementation in April 2012. A few of the enterprises mentioned friends/family and other businesses. The business comments on how they heard of SEIS were:–

- *“Through my accountant....HMRC could do a better job of alerting businesses with more publicity...I know because I am in the industry...if I was starting out I wouldn't know where to start looking...”* (SEIS enterprise)
- *“Through the accountant... that was the direct route... with a budget update newsletter.”* (SEIS enterprise)

4.3.2 Having been alerted to SEIS, the companies tended to follow up to obtain further information on how the scheme worked, their eligibility, the duration of the scheme, and any conditions associated with it. They usually followed up by contacting HMRC directly by telephone (or e-mail) and visiting the website or with their accountants (who subsequently advised on the SEIS application). A small number followed up on the original alert via their solicitor. A small number of enterprises did not seek further information when they made applications.

4.3.3 The SEIS enterprises preferred to be alerted to Government schemes by direct e-mail or via their advisers (usually their accountants), and newsletters. The advice required from their accountants was on the Budget, or Government policy updates. They did

not see the media (i.e. radio, television, or newspapers) as a primary means of alerting them. They considered the information provided by their advisers was usually more detailed and allowed them to gain a fuller understanding of schemes. The comments on the best ways to alert them to schemes were:

- *“Through my accountant... HMRC could do a better job of alerting businesses... I know because I am in the industry... if I was starting out I wouldn't know where to start looking.”* (SEIS enterprise)
- *“E-mail would be the best way, and in the financial press there are plenty of notifications.”* (SEIS enterprise)
- *“Generally by direct e-mail, but I would be aware of schemes through Government announcements. The two directors, myself, and some of the employees as well... so some of the directors and myself would be aware; we would know about them.”* (SEIS enterprise)

4.3.4 There was no indication that enterprises from different sectors, or locations, participating in the research favoured alternative ways of communication. The possible exception to this was that IT companies placed more emphasis on e-mail alerts.

4.4 The SEIS Investors

4.4.1 The SEIS investors most commonly first heard of SEIS through their accountants (via e-mails and newsletters), or the company they invested in via SEIS, followed by a family, friend, or business contact. Their comments were:

- *“A local accountant I talk to on a regular basis told me about it. They have an advisor working with the company who also has useful information, those are the best ways of finding out and doing it. I would always talk to a financial advisor before I did anything. If the Government tells the accounting profession, I can get the information from them... I use them on tax and other issues.”* (SEIS investor)
- *“Networks and friends is how we heard of SEIS and we were not aware of it at all until then. I wouldn't normally invest in something of this nature but by speaking to people and to some of the companies we already invested in, and the people we are linked with who all help... A very impressive lot. I thought I am going to look at investing in this... high risk stuff though.”* (SEIS investor)

4.4.2 The investors tended to follow up for further information, usually via their accountants or solicitors or by accessing the HMRC website. A small number of investors had not sought any follow up information. The SEIS investors preferred to be alerted to Government schemes via their advisers (usually accountants) coupled with e-mails, newsletters, or budget updates, and by the press (television, the radio, or

newspapers). Trade and professional magazines were not generally a preferred means. The comments on how to be alerted to Government schemes were:

- *“I heard it from the Chancellor last year in the Budget...I have inheritance tax issues, so it will help... a great, great advantage... the second thing is capital gains offset reduces risks...He stated that clearly, and it seemed a very sweet deal. So through the Budget is best.”* (SEIS investor)
- *“Alerting me to schemes? Accountants would be best... direct to me with their newsletters.”* (SEIS investor)

4.4.3 The results of the research on the extent to which the businesses who were not involved in SEIS were aware of the scheme are shown in Chapter 10 on Non SEIS Enterprises.

5 The Decision to Apply for SEIS

5.1 Introduction

5.1.1 The findings on how decisions were made to apply for SEIS potentially raise some policy issues for HMRC as to who to alert. The discussions with agents, the SEIS enterprises, and the investors examined how the decision was reached and who influenced or initiated the decision. They also covered the extent to which there were negotiations between the parties and conditions sought.

5.1.2 The chapter initially considers the views on the advance assurance facility for SEIS and then the participants' views on the full application process.

5.2 The Advance Assurance Facility

5.2.1 The advance assurance facility is an option provided by HMRC to allow investors to examine whether they were eligible for SEIS prior to a full application. The process was normally initiated on the advice of the agents and was used by them for three quarters of the applications. Around half of the agents thought it was a necessary condition for SEIS enterprises and investors before the full application went ahead. The businesses and investors also held this view. However, they were more likely to think that investment would have gone ahead anyway in some form, without the facility, compared to the agents. Overall the facility was considered to be useful and the assurance given allowed applications to be submitted with greater confidence.

5.3 The Agents

5.3.1 The agents took the view that by and large they influenced the decision, which was made ultimately by businesses, to apply for SEIS, primarily through their discussions with SEIS enterprises. Initially, the SEIS enterprises approached their accountants, usually with a potential investor in mind, that they knew, to discuss an investment. The agents then usually advised them that SEIS would be an appropriate vehicle for the company (to obtain the investment) and for the investor, in particular, to take advantage of the tax breaks. The comments made on the decision to apply for SEIS were:–

- *“Yes we acted for the company so ... we completed the forms... and made the submission to the Inland Revenue so we dealt with all of that side on behalf of the company and we completed the appropriate forms for the investors... for the companies to send on to the investors...”* (Agent)
- *“There was some connection with the business as clients, but we advised them to use SEIS. I suppose it is a joint decision... in the end.”* (Agent)

5.3.2 Generally the agents did not act as brokers to deal with any issues that arose between the SEIS enterprises and the investors, in the sense that they needed to be “deal makers”. However, the agents considered that there were some negotiations between some of the parties involved in the applications, but these were generally not deemed to be significant. When issues/negotiations arose, the SEIS enterprise and the investors were mainly involved without the agent. These issues usually covered the price and the number of shares, the role of other investors, intellectual property, changes to the business Articles, and employment contracts for staff in the businesses. The agent generally became involved in negotiations only on a few occasions. In some cases these issues were covered by conditions made by the investors but usually there were not formal written conditions reflected in agreements or, for example, company articles. One illustrative view expressed by an agent was:

- *“We advised the company, who knew the investor. No we didn’t act as a broker. There were no significant negotiations, not really.” (Agent)*

5.4 The SEIS Enterprises

5.4.1 The enterprises either used an agent to submit their SEIS applications or, in a small number of cases they made the applications themselves. Where an agent was used (usually an accountant) it was primarily because they liaised with the director of the company anyway on investment and taxation issues. Generally the fees charged for the application by agents were not large (in a range of £350 to £1,500) and they were usually more interested in the income and fees that would result from the ongoing business relationship as the companies became successful and grew.

5.4.2 The SEIS enterprises maintained they usually made the decision to use SEIS to obtain investment and/or worked with an accountant/adviser to reach it (which was by and large confirmed by the agents). The enterprises said they usually initiated the application procedure (in liaison with the investors) and in most cases the accountant submitted the application on behalf of the company. The businesses tended to know the investor through personal or business contacts. In one case the initial investor introduced them to several other investors. The views on the decision were:-

- *“It was the accountants because they alerted us to it. It was a joint decision with the accountants... to invest through SEIS at the time.” (SEIS enterprise)*
- *“We knew two or three investors. I suggested it to them I think and probably played a fair part, and introduced it through neutral contacts, to get up to the nine investors.” (SEIS enterprise)*

5.4.3 Generally, the enterprises said that no broker was required to agree the “deal” between them and the investors but where necessary the deal making could fall to the agent. The negotiations between the parties generally did not involve significant issues. There were few issues where there were substantially different views between the enterprises and investors and a compromise agreement was required. Where the need for compromise did occur, it was usually on the value of shares and the extent

of the shareholdings. Generally, the enterprises considered that the investors did not make formal conditions as such – if they did it was usually to use the assurance facility to provide “comfort” to the SEIS enterprise and the investor that the former was eligible for SEIS.

