



Income tax and capital gains tax: changes to Venture Capital Schemes for companies and community organisations benefiting from energy subsidies

Who is likely to be affected?

Companies and community organisations seeking Seed Enterprise Investment Scheme (SEIS), Enterprise Investment Scheme (EIS) or Venture Capital Trust scheme (VCT) investment (tax-advantaged venture capital schemes) and community organisations seeking Social Investment Tax Relief (SITR) investment, where a substantial activity of the company or community organisation is, or will be, eligible for a government subsidy for the generation of energy from renewable sources. Individuals and some fund managers who invest in the companies or community organisations may also be affected.

General description of the measure

This measure amends the list of excluded activities within the tax-advantaged venture capital schemes and SITR. Companies (excluding community organisations) whose trade consists wholly or substantially of the subsidised generation of energy from renewable sources where anaerobic digestion or hydroelectric power is involved, or where a company enters into a Contract for Difference, will cease to be eligible for investment under the SEIS, EIS and VCT schemes.

When the enlargement of SITR receives State aid clearance, community energy companies whose trade consists wholly or substantially of the subsidised generation of energy from renewable sources will cease to be eligible for investment under the SEIS, EIS and VCT schemes. At the same time, the qualifying activities under SITR will be amended to allow activities for which a Feed in Tariff (FIT) subsidy is receivable.

The measure will apply in respect of UK subsidies and overseas equivalents.

Policy objective

The measure will help target tax reliefs provided by the venture capital schemes and SITR on investment for riskier, early stage and developing companies and community organisations, which may face barriers in raising external finance. It will help the venture capital schemes and SITR to provide better value for money. The change ensures the venture capital schemes continue to support smaller and growing businesses in a targeted and effective way and that SITR in particular supports activities which produce a social benefit.

Background to the measure

In general, where trading activity consists to a substantial extent of the generation of energy from renewable sources for which a government subsidy is available any investment will not be eligible for the tax-advantaged venture capital schemes or SITR. However there are exceptions where the activity is carried out by a community organisation or involves anaerobic digestion or hydroelectric power and, for SITR only, where the activity is subsidised by way of Renewables Obligation Certificates (ROCs) or Renewable Heat Incentives (RHI). Some of these subsidies will be replaced by new Contract for Difference subsidies from 2015.

The Government consulted over the summer to assess the impact of the tax-advantaged venture capital schemes and on changes to the Sitr. The consultation sought views on whether the reliefs for some types of renewable energy generation that qualify for extra government support were still justified.

The Government continues to be concerned about the proportion of investments into renewable energy activities that are relatively low-risk and benefit from government support. There has been a recent increase in the marketing around these investment opportunities for companies currently unaffected by the restrictions on renewable energy. Much of this investment activity is explicitly marketed as lower risk or capital preservation, emphasising the tax reliefs, the predictable income stream from the energy generation and certain proven technologies, and the government support in the form of subsidies for the generation of renewable energy to attract investors.

Detailed proposal

Operative date

This measure will have effect for activities involving anaerobic digestion and hydroelectric power, and activities subsidised under a Contract for Difference, for:

- the EIS and SEIS, in relation to shares issued on or after 6 April 2015
- VCTs, in relation to relevant holdings issued on or after 6 April 2015.

The other provisions will take effect from a future date once State aid clearance is received for the enlargement of the Sitr, but no earlier than 6 April 2015.

Current law

Sections 198A, 198B, 257MS, 309A and 309B of the Income Tax Act (ITA) 2007 provide exceptions to the general exclusion of subsidised energy production from the SEIS, EIS, VCT and Sitr schemes in relation to community energy schemes and anaerobic digestion and hydroelectric electricity. There are no separate rules for the SEIS, which follows the EIS rules on excluded activities.

Proposed revisions

Legislation will be introduced in Finance Bill 2015 to amend ITA 2007 to modify the existing rules that currently allow companies and community organisations to be eligible for the SEIS, EIS and VCT schemes, where their activities consist wholly or substantially of the subsidised generation or export of electricity, or the subsidised generation of heat or production of gas or fuel, and:

- the activities are carried out by community groups or
- where anaerobic digestion or hydroelectric power is involved or
- the company has entered into a Contract for Difference under the Energy Act 2013.

For Sitr, activities that are subsidised by way of FITs will cease to be excluded activities following State aid clearance of the scheme.