5.5 The Investors

5.5.1 The investors made their decision to invest and apply for SEIS usually in conjunction with the SEIS enterprise and in some cases also in liaison with agents. In many cases they already knew the SEIS enterprise. A small number of investors had made the application themselves on behalf of the enterprises (especially where they had made investments in other businesses and where they were already familiar with EIS). Generally, no broker was required, but in some cases the investors led the negotiations and could act as a broker along with other investors. The negotiations were not usually significant and would be led by the investor or the company without prior conditions being made, in the sense that specific terms had to be met. However, for some investors the advance assurance facility with HMRC was a prerequisite for their investment. Some views of investors on the decision to invest were as follows:

- *“That was taken care of....through the accountants and the company. They organised the HMRC documentation and the approval was made, and sorted out for me.”* (SEIS investor)
- *“The company accountant put the application in for everybody. Acted as broker? I am not aware of extensive negotiations. No it wasn’t laborious or heated at any point.”* (SEIS investor)

6 The Links Between Agents, Seed Enterprises, and Investors

6.1 Introduction

6.1.1 The extent of links between the parties prior to the SEIS application gives some indication of whether SEIS is helping to form new relationships and consolidating or strengthening links that already existed. The interviews with the parties sought to explore both two way links (between some types of parties) prior to the SEIS investment, and three way links in that all the parties (the agent, the SEIS enterprise, and the investor) knew one another. This chapter deals with the extent of these links and their nature.

6.2 The Extent of Links Between the Participants

6.2.1 In terms of the links between the agents and the SEIS enterprises the agent usually said that they knew the business director(s) as potential or existing clients and had liaised with, or given advice to, them. The enterprises agreed that they usually knew the agent prior to the SEIS application. The agents considered that the directors usually knew the investor(s) prior to the SEIS application. In a small number of cases the agent knew both the business and the investor. On a few occasions the businesses that the agents knew were also looking for an investor(s) to put money into the business. There tended to be very few businesses that were “new” to the agent at the time of the SEIS application process. Hence the application process tended to help consolidate/ existing links between the agents and enterprises and the enterprises and investors.

6.2.2 If the businesses did not know of an investor (which was in a limited number of cases) the agents could help by approaching existing clients/contacts who were investors, the business networks (i.e. other accountants or solicitors), or professional bodies.

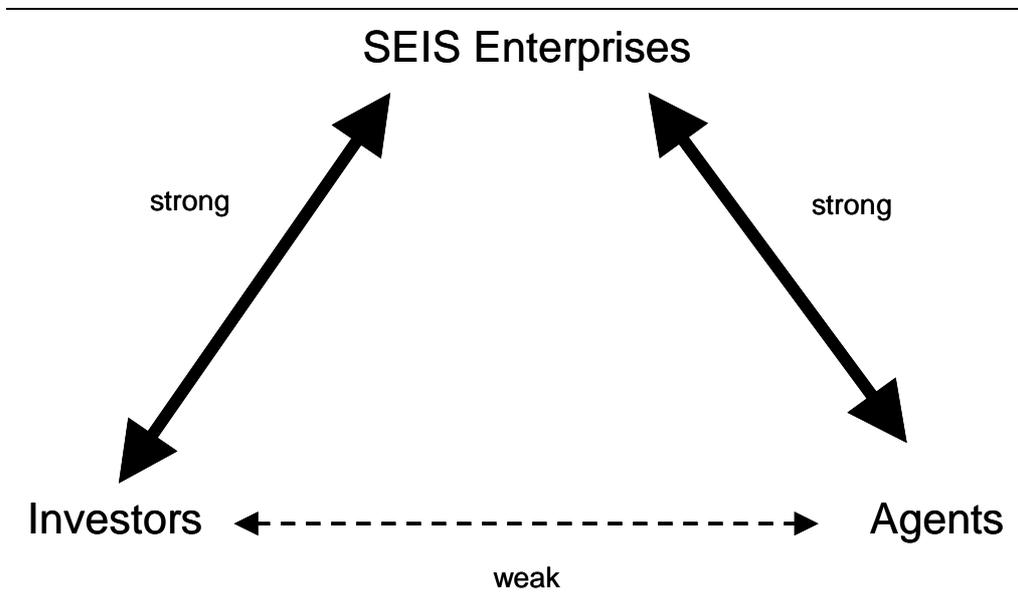
6.2.3 Generally the agents did not know the investors (but some did) and they were introduced to them (if necessary) by the SEIS enterprise.

6.2.4 If the investors did not know of a company to invest in (which was not usually the case with SEIS investments) the agents would firstly consider their existing business contacts and portfolio and liaise with the business networks (accountants and solicitors) and professional bodies.

6.2.5 The criteria the agents and investors usually used to identify businesses to invest in if they needed to, were the growth potential, the management team/directors, the value of assets, and the opportunity to sell shares and subsequently exit the business with a reasonable return. The agents considered that the investors did not usually focus on seed/start-up firms as the risks were greater and, as yet, SEIS did not form part of a deliberate investment strategy for investors.

- 6.2.6 For the SEIS application it was commonplace for the SEIS directors to already know the investors (although sometimes networks were used to find additional investors).
- 6.2.7 The investors (apart from the SEIS application) usually heard about general investment opportunities through friends, family or businesses they already knew or worked with. Sometimes their accountants alerted them. They preferred to carry out some form of due diligence themselves or alternatively via a professional adviser. The criteria used were business growth prospects, the ability of the management team (and whether they could get on with them), the value of assets in the business and the opportunities to sell shares in the business in order to make an acceptable return. By and large the investors had made equity investments in other firms as well as the SEIS companies. They tended to be in small growth businesses and in sectors where the investors already had some experience. When other investments had been made the investors had acted independently and some had used EIS or invested through syndicates. The size of portfolios for investors ranged from less than £50k to over a million, and were spread fairly evenly over this range. The median size was £50-250k.
- 6.2.8 The discussions indicated that there were usually strong links between the SEIS enterprises and the agents prior to the SEIS applications. There were also usually strong links between the SEIS enterprises and the investors. There were relatively weak links between the investors and agents. See Figure 6.1 below, which illustrates the relationships.

Figure 6.1 Strong / Weak Links between Parties



- 6.2.9 Hence the role of the SEIS enterprise was pivotal in that they had strong links with the investors and the agents.

- 6.2.10 Some illustrative points made by the SEIS enterprises on the links that existed with their accountants and investors were as follows:–

SEIS enterprise views on accountants:

- *"They [the accountants] act as an advisor as well as an accountant for us. They give us general business advice."* (SEIS enterprise)
- *"SEIS was introduced to us by the accountant... who we knew"* (SEIS enterprise)
SEIS enterprise views on investors:
 - *Yes [we had existing relationships] with all of them [investors]... none of them are strangers... Some of them are friends... some of them are family... some of them ex-colleagues."* (SEIS enterprise)
 - *"Yes [we knew the investors]. To get people to invest in the business we still need to go to people we know."* (SEIS enterprise)

6.3 The Nature of Links

- 6.3.1 The length of time links had existed between the SEIS enterprises, accountants and investors varied. The agents considered that they had known the company director(s) of the SEIS enterprises for around two years on average prior to the application, and had usually provided them with general business or investment advice prior to the SEIS application. A few agents had made introductions to investors but this was not usually the case.
- 6.3.2 The SEIS enterprises considered that they had known the agents and accountants for a longer period and usually five years or so and before the SEIS application was made. General business advice was usually given together with some advice on investment issues and raising finance.
- 6.3.3 The SEIS enterprises tended to have known their investors for five years or so, on average (and some were friends, other businesses, or family who they had known for a longer period). Some enterprises had known their investors for a shorter period than five years and some for longer. Potential investments (along with other business issues) had been discussed over this period with them. For some enterprises and investors, SEIS helped influence the timing of investments, and probably speeded it up. For others an investment could have been made anyway within a similar timescale.
- 6.3.4 The investors considered that they had known the SEIS enterprises for ten years or so, on average (which indicates they were a friend or existing business contact) but that they knew them for longer where there were family connections. They had discussed business and investment issues generally (along with other matters) but not usually made investments (apart from through the SEIS application). In this context, SEIS potentially helped to bring forward the time when investments were made, although some investors may have subsequently invested in the businesses without SEIS.
- 6.3.5 Where investors knew the agents it was for around ten years or so and the latter had usually advised on taxation and investment issues (but not usually made introductions to companies to invest in). SEIS helped to strengthen the relationships between investors and agents to some extent.

- 6.3.6 Where agents knew the investor prior to the SEIS application (which was the case for a small number of agents) it was usually for around five years or so on average. They had discussed general business/taxation issues and making investments over this time in other businesses that were not SEIS applicants. Some of these investments had gone ahead.
- 6.3.7 The agents considered that there were usually existing links between the SEIS enterprises and the investors in almost all cases where a SEIS application was made.
- 6.3.8 The SEIS enterprises were of the view that the agents and the investors did not usually have links prior to the SEIS investment.
- 6.3.9 The investors were aware that there were usually strong existing links between the SEIS enterprises and the agents prior to the SEIS applications. The results of the research with businesses that did not participate in SEIS indicates that they probably did not have relationships with accountants, and other external advisers, to the extent that the SEIS enterprises had. There was rather mixed evidence as to whether the non-SEIS enterprises sought advice before investment decisions were made. They had some links with accountants for advice and with family and friends, but not generally with investors. This may partially explain their relatively low level of awareness of SEIS, compared to the SEIS enterprises, and where they were aware, why they did not seek to apply. (Please see Chapter 10).

7 The Reasons for Participating in SEIS

7.1 Introduction

7.1.1 The specific reasons why participants use SEIS provide some insights into the attractive features of the scheme especially for the SEIS enterprises and the investors. The general aims and financial and business objectives were discussed with the SEIS enterprises along with the alternative sources of finance to SEIS sought or used. The discussions with investors primarily covered the tax incentives.

7.2 The Agents

7.2.1 Generally, when agents had sought to identify businesses for potential investments the focus was on the growth potential of businesses. Agents would usually review their existing clients, or portfolio, or they would consult business networks (mainly other accountants) or professional bodies. The SEIS businesses were by and large already known to the agents through existing links, and the businesses were alerted to SEIS by them. These businesses, in the views of agents, generally fitted the investment criteria in that they were businesses which sought to grow, and for the agents they met the other criteria for the SEIS scheme, for example, their trade, age and sector eligibility. For most businesses that applied this was confirmed, in the view of the agents, by the use of the advance assurance facility.

7.2.2 Usually the aim of agents when participating in SEIS was to continue to offer a service for existing business clients with the anticipation of future fees as the businesses grew. Initially they charged clients a relatively low fee of between £350 and £1,500 to make the SEIS application. SEIS was seen by agents as a suitable investment vehicle given the early stage the businesses were at, i.e. very young with little trading record. The agents considered that the Enterprise Investment Scheme (EIS) may be suitable for these businesses at a later date, when they had grown.

7.2.3 Agents believed that the businesses used SEIS because it allowed them to attract growth funds. By and large these businesses had not sought alternative funding, in the view of agents. The investors were attracted to SEIS primarily because of the up front tax relief, in the view of agents, and the CGT relief on shares they owned and sold as businesses grew and became more profitable (i.e. disposal relief). Some of the agents' views were:–

- *“I could see that new investors were looking at the tax relief and they would say well that is a good opportunity. So yes it may attract people that wouldn't have considered investment before, because of the tax relief.”* (Agent)
- *“I can't see how SEIS could not be attractive, for investors... the attractions for tax reasons are so great. If you had even half a mind to do it, you would be crazy not to try and use the SEIS or the EIS scheme. SEIS is so generous.”* (Agent)

7.3 The SEIS Enterprises

7.3.1 The main reason for businesses applying to SEIS was to obtain investment to help the business to consolidate following the start up phase, and subsequently grow. Commonly, the businesses also sought to develop their existing or new products and services. Some examples here were websites for hotels and venue event bookings and online sites for retailing and social networks. The other aims were to share the risks with investors as the businesses developed.

7.3.2 The specific financial objectives for enterprises were primarily to obtain equity funds as opposed to debt funding. The SEIS directors were prepared to share ownership of the business and dilute their equity holding within reason. Debt was not seen as an attractive alternative (apart from some short term debt for day to day business operational purposes) primarily because it had to be repaid and had to be serviced, for example through interest payments. Early stage funding was seen as important as well as the contribution equity would make to increasing the overall flow of cash into the business. The SEIS investment met a funding gap and also provided day to day working capital.

7.3.3 Funding for innovation was important for SEIS enterprises and in particular the development of existing and new products, services, processes, and funding for R&D (specifically testing the feasibility of ideas). A smaller number of enterprises had sought to finance recruitment to help improve their skills base.

7.3.4 By and large the enterprises said they had not sought **alternative funding prior to the SEIS application**. Where they had, a minority had sought a bank loan and a very small number had sought business angel or venture capital finance or approached their family and friends. In a few cases where they had sought a bank loan and had been offered it they tended not to take it as the terms and conditions were not acceptable to them, (i.e. securities and guarantees, because the businesses were relatively new and did not have a strong trading record.)

- *“No, we did not apply for any other funds, as SEIS was the best way forward. We knew we wouldn’t be able to get any type of loan finance, especially from the banks.”* (SEIS enterprise)
- *“Yes, we sought funds, before SEIS, and it just didn’t seem like they were going to be right for us...”* (SEIS enterprise)

7.3.5 The businesses that did not seek **alternative funding prior to SEIS** primarily thought it would not be obtained given the stage their businesses were at i.e. very young. The business comments on alternative funding to SEIS were:–

- *“No. There was not other funding. You can’t get funding, not from the banks.”* (SEIS enterprise)

- *“Well, we never took it quite that far to look for other funds. I think we would have been offered something... but I think we sort of concluded that they weren’t the right route for us.”* (SEIS enterprise)

7.3.6 By and large the SEIS enterprises did not seek **additional funding to SEIS once the application had been approved**, but where they did it was primarily for equity or mezzanine finance from business angels. Where they did not seek additional funding they thought they could manage without it (and/or did not think it appropriate for the stage they were at) or they considered that the cost would be too high.

7.3.7 Whether or not the SEIS enterprises had sought additional funding, they generally thought that having SEIS “status” would help them obtain it in the future. The main reasons were that having SEIS funding showed that their business had some credibility, i.e. they had been the subject of some form of “due diligence” carried out by SEIS investors and/or to some extent by the agents/accountants. Also any new investors would be sharing the risk with existing investors and the company itself. However, it was not considered that having SEIS “status” would assist or help to raise debt finance, primarily because the businesses were still very young with some still seeking to make sales which could be important evidence of their likely future success for potential investors.

7.3.8 The SEIS enterprises did not see SEIS investment as funding in the “last resort”. These views were shared by the agents/accountants and the investors. However, some agents did say that the SEIS enterprises were at a very early stage and could not demonstrate strong revenue streams, which would make it difficult for them to raise finance. The agents said that where enterprises could raise finance it would not be as much as the SEIS investors could provide.

7.4 The SEIS Investors

7.4.1 The criteria investors usually used to identify and select a business to invest in were the growth potential of businesses, the management team / directors, the value of assets, the opportunity to sell shares and ultimately exit the business with a reasonable return. Investors also selected businesses where they knew the owners and directors and they liked the business idea and concept, and they had experience of the sectors and trades the businesses were in.

7.4.2 The main aims of investors when they used SEIS were to take advantage of the front end tax relief and the CGT exemptions, in particular the likely gains in the share value of their SEIS investment as the businesses grew and became more profitable, and/or increased their prospects of profitability. The comments made by investors on the attractions of SEIS were:-

- *“What clicked with me is the tax relief... I am a higher rate tax payer, by quite a long chalk...so obviously the 50 per cent tax relief does make sense...it doesn’t reduce the risk of the investment but it does mean you are getting tax*

relief, so the real investment costs you quite a lot less... It's fantastic... it's a great tax break. You would be crazy not to use SEIS." (SEIS investor)

- *"Long term exemptions, CGT gain. Not bothered about anything else, but nice to have the tax break."* (SEIS investor)

7.4.3 The investors were asked whether they would make further investments in the SEIS businesses or invest in other firms. Some investors said they were likely to make further investments in the SEIS business and could use SEIS again. Some investors would make investments in other businesses with or without SEIS. They were not sure exactly how at the time of the interview. Other investors would probably not invest in other businesses at all.