Summary of impacts

Exchequer impact (£m)	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
	-	-15	+30	+10	+10	+10
	<p>These figures are set out in Table 2.1 of Autumn Statement 2014 and have been certified by the Office for Budget Responsibility. More details can be found in the policy costings document published alongside Autumn Statement 2014.</p>					
Economic impact	<p>This measure is not expected to have significant economic impacts.</p>					
Impact on individuals, households and families	<p>Individuals investing under the schemes benefit from a range of tax reliefs including income tax relief on the amount subscribed for shares in eligible companies (or qualifying loans under the SITR) and favourable capital gains tax treatment on eligible investments.</p> <p>This measure is not expected to have an impact on family formation, stability or breakdown.</p>					
Equalities impacts	<p>From the data available it is reasonable to conclude that these changes will not have any further impact on those groups affected by equality legislation.</p>					
Impact on business including civil society organisations	<p>The changes proposed will limit the availability of tax reliefs for investment in some smaller companies and change the availability of tax reliefs for civil society organisations benefiting from, or planning to benefit from, existing government support, whose trades involve the production of electricity or heat from renewable sources. These changes will have some minimal administrative costs on those companies and organisations, although this is necessary to ensure that the reliefs remain properly targeted and the impact of the changes will be fairly small, within the existing framework of the reliefs.</p> <p>VCTs will incur some one-off administrative costs since they will need to ensure that their investments meet the new conditions. These costs are expected to be negligible.</p>					
Operational impact (£m) (HMRC or other)	<p>The additional costs for HM Revenue and Customs in implementing this change are anticipated to be negligible. There will be some small costs in updating forms and guidance.</p>					
Other impacts	<p><u>Small and micro business assessment:</u> tax-advantaged venture capital schemes are reliefs intended to help small and micro businesses and changes to them may therefore have an impact on such business.</p> <p><u>Competition assessment:</u> The changes should not have any impact on competition as they do not affect or limit suppliers' ability to compete.</p> <p><u>Environmental impact:</u> The removal of the exceptions for anaerobic digestion and hydroelectric power will remove the incentive for companies to be set up to take advantage of these "double-subsidies". Any impact on renewable energy will be offset in part by the extension of SITR to community energy organisations.</p> <p>Other impacts have been considered and none have been identified.</p>					

Monitoring and evaluation

Uptake of the Venture Capital Schemes in terms of numbers of investors and investees, amounts of investment and the distribution of levels of investment will continue to be monitored and published.

Further advice

If you have any questions about this change, please contact Cathy Wilson on 03000 536678 (email: cathy.wilson@hmrc.gsi.gov.uk).

1 Investment reliefs: excluded activities

Schedule 1 makes provision about excluded activities for the purposes of the following provisions of ITA 2007 –

- (a) Part 5 (enterprise investment scheme) and, by virtue of section 257DA(9) of that Act, Part 5A (seed enterprise investment scheme),
- (b) Part 5B (tax relief for social investments), and
- (c) Part 6 (venture capital trusts).

SCHEDULE 1

Section 1

INVESTMENT RELIEFS: EXCLUDED ACTIVITIES

PART 1

PART 5B OF ITA 2007: AMENDMENT COMING INTO FORCE ON PASSING OF ACT

Tax relief for social investments: power to amend excluded activities

- 1 In Part 5B of ITA 2007 (tax relief for social investments), after section 257MV insert –

“257MW Excluded activities: power to amend

- (1) The Treasury may by regulations make such amendments of sections 257MQ to 257MT as they consider appropriate.
- (2) Regulations under this section may –
 - (a) make different provision for different cases or purposes, or
 - (b) include such transitional provision as the Treasury consider appropriate.
- (3) So far as they cause an activity to cease to be an excluded activity, amendments made by regulations under this section may have effect in relation to times before they come into force, but not times before 6 April 2015.
- (4) Any provision that may be made by regulations under this section may be made by order.”

PART 2

PART 5 OF ITA 2007: EXCLUDED ACTIVITIES FROM 6 APRIL 2015

Introductory

- 2 The following provisions of Part 5 of ITA 2007 (enterprise investment scheme) are amended as set out in paragraphs 3 and 4 –
- (a) section 198A (excluded activities for purposes of Part 5 (and, by virtue of section 257DA(9), Part 5A): subsidised generation or export of electricity), and
 - (b) section 198B (excluded activities for those purposes: subsidised generation of heat and subsidised production of gas or fuel).