7.4.4 Generally the SEIS investment did not mean that the investors would invest less money in other businesses. In fact SEIS could well stimulate them to invest in other companies in the future (and for some investors SEIS had given them more confidence to make equity investments rather than other forms of investment).

7.4.5 SEIS investors either said that the returns from the SEIS investments would be greater compared to investments they made in other businesses without SEIS, or said they were not sure of what was likely to happen.

7.4.6 The investors were also asked what may have taken place if they had not invested via SEIS. Generally, they would have invested less than they had done through SEIS.

7.5 The Attractive/Unattractive Features of SEIS

7.5.1 Clearly the features of SEIS have a significant influence on the decision to apply. For the agents and the SEIS enterprises the scheme played a vital role in bringing the enterprises and the investors together to allow the investments to proceed. It increased the flow of investment funds for businesses when they were at an early stage in their development and potentially more risky to investors. The businesses and agents considered that, in some cases, the businesses were able to secure funding where they could show a credible business plan that showed the start of activity and the intention of trading, even though their products were new, and the revenue stream, as such, may not have materialised.

7.5.2 The attractions of SEIS for the investors (and confirmed by the agents and enterprises) were the front end income tax relief followed by the exemption from any general realised capital gains in the share value within the prescribed period².

7.5.3 The participants identified very few unattractive features of SEIS. A few made the following points:–

- The share of the investment that qualified for the up front tax break could be larger.

² This is the "disposal relief" from the gain in the value of SEIS shares when they are sold.

- The period for the CGT relief on the gain from a disposal of an unconnected asset (where it was reinvested in a SEIS company) could be extended over a longer period of time³. They did not specify the period.
- The investment threshold could be raised for enterprises and investors.
- Eligible businesses could be more than two years old to allow them to be more investment ready.
- The trade or sector eligibility rules could be relaxed.

7.5.4 A further point made was that some clarification was needed on whether investors had to invest equal amounts or not.

7.5.5 In terms of potential changes to SEIS, some of the points made were:–

- *“As far as HMRC goes it is a well-run business service. What is not helpful to me is chopping and changing rules. That is never helpful.” (Agent)*
- *“Hang on – can we just have some stability here?” (Agent)*

³ This is a reference to a “re-invested relief” as opposed to a “disposal relief” arising from the sale of shares in the SEIS company.

8 The Implementation of SEIS and the Application Process

8.1 Introduction

8.1.1 To assess how SEIS operates, a key part of the discussion sought to provide insights into how the participants perceived the application process once they had been made aware of SEIS, identified their respective partners, and made a decision to apply. The interviews sought to examine, for example, how useful the guidance notes were, the advice obtained from HMRC and the time period within which a decision was made by HMRC. The discussions were mainly with the agents and enterprises as the investors had less direct involvement in making the applications. The views of participants were important to HMRC, as feedback from early stage applicants could provide suggestions for improvements and highlight issues of concern.

8.2 The Views of the SEIS Agents

8.2.1 The agents said most features of SEIS were very useful/helpful. The main features regarded as useful were:–

- The application form and the guidance notes. The former was considered to be easy to use and the latter provided adequate explanation.
- The guidance offered by the HMRC website.
- The written/verbal guidance offered by HMRC.
- The advance assurance facility.
- The guidance and decisions on the advanced assurance facility.
- The time period for making the main application and receiving a decision.
- The overall terms and conditions.

8.2.2 Some of the views expressed by agents on the features of SEIS were:–

- *“Yes, I didn’t have any problems... I mean I had read it all (the guidance) in detail. I was able to work through it and I was able to provide what HMRC required... I don’t think they had any issues with anything that I submitted.”* (Agent)
- *“Yes, we were happy. With our queries I got a reply quite quickly, and actually the lady that wrote to me to confirm the advanced assurance was really helpful and pointed out a condition that I had missed.”* (Agent)

8.2.3 The views expressed by some investors, who tended to use accountants, were:–

- *“Because an accountant did it for me it was relatively painless. They didn’t have any draws on my time for the application or questions... relatively easy.”* (SEIS investor)

- *“Went very smoothly, no problems. I was given a form and I gave it to my accountant.”* (SEIS investor)

8.2.4 Only one issue was raised on which agents had some concerns and this was the perceived delay between the budget announcement to set up SEIS (in March/April 2011) and the availability of application forms⁴.

8.2.5 Agents taking part in the research were usually involved in other Government schemes (particularly EIS) and some thought the application process for SEIS was shorter and easier.

8.3 The Views of Enterprises

8.3.1 The enterprises were not quite as positive about the application process as the SEIS agents in that fewer identified the scheme's strengths. For them the features considered to be useful were similar to those identified by agents but not stressed to the same degree:

- The SEIS application form and guidance notes.
- The time period given to make the application.
- The time taken to receive a decision
- The guidance provided on the HMRC website.
- The verbal/written advice provided by HMRC.
- The advance assurance facility.

8.3.2 As with agents, the enterprises had also initially been concerned over the time taken to make application forms available.

8.4 The Views of Investors

8.4.1 The investors had not been as involved in making applications, but where they had (or based on their liaison with agents and enterprises) they shared the views of the agents and enterprises shown above. This included the views on the advance assurance facility which played some part in attracting investors, as it provided them with some “comfort”, although most said they would have invested anyway in the business without it.

8.5 Suggested Improvements to the Application Process

8.5.1 Very few suggestions were made to improve the application process. Some interviewees said that it would be useful if the application form could be printed, more than one page could be looked at at the same time as part of making the online

⁴ This arose primarily because the Finance Act 2012 was not given Royal Assent until July 2012, after which applications could be made.

application, and that it would be helpful for applicants if they could monitor the progress that was being made on their application over the decision making period.

9 The Impacts that Resulted from SEIS

9.1 Introduction

9.1.1 This part of the research focuses on the impacts and benefits of SEIS from the perspective of the participants. It considers the investor views on the investment landscape as a context for the discussion. It then covers the changes to investment behaviour, and equity investments as a result of SEIS and the impacts on the outputs and outcomes of businesses. The final section assesses what may have occurred in the absence of SEIS.

9.2 The Investment Landscape

9.2.1 On the whole, the agents took the view that the investment landscape had changed significantly over the past five years or so (and specifically since the credit crunch in 2008/9 and steps taken to support the banks, the recessionary phase, and subsequent flatlining of the economy). They said that both debt and equity funds had become more difficult to obtain for businesses, especially from the banks. Within this context the options for investors to grow their capital and income had become more limited with relatively low interest rates, Government bond returns, and equity growth (apart from the stock market growth in the recent past). Hence there has been a growth in other forms of investment, for example, some commodities and property investments, and in particular the buy to let sector

9.2.2 In this context the agents generally considered that in their search for investors there had been a small increase in the activity of business angels but that venture capital activity had seen little change. Primarily in the context of lower levels of bank debt funding, they felt that seed/start-up and micro businesses had started to show more interest in “business angel” finance and vice versa.

9.3 Changes that Resulted from SEIS

9.3.1 The introduction of SEIS had generally, in the view of most of the SEIS enterprises, made them more positive about using equity finance via “business angels” and small investors. The agents shared this view but not as strongly as the SEIS enterprises. The main reasons given by enterprises who were more favourable to equity were that equity did not have to be serviced (through interest payments) or repaid over time. Enterprises could also benefit from the advice and expertise of investors who bought shares and played a role in the company. The agents’ views were:–

- *“Well I would like to think businesses are more positive about equity... it is something that we as a practice encourage people to do and make them aware of it. We would like more take up really because I think it is a good relief on the gains. I can see the attraction for both the investor, who probably favoured equity more, and the company...” (Agent)*

- *“Well possibly they are more attracted to equity funding now... I did a presentation on SEIS to businesses and it was quite well received on the equity funding side. I think people are receptive and the investors were saying you know could I put equity in to that... people were thinking more positively about it.”* (Agent)

9.3.2 Some of the business comments were:–

- *“No. I wouldn’t be funded by anyone apart from using SEIS. Equity financing is much better.”* (SEIS enterprise)
- *“Because for high risk technology business, there is no other financing to compare with equity to support these businesses... as far as I am aware.”* (SEIS enterprise)

9.3.3 Some of the investors considered that they were more positive to equity funding as a result of SEIS (and they had a preference for equity investments) but that their views on debt funding had not changed. There was a general preference for equity funding compared to debt funding as the returns were potentially better and underpinned by greater investor involvement with the business and its development.

9.3.4 In the views of the agents, SEIS was attracting different types of investors compared to other Government schemes (particularly EIS). These investors were prepared to invest smaller amounts in riskier businesses. However they may well have otherwise invested in EIS and possibly in similar companies to some extent but with smaller investments i.e. SEIS encouraged them to invest more in these kinds of firms. The comments made by investors were:

- *“What about equity finance? Probably we now find it more positive as an investment... the best opportunity for a substantial reward is via equity.”* (SEIS investor)
- *“When starting a business you do not want to be held back by repaying big debts...not enough cash flow to do that. Initially equity financing avoids this... At the early phases of business you need to keep as much debt off the business as possible. As the business grows you can move to more debt based financing. So equity is better early on.”* (SEIS investor)

9.3.5 Generally, the agents and enterprises were of the view that participation in SEIS made it easier for the businesses to raise additional external finance from elsewhere (i.e. in addition to the finance from SEIS investors). In part they said this was because they could demonstrate that the SEIS investors had shown confidence in them and invested, and because their investments alleviated the risk for other investors to some extent. Also some form of “due diligence” had already been carried out and the SEIS investment itself gave businesses better growth prospects for new investors.

- 9.3.6 However, it needs to be recognised that some of the SEIS investors said they would probably have invested in the SEIS companies anyway, so that not all the additional investment can be attributed to SEIS.

9.4 Business Outputs and Outcomes

- 9.4.1 The interviews with SEIS enterprises sought to explore what the outputs of the SEIS funding had been, in terms of the aims of businesses when they sought SEIS funding. For example, business consolidation, growth, and improved performance. Overall the enterprises said that their business and funding aims had been wholly or largely satisfied. None said they had not been met. The specific points made were:–

- Consolidation and growth. The funds had consolidated the start-up phase and helped the business grow.
- The funding gap. Generally the equity funding sought had been obtained. As early stage funding, it had met funding gaps, improved cash flow, and provided useful working and investment capital.
- Business operation and recruitment. The main output was successful recruitment and enhancement of skills for the business. The funding allowed businesses to recruit key additional staff.
- Innovation. The finance allowed products to be refined and developed and R&D to be stimulated, especially to allow the feasibility of their ideas to be tested.

- 9.4.2 In terms of business performance outcomes, for some there had been an increase in either employment or the value of the company. Some enterprises also mentioned an increase in turnover, profit margins, or the value of the business' assets. The business comments were:–

- *“Generally the equity funding sought had been obtained. As early stage funding, it has met a funding gap, improved cash flow, and provided useful working capital.”* (SEIS enterprise)
- *“SEIS has enabled the business to expand, employ more people and grow its sales as a further means of raising finance which it may well not have been able to do without SEIS.”* (SEIS enterprise)

9.5 Changes in the Absence of SEIS

- 9.5.1 The SEIS enterprises and their agents considered that by and large the flow of funds they received and the outputs and outcomes for businesses were unlikely to have occurred without the SEIS scheme, albeit the businesses were at a relatively early stage. Some illustrative points made by the businesses were:

- *“No, I don’t think we would have seen the same growth... probably not.”*
- *“No – we would not have achieved the business aims without SEIS.”*

9.5.2 Some investors said they probably would have invested in the businesses anyway without SEIS because they knew the directors and were attracted by the business ideas. By and large there was a consensus amongst the investors that they would not have invested the same amount of money in the company they invested in without the SEIS scheme. Some said they were likely to make further investments in the businesses using SEIS. Some of the investor comments were:–

- *“If the benefit of the SEIS hadn’t been there...it would be less attractive to a person like me who is not especially wealthy... No, definitely not. I would not make the commitment without SEIS.”* (SEIS investor)
- *“Probably not, I would not have invested without SEIS. You either invested money of that sort of order £15K or £25K with SEIS or you didn’t invest.”* (SEIS investor)

9.5.3 Generally the businesses said that:–

- *“Not all the investors would have invested without SEIS. So the business benefits would have been difficult to achieve.”* (SEIS enterprise)
- *“Given that SEIS exists, had we not got it, it would have then been difficult because the investors would have had the opportunity to invest in other companies. Had the whole scheme not existed... then I still am quite confident that we would have probably still managed to raise some money somehow but I’m not sure as much as we did.”* (SEIS enterprise)

10 Non SEIS Enterprises

10.1 Introduction

10.1.1 The interviews with the non-SEIS enterprises focused on businesses that had similar characteristics to the seed enterprises, with respect to, for example, their size, age, sectors and trades. These enterprises were potentially eligible to make a SEIS application. The discussions concentrated mainly on their awareness of Government schemes in general, and SEIS in particular; their general investment decisions; and their likelihood of making a SEIS application.

10.2 Awareness of Government Schemes and SEIS

10.2.1 Generally the interviewees considered that email alerts were the most useful way to make them aware of new Government schemes that are available to different types of business. However, some also suggested that television promotion and, to some extent, letters (with newsletters) as alternative means of communicating with them. It was notable that while they did not discount radio promotion entirely, fewer respondents expressed a preference for this medium, and fewer still, newspapers and trades publications. Some comments by the businesses were:-

- *“Yes e-mails would be better – more direct. I don’t listen to the radio and I don’t watch telly that much so e-mails would be better... E-mails probably are best – direct to me...”* (Non SEIS enterprise)
- *“I don’t read the newspapers... personally... and I watch the news with a very sharp eye... so I guess for me... if it was something that was relevant to me and my business... it would be best to inform me by post... that would be the most useful way of getting the information to me.”* (Non SEIS enterprise)

10.2.2 With regard to the SEIS initiative itself, the level of awareness among non-SEIS enterprises was very low, with only a small number of the respondents expressing any knowledge of the scheme at all. This was still the case after they had been provided with information on SEIS as part of the interview to prompt them about the scheme and other Government schemes, and the potential benefits to enterprises and investors. The few respondents who claimed some awareness of SEIS were asked how they became aware of it. However, they could not recall how they were alerted to the scheme.

10.2.3 Notwithstanding the low level of awareness of SEIS among of the non-SEIS enterprises, many of the interviewees thought, nevertheless, that they would be encouraged to take part in a Government scheme that provided finance, if they were offered the right type of incentives. The main incentive of any Government scheme that would provide businesses with the opportunity to obtain finance was whether the finance was in the form of grant or not. Interviewees favoured grants primarily because they did not have to be repaid. However, whatever the scheme, the

interviewees would take into consideration the costs and conditions attached to it. Another important consideration was the need for good information about the scheme to encourage participation. Lastly, many of the respondents indicated they would like to apprise themselves fully with the ease of applying to use the scheme, whatever it was.

10.3 General Investment Decisions

10.3.1 On the whole, the non-SEIS enterprises said they were using only a narrow range of sources of finance to support their business. The main ones were the sales and turnover of the business and their own personal savings. There was little evidence of them relying on or using external sources of funding. Money from family and/or friends appeared to be the primary external sources of funds for investment. Only a small number of the enterprises were inclined to seek investment funding from other external sources, and, in those instances they were loans from the bank and/or an overdraft facility. Some of the enterprises indicated that they use or had used public sector funding, although it was not clear what the specific source of this funding was. On the whole the non-SEIS enterprises indicated that they preferred the means of funding they were already using as outlined above i.e. sales/turnover, their own savings, money from family and friends and bank funds if they could be obtained. Typically comments from businesses on why they generally did not raise external funding were:

- *“I looked into schemes some time ago. They never appeared to be anything I would quality for. Mostly the schemes I could see were for people to train and develop their skills.”* (Non SEIS enterprise)
- *“I think there are a few Government schemes but obviously because we are up and running I don’t take it any further but I do know there are some schemes available.”* (Non SEIS enterprise)
- *“I mean I don’t think there are Government schemes. I think they are more... charity run things... the one that I am aware of is the Prince’s Trust.”* (Non SEIS enterprise)

10.3.2 There was rather mixed evidence as to the extent to which the non-SEIS enterprises sought advice or information prior to making investment decisions or seeking investment finance. For the few that took advice, it was mostly from an accountant, or family and friends. Several of the enterprises claimed that they sought advice from public sector bodies, although they were not specific about which ones.