Generation of electricity involving contracts for difference

- 3 In section 198A –
- (a) in subsection (3), omit “or” at the end of paragraph (b) and after paragraph (c) insert “, or

- (d) a contract for difference has been entered into in connection with the generation of the electricity.”, and
- (b) in subsection (9), at the appropriate place insert –
 - ““contract for difference” means a contract for difference within the meaning of Chapter 2 of Part 2 of the Energy Act 2013 (see section 6(2) of that Act);”.

Subsidised energy-related activities: anaerobic digestion and hydroelectric power

- 4 (1) In section 198A –
 - (a) in subsection (5), omit “, B or C” (exceptions for generation involving anaerobic digestion and hydroelectric power),
 - (b) omit subsections (7) and (8), and
 - (c) in subsection (9), omit the definition of “anaerobic digestion”.
- (2) In section 198B –
 - (a) in subsection (3), omit “or B” (exception for generation or production involving anaerobic digestion), and
 - (b) omit subsection (5).

Application

- 5 The amendments made by this Part of this Schedule have effect in relation to shares issued on or after 6 April 2015.

PART 3

PART 6 OF ITA 2007: EXCLUDED ACTIVITIES FROM 6 APRIL 2015

Introductory

- 6 The following provisions of Part 6 of ITA 2007 (venture capital trusts) are amended as set out in paragraphs 7 and 8 –
 - (a) section 309A (excluded activities for purposes of Part 6: subsidised generation or export of electricity), and
 - (b) section 309B (excluded activities for those purposes: subsidised generation of heat and subsidised production of gas or fuel).

Generation of electricity involving contracts for difference

- 7 In section 309A –
 - (a) in subsection (3), omit “or” at the end of paragraph (b) and after paragraph (c) insert “, or
 - (d) a contract for difference has been entered into in connection with the generation of the electricity.”, and
 - (b) in subsection (9), at the appropriate place insert –
 - ““contract for difference” means a contract for difference within the meaning of Chapter 2 of Part 2 of the Energy Act 2013 (see section 6(2) of that Act);”.

Subsidised energy-related activities: anaerobic digestion and hydroelectric power

- 8 (1) In section 309A –
- (a) in subsection (5), omit “, B or C” (exceptions for generation involving anaerobic digestion and hydroelectric power),
 - (b) omit subsections (7) and (8), and
 - (c) in subsection (9), omit the definition of “anaerobic digestion”.
- (2) In section 309B –
- (a) in subsection (3), omit “or B” (exception for generation or production involving anaerobic digestion), and
 - (b) omit subsection (5).

Application

- 9 The amendments made by this Part of this Schedule have effect in relation to relevant holdings issued on or after 6 April 2015.

PART 4

FURTHER AMENDMENTS OF PARTS 5 TO 6 OF ITA 2007

Parts 5 and 6: certain community-based activities to be excluded activities

- 10 (1) Part 5 of ITA 2007 is further amended as follows.
- (2) In section 198A –
- (a) omit subsections (5) and (6) (exception for community-based generation), and
 - (b) in subsection (9), omit the definitions of “community benefit society”, “co-operative society” and “NI industrial and provident society”.
- (3) In section 198B –
- (a) omit subsections (3) and (4) (exception for community-based generation or production), and
 - (b) omit subsection (6) (interpretation of section).
- 11 (1) Part 6 of ITA 2007 is further amended as follows.
- (2) In section 309A –
- (a) omit subsections (5) and (6) (exception for community-based generation), and
 - (b) in subsection (9), omit the definitions of “community benefit society”, “co-operative society” and “NI industrial and provident society”.
- (3) In section 309B –
- (a) omit subsections (3) and (4) (exception for community-based generation or production), and
 - (b) omit subsection (6) (interpretation of section).
- 12 In consequence of paragraphs 10 and 11 –
- (a) in FA 2014, omit section 56(3)(b) and (6)(b), and

- (b) in the Co-operative and Community Benefit Societies Act 2014, omit paragraphs 106 and 107 of Schedule 4.

Part 5B: subsidised generation or export of electricity to cease to be excluded activity

- 13 (1) Part 5B of ITA 2007 is further amended as follows.
 - (2) In section 257MQ(1) (list of excluded activities) omit paragraph (f) (subsidised generation or export of electricity).
 - (3) Omit section 257MS (subsidised generation or export of electricity).