10.3.3 On the whole, when they had considered external investment finance, the enterprises were influenced by a narrow range of factors. The cost of finance was foremost among their considerations, with most of them seeking finance at as low cost as possible. The other important considerations were the conditions attached to the finance, and whether these were acceptable or not; whether they would be successful in securing the right amount of finance; and for some, importantly, whether they were

still able to retain control of the business, especially if equity funding was involved. One of the comments was:

- *“I don’t have preferences for debt or equity funding... I think probably towards the bank overdraft because then I maintain control of the company so I think if anything it is that. However I know that companies have grown with equity funding.”* (Non SEIS enterprise)

10.3.4 Only a small number of the businesses interviewed had sought funding over the past two or three years. When these businesses were probed on what types of funding they had applied for or sought, their views corroborated the broad trends set out above: reliance on money from family and friends, bank loans and overdrafts, and in some cases unspecified public sector bodies. Where the enterprises had applied for or sought such finance, generally it had been to enable them to consolidate their start-up business. For the most part the non-SEIS enterprises that had sought such investment were offered what they had sought. It is useful to point out, though, that the amount of finance sought in these circumstances was, on the whole, small, with the median around £5,000. The businesses usually acted alone and did not seek advice.

10.3.5 Very few of the enterprises had used anyone to broker or negotiate funding deals for them to allow them to obtain the finance they required especially as in many cases friends and family were the main sources – although there were some bank loans.

10.3.6 In the main, the non-SEIS enterprises interviewed had not sought any external investment funding in the past, and were not seeking to do so now. The reason given by most of them for not seeking such funding was that they did not need or require it. Some of the illustrative views were:

- *“I suppose I didn’t think we were in need of any funding at the time so we didn’t bother.”* (Non SEIS enterprise)
- *“Don’t trust banks. In business before I lost a lot of money. I have done it different this time around, with my own funds.”* (Non SEIS enterprise)

A relatively large number of enterprises also claimed they were deterred by the high cost of finance in general.

10.3.7 To explore sources of funding further interviewees were asked whether they had any preferences between debt and equity funding if they were seeking to raise finance. They generally had a preference for debt rather than equity funding primarily because of a desire to maintain their independence.

10.4 The Potential for Future SEIS Applications

10.4.1 It was noted earlier that the level of awareness of the SEIS scheme among the non-SEIS enterprises interviewed was very low. This was equally true of their overall

awareness of any (other) Government funding schemes which sought to improve finance and investment in enterprises.

- *“I am not aware of Government funding schemes. No. If I was, I certainly would have looked at it.”* (Non SEIS enterprise)

10.4.2 The non-SEIS enterprises were probed to assess the likelihood of them making an application for funding through SEIS in the future. On the whole, very few of the interviewees indicated they were likely to consider making a SEIS application in the future. They were not looking for external finance from Government schemes or other sources and some businesses did not think they were eligible for any. One view expressed on Government schemes is illustrated thus:

- *“I need funding for the business much like everybody else... I need it but generally it is because every Government avenue that I have looked down, I have not been eligible for anything...”* (Non SEIS enterprise)

10.4.3 Some points on testing the awareness of SEIS in the future are made in the concluding chapter.

11 Conclusions and Summary Points

11.1 Introduction

11.1.1 In this chapter we bring together the main study findings to assess who participated in SEIS in the early stages, address the aims and objectives of the study set out in the introduction, and draw some conclusions on its impact.

11.1.2 The conclusions are based on the views of those participating in the early stages of SEIS, up to the end of the 2012 calendar year. They may not reflect the views or characteristics of those who have participated since then.

11.1.3 Overall, the findings suggest the SEIS scheme has been positively received (and is meeting its operational objectives) in the first few months of its operation.

11.2 The Profile of Early Participants in SEIS

11.2.1 Based on both the initial information provided by HMRC and information gathered during the interviews, the characteristics of those involved in SEIS in the early stages up until the end of 2012 were:–

- a Agents. Some nineteen who were mainly accountants and financial services were firms primarily based in London and the South East, with some around Manchester. Generally, they had submitted two to three SEIS applications each.
- b SEIS Enterprises. There were sixty four companies with early SEIS applications who were generally based primarily in London and the South East, and to a lesser extent in the Manchester area, as micro and start-up businesses. They were generally seeking to grow rapidly and were mainly in online services for retailing, and/or creative industries (i.e. film or advertising), or in software development.
- c Investors. There were two hundred and eighty five investors listed in early SEIS applications, usually resident in London and the South East. These were mainly men over the age of fifty who were self employed or retired. Most made relatively few business investments.

11.2.2 Given that the SEIS scheme was in its early stages only a small proportion of eligible businesses had applied. The research with businesses that had not applied shows that they were generally located in London and the South East (where the vast majority of SEIS businesses were from), with significant numbers of potential eligible applicants also in the North West and the Midlands, and spread across a number of trades similar to the SEIS sectors. The vast majority of these potential SEIS applicants were not aware of the scheme, which is to be expected in the early stages of delivery.

11.3 The Implementation of SEIS and Application Process

- 11.3.1 The participants in SEIS said that once they were initially aware of SEIS, there was a delay before they could apply which in turn delayed investment. However, most features of the application process itself were acceptable to them and they generally found them very useful. The features they highlighted were the application form itself and the associated HMRC guidance notes and the information provided. The guidance offered by HMRC via the website, verbally and in writing was seen as being equally helpful. The time period within which applications needed to be made, and the period taken for decisions to be given were seen as quite adequate.
- 11.3.2 These positive points were also made on the advance assurance process, by agents, businesses, and investors, which allowed them to ascertain whether the applications were likely to be approved and whether businesses were eligible. Although most used it, the businesses and investors thought by and large the investments using SEIS would have been made without it anyway.
- 11.3.3 By and large, the agents interviewed were familiar with other “similar” Government schemes, especially EIS, and considered that the SEIS application process, if anything, was slightly simpler than EIS.

11.4 SEIS Awareness and Communication

- 11.4.1 The SEIS enterprises generally heard about the scheme through their accountants who subsequently became involved in making the SEIS applications (both for the advanced assurance stage and the full application). Some had also been alerted by the financial press at the time of the budget. A few mentioned that SEIS had been drawn to their attention by friends, other businesses and their families.
- 11.4.2 Overall the enterprises participating in the research said they preferred to be alerted to Government schemes via direct email contact (with newsletters) and through their advisers and accountants, many of whom provided detailed budget updates (following budget announcements).
- 11.4.3 There was no indication that enterprises from different sectors, or locations, participating in the research favoured alternative methods of communication. The possible exception to this was that IT / communication companies placed more emphasis on email alerts.
- 11.4.4 The enterprises interviewed did not appear to use any information hubs or networks such as universities, business networks, trade associations or online hubs. However, the agents often received detailed information, for example, on budget announcements, through the professional bodies / service companies they used to provide, for example, continuing professional development (CPD) and “training”.
- 11.4.5 However, participating agents had mainly been alerted to SEIS through the budget statement followed by articles in the financial press and through the HMRC website.

They preferred these means as ways of informing them of Government schemes. On the whole, the investors first heard about SEIS via their accountants (through emails and newsletters) and had a preference for this method along with direct emails and newsletters.

- 11.4.6 The non-SEIS enterprises interviewed were in the vast majority of cases not aware of SEIS. To alert them to SEIS and Government schemes, their preference was for e-mail alerts, followed by television promotion and to some extent letters, i.e. they said that mail shots and newsletters would be appropriate.

11.5 Sources of Finance Used by Enterprises

- 11.5.1 Generally, SEIS enterprises said they had not sought alternative finance to SEIS. Where they had, they had sought a bank loan and/or business angel or from venture capital companies. A small group had approached their family and friends. However, the feedback given was that receiving a bank loan equivalent to the size of their SEIS investment, or for a lesser amount, was seen as unlikely by the enterprises and their agents, primarily because they were very new businesses. Those enterprises which had been offered a bank loan tended not to have taken it up because of the conditions attached and the guarantees and securities required. However, SEIS was not generally seen as “last resort” funding by the agents, investors and enterprises. Some investors said they would have invested some money in the businesses anyway as they knew the directors of the businesses and were attracted by the business ideas and the products and services.

- 11.5.2 Generally, the SEIS enterprises said they preferred equity funding as (in spite of a dilution in their equity holding) it did not have to be “serviced” (through interest charges) or repaid as debt finance does. It also tended to be more substantial and provided both day to day operational and growth/investment finance. Investors could also give useful business advice when they provided equity funding as they had a stake in the business.

- 11.5.3 Underpinning this, the SEIS businesses interviewed were growth orientated and some aimed to achieve significant growth. They were also relatively innovative with a focus on the enhancement of existing products and services and the development of new ones in conjunction with some R&D, primarily to test feasibility options. Hence equity funding was more appropriate than debt funding.

11.6 The Reasons for Participating in SEIS

- 11.6.1 Generally the aims of agents for participating in SEIS were to continue to offer a service for existing business clients with the anticipation of future fees as the businesses grew. For them, SEIS was a suitable investment vehicle given the stage the SEIS businesses were at.

11.6.2 For the SEIS enterprises the main reason for applying to SEIS was to obtain investment finance to allow their businesses to consolidate and grow. Commonly they sought to develop their existing and new products and services. A specific financial objective was to obtain equity funds as opposed to debt funding.

11.6.3 The main aims of investors were to take advantage of the front end tax relief that SEIS offered and in particular the CGT exemptions from the likely gains in the share value of their SEIS investments as the businesses grew and increased their profitability (i.e. equity disposal relief). Generally the investors also knew the directors of the businesses prior to investing via SEIS and they liked the business ideas so that some may have invested in the business without SEIS but generally they would have invested less than they had done through SEIS.

11.7 Links Between Agents, SEIS Enterprises, and Investors

11.7.1 The strongest links in the SEIS process for early applicants were between the agents and the SEIS companies and the latter and the investors. The links between the agents and the investors were generally relatively weak and the introductions of these two parties, where appropriate, were made via the SEIS enterprises. The agent / SEIS enterprise links could have existed for several years and the latter tended to act for existing businesses as clients rather than new ones.

11.7.2 The agents interviewed tended to play an important role in making the businesses aware of the SEIS opportunity, persuading the enterprises to make an application and organising it for them. Generally, the agents did not act as brokers between the enterprises and investors to resolve issues between them. By and large, there were some negotiations between the enterprises and investors involved in the application but these were not deemed to be significant.

11.7.3 The links between the investors and enterprises interviewed had usually existed for a few years prior to the SEIS application and they were usually business contacts, friends or family.

11.7.4 The agents took the view that by and large they influenced the decision, made ultimately by businesses, to apply for SEIS, primarily through their discussions with SEIS enterprises. The SEIS enterprises maintained they usually made the decision to use SEIS to obtain investment and/or worked with an accountant/adviser to reach a decision. The investors made their decision to invest and apply for SEIS usually in conjunction with the SEIS enterprise and in some cases also in liaison with agents.

11.8 Agent and Investor Behaviour in Relation to Investment

11.8.1 In terms of the criteria that the agents interviewed usually used to identify businesses for potential investment, the focus was on the growth potential of businesses. When seeking to identify businesses they would usually review their existing business clients, existing portfolio, or they would consult their business networks. In general,

the agents already knew the businesses that were applying to SEIS. By and large they were growth businesses who met the SEIS eligibility criteria. The agents charged a relatively small fee to make the SEIS application and generally saw prospects of future fees as businesses grew. Given the stage the SEIS businesses were at, SEIS was the most suitable investment vehicle although the Enterprise Investment Scheme (EIS) could be used at a later stage as the businesses grew and needed larger amounts of finance.

- 11.8.2 It was commonplace for the agents interviewed to be involved in other Government schemes (especially EIS). In general, they thought that SEIS played a different role in encouraging start-up / early stage investments but EIS could come into play as the business became larger and more successful and additional funding was sought. Investors shared this view and some had experience of using EIS for investments in more mature companies.
- 11.8.3 The criteria investors would use to identify and select a business to invest in were the growth potential, the management team / directors, the value of assets, the opportunity to sell shares and ultimately exit the business with a reasonable return. Investors also selected businesses where they knew the owners and directors and liked the business idea and concept. They also preferred sectors they had previously worked in and had experience of.
- 11.8.4 Overwhelmingly the SEIS investors used the scheme because they sought to take advantage of the front end tax relief and the CGT exemptions, in particular the likely gains in the share value of their SEIS business on disposal of the shares.

11.9 The Impacts that Resulted from SEIS

- 11.9.1 Based on the information provided by HMRC, up to the end of the 2012 calendar year, the participation in SEIS seems to have been relatively low, i.e. some nineteen agents, sixty four SEIS enterprises, and two hundred and sixty investors in these companies. This is expected considering that the scheme had only been open to applications for a few months.
- 11.9.2 Based on the views of the agents and the SEIS enterprises interviewed, it was the view that the latter had become more favourably inclined to equity funding as a result of SEIS. Equity finance, unlike debt, did not have to be repaid, or serviced through interest rate payments; the directors could ultimately achieve higher rewards through business growth and the potential sale of their shares. The businesses could also benefit from the advice given by investors, especially where they had experience of the sector.
- 11.9.3 In the view of investors and agents, SEIS had encouraged some investors to be more inclined to equity funding (compared to other investments). Debt funding was not generally preferred and SEIS had not changed the attitude of investors in this respect. This has resulted in a small change to the investment landscape nationally (i.e. primarily banks, business angels and venture capital funds where relatively larger

amounts of growth funding were sought). SEIS had encouraged equity funders because of the up front tax relief in particular and the CGT allowances they benefitted from, and especially the share disposal allowance from gains in value. However, some funders said they would probably have invested in the SEIS businesses anyway – but, for some, with a lesser amount. They tended to know the directors of the business they had invested in and liked the business ideas. The investment through SEIS did not mean that the investors would not invest in other small businesses if suitable opportunities arose.

11.9.4 Some investors said they would make further investments in the SEIS enterprise they had already invested in, but not necessarily through using SEIS again. Their SEIS investment was not likely to mean that they would not make investments in other businesses but the amount could be smaller compared to their investment in the SEIS enterprises.

11.9.5 The SEIS programme also had some initial impacts on business outputs and outcomes, in the view of SEIS enterprises. The initial aims of businesses when they sought SEIS funding had been to grow and consolidate their businesses as well as developing new products and services. Funding for innovation was also seen as important. Overall these aims of businesses had been wholly satisfied. According to the enterprises, the funds generally had consolidated the start-up phase and resulted in early growth for most. The equity funding sought had been obtained, met the funding gap, and improved cash flow and working capital. For some businesses, there had been recruitment of key staff with appropriate skills, and innovation activities had been strengthened with existing and new products and services refined and developed and the feasibility of ideas tested. For some businesses there had been consequent increases either in turnover, profit margins, or in the value of business assets.

11.10 The Views of Non SEIS Enterprises

11.10.1 The level of awareness of SEIS among non-SEIS enterprises was very low, with only a small number of the respondents expressing any knowledge of the scheme at all. The few respondents who claimed some awareness of SEIS were asked how they became aware of it. However, they could not recall how they were alerted to the scheme.

11.10.2 Notwithstanding the low level of awareness of SEIS and other Government schemes among these enterprises, many of the respondents thought, nevertheless, that they would be encouraged to take part in a Government scheme to provide finance, if they were offered the right type of finance with appropriate conditions. Grants were the most attractive form of finance for them as they did not have to be repaid. Grants were more attractive than loans or equity finance.

11.10.3 Generally the interviewees considered that emails were the most useful way to alert them to information about Government schemes available to businesses. However,

some also suggested that television promotion and, to some extent, letters and newsletters would be an appropriate means of communicating with them.

- 11.10.4 On the whole, the non-SEIS enterprises said they were using only a narrow range of sources of finance to support their business. The main ones were the sales and turnover of the business and their own personal savings. On the whole, very few of the respondents indicated they were likely to consider making a SEIS application in the future as they were not looking for external finance.

11.11 Suggestions for Further Research

- 11.11.1 The research carried out for this report has covered the early stages of SEIS and the initial participants in the first few months of the scheme's operation. As the participation increases and the programme matures further research could help gain additional insights into the operation of SEIS, the potential need for improvements, evidence of the impact of SEIS and the benefits.

- 11.11.2 The discussions have provided some indications as to where further research could be carried out. The suggestions for consideration by HMRC are as follows:–

- a Continued monitoring of the take-up of SEIS in terms of the number of successful and unsuccessful applications at the advance assurance facility and full application stages, with characteristics of the types of applicants using the characteristics shown in Chapter 3 above.
- b Continued monitoring of the awareness of SEIS, by gathering the views of eligible applicants and their agents (i.e. accountants and tax advisers) to assess how they became aware of SEIS. It may also be useful to assess what their preferences are for being alerted to SEIS and/or other Government schemes
- c Focussing the promotional activities to alert businesses to SEIS (and other schemes) on 1) agents (e.g. accountants and tax advisers) as key conduits of information to businesses and investors; and 2) on the financial services sector, including banks and business angels / venture capital investors and networks/associates. Fully utilising HMRC and other relevant Government web sites (e.g. Business Innovation and Skills and the Technology Strategy Board).
- d The role of SEIS in helping to raise additional funds for investors could also be explored, and whether the current SEIS investment threshold for business is appropriate.
- e Exploring the investment that enterprises attract in addition to the SEIS funding and whether constraints to additional funding apply.

- f Whether the SEIS investors invest more in a SEIS business than they would have done without SEIS, and whether they invest in the same and other businesses without using SEIS.
- g Whether the SEIS thresholds are appropriate for investors in terms of the amount of finance they can invest with tax relief.
- h Evaluation of the gross and net additional impacts of SEIS (and other levered in funds) on businesses: the intermediate impacts on capabilities and skills; on innovation activities; on exploitation of products and services; and on business performance impacts – turnover, jobs, exports, profits, along with the value of the business. Monitoring and evaluation systems can be put in place at an early stage in the implementation of SEIS to capture baseline information. Subsequently, change can be assessed using management information and survey research (as well as case studies).

Consideration could also be given to whether a comparison group of businesses (that were similar to the SEIS enterprises) could be used to examine the net effects of SEIS.

This monitoring and evaluation task would help to estimate the economic and wider benefits of SEIS.

- 11.11.3 These are the main points suggested for further research following the initial stages of the delivery of SEIS.

Appendix A The Discussion Guide Topics

The Investors

- Their characteristics. Age, gender, employment status.
- The SEIS investment. When it was made, the use of the advance assurance facility and whether it was a necessary condition for the investment, would the investor have invested without SEIS, how much was invested through SEIS, participation on the Board.
- The characteristics of the business invested in (age, products, services, sector, location, independent/subsidiary status, growth aspirations and innovation activities such as R&D).
- Investment decisions. Sources of information used to identify opportunities, due diligence, criteria used for investments and funding provided to other businesses, either through syndicates or not, and the value of any total investment portfolio.
- The aims of using SEIS. Tax benefits and future returns.
- Awareness of SEIS. How investors heard of SEIS and preferred methods of alerts to Government schemes. Follow-up to gain further information on SEIS (e.g. HMRC, accountants, professional bodies).
- Links with SEIS participants. The extent of prior links with agents and SEIS enterprises. The nature and duration of links.
- The SEIS investment decision. Who influenced the decision to apply to SEIS and their roles in brokering and negotiations between the parties, and issues covered.
- Reasons for using SEIS, e.g. the front end tax breaks and CGT exemptions. The more and less attractive features of SEIS.
- Further investments in SEIS and other businesses, and the likely relative returns.
- Changes in attitudes to investment. Changes in views towards equity and debt funding.
- The counterfactual. Investment that may have been made in SEIS businesses in the absence of SEIS, and the amounts.
- Improvements to SEIS. The application process and the scheme conditions.

Agents / Intermediaries

- Characteristics. Accountants, tax advisers, location, whether they act for businesses and investors.
- Type of business they act for (by size, sector, stage of development, and region)
- Type of investors (e.g. small investors and business angels) they usually act for (small, medium, large, key sectors, locations)
- The SEIS applications. Number of applications made, the dates and the characteristics of businesses and investors. Use of the advance assurance facility.
- How businesses and investors are usually identified, investment opportunities sought, the sources and criteria used.
- Awareness of SEIS. Sources used for SEIS and preferred methods of hearing about Government schemes.
- The aims of using SEIS – services provided for clients and ongoing client relationships
- The follow-up sources used to gain further information on SEIS (e.g. HMRC).
- The SEIS application decision. Who influenced the decision and how it was made. The roles of brokers, negotiations and issues, the conditions of enterprises / investors.
- The links with SEIS enterprises and investors. The extent to which the agents, investors and enterprises already knew one another prior to the SEIS application, and the strength/duration of links.
- Whether businesses had sought alternative funding to SEIS and from where. Whether SEIS was funding of the last resort.
- The SEIS application process. The usefulness of the forms and guidance notes and advice received.
- Improvements to SEIS. The application process and the scheme conditions.
- Changes in attitudes. How SEIS changed attitudes amongst businesses and investors towards equity and debt finance and the attractive / unattractive features of SEIS.
- Other Government schemes. Use of other schemes and comparisons with SEIS in terms of the application process and different types of businesses and investors involved.

- The counterfactual. What investments in businesses may have been made in the absence of SEIS.

The SEIS Enterprises

- Characteristics. Age, period of trading, products, services, size, sector, location, innovation activities (such as R&D), growth ambitions.
- SEIS applications. Number made. Use of the advance assurance facility. The value of the SEIS investment.
- Awareness of SEIS. Sources used and preferred methods of hearing about Government schemes.
- The SEIS application decision. Who influenced the decision (the business, agent and/or investor). The roles of brokers, negotiations with the issues and the conditions of enterprises/investors.
- The links with agents and investors. The extent to which the agents, investors and enterprises already knew one another prior to the SEIS application, and the strength/duration of links.
- Reasons for using SEIS. Obtain finance, consolidation and growth, share risks with others, purchase plant, equipment, recruit staff, improve innovation and improve sales and profitability.
- Whether businesses had sought alternative funding to SEIS, the amounts, sources and outcomes and additional funding sought as well as SEIS.
- The SEIS application process. The usefulness of the forms and guidance notes and advice received.
- Improvements to SEIS. The application process and the scheme conditions.
- Changes in attitudes. How SEIS changed attitudes to equity and debt finance and the attractive / unattractive features of SEIS.
- The SEIS impacts on the business. Whether aims were satisfied. The finance raised and the impacts on products, services, plant, equipment, recruitment, innovation, and business performance (growth, turnover, profits)
- The counterfactual. What investment finance may have been made in the absence of SEIS and whether similar business outputs and performance outcomes would have been achieved.

Non-SEIS Enterprises

- Characteristics. Age, period of trading, products, services, size, sector, location, innovation activities (such as R&D), growth objectives.

- Awareness of SEIS. Whether businesses were aware of SEIS, sources used and preferred methods of hearing about Government schemes.
- If businesses were aware of SEIS, whether they sought additional information and advice.
- Whether businesses could apply to SEIS in the future (if they were aware of the scheme) with reasons and what the general business aims may be (e.g. consolidation, growth, attract finance, develop products/services, premises, equipment, recruitment and business growth).
- Investment. Sources of finance usually used and sources of advice received (e.g. accountants, friends and family).
- Types of funding applied for (or not), and the sources used, success in raising finance and what the finance was for. Why funding was not sought.
- Awareness of Government schemes and preferred methods of being alerted to them.
- Preferences between debt and equity finance, with reasons.