Application of Part

- 14 (1) The amendments made by this Part of this Schedule have effect in accordance with regulations made by the Treasury.
 - (2) Regulations under this paragraph may make different provision for different purposes.
 - (3) Section 1014(4) of ITA 2007 (regulations etc subject to annulment) does not apply in relation to regulations under this paragraph.
 - (4) Regulations under this paragraph may not provide for amendments of ITA 2007 to have effect –
 - (a) in the case of amendments of Part 5 of that Act, in relation to shares issued before 6 April 2015;
 - (b) in the case of amendments of Part 6 of that Act, in relation to relevant holdings issued before 6 April 2015.

EXPLANATORY NOTE

INVESTMENT RELIEFS: EXCLUDED ACTIVITIES

SUMMARY

1. This measure excludes all types of renewable energy generation activities subsidised by the government from the scope of the venture capital schemes – the Seed Enterprise Investment Scheme (SEIS), the Enterprise Investment Scheme (EIS) and Venture Capital Trusts (VCTs). It makes provision for activities involving the generation of energy for which a Feed-in Tariff is receivable to be eligible for social investment tax relief (SITR), and provides a power to use secondary legislation to amend the activities that are not eligible for SITR. The legislation provides for different provisions to take effect at different times.

DETAILS OF THE SCHEDULE

Part 1

2. Paragraph 1 introduces new section 257MW of the Income Tax Act 2007 (ITA 2007). The power allows the list of activities that are excluded from qualifying for SITR to be amended by regulations. The new power allows regulations to take effect retrospectively (but no earlier than 6 April 2015) where the activities become newly eligible for the SITR, that is, where the regulations are wholly relieving.

3. Subsection (4) of new section 257MW provides for regulations made under this section to be combined in the same statutory instrument with orders made under other powers. For example, section 200 and section 311 of ITA 2007 allow the list of excluded activities for EIS (and SEIS by virtue of section 257DA of ITA 2007) and VCTs respectively, to be amended by order. It will be possible to use one statutory instrument to amend the excluded activities for all four schemes at the same time.

Parts 2 and 3

4. Parts 2 and 3 of the Schedule exclude from the EIS, SEIS (by virtue of section 257DA of ITA 2007) and VCTs companies generating power whose activities involve anaerobic digestion or hydroelectric power for which a government subsidy is obtained.

5. The provisions also exclude activities where the generation of the electricity is carried on under a Contract for Difference, a new government subsidy that will replace Renewables Obligations Certificates (ROCs) and Renewable Heat Incentives (RHIs) in due course. Activities involving ROCs and RHIs are already excluded activities for the purposes of the venture capital schemes.

6. The changes in Parts 2 and 3 will take effect from 6 April 2015.

Part 4

7. Part 4 of the Schedule makes further provision on excluded activities for the EIS (and the SEIS by virtue of section 257DA of ITA 2007) and VCTs. However, unlike the changes in Parts 2 and 3 of the Schedule, the changes in Part 4 will take effect on a date specified by Treasury regulations.

8. Paragraphs 10 and 11 of the Schedule make provision to remove the exception that currently allows all types of subsidised energy generation activities by certain types of community organisations to qualify for the venture capital schemes.

9. The effect of paragraphs 10 and 11, taken together with Parts 2 and 3 of the Schedule, will be to exclude all activities involving subsidised energy generation from the EIS, SEIS and VCTs.

10. Paragraph 13 of the Schedule makes provision to amend the list of excluded activities for SITR. The export or generation of electricity subsidised by way of a Feed-in Tariff will no longer be an excluded activity.

BACKGROUND NOTE

11. The purpose of these provisions is to:

- exclude from the venture capital schemes (EIS, SEIS and VCTs) companies that can currently benefit from government subsidies on activities involving the generation of energy; and,
- extend the activities allowed under SITR once State aid clearance for the enlargement of SITR is received.

12. Subsidised energy generation activities involving anaerobic digesters, hydroelectric power and Contracts for Difference will be excluded from the venture capital schemes with effect from 6 April 2015.

13. However it is the Government's intention that the special provisions for community groups involved in subsidised energy activities, to qualify under the venture capital schemes, will remain in place until State aid clearance is received for the enlargement of SITR.

14. When State aid clearance is received for the enlargement of SITR, the Government intends to introduce regulations to bring into effect the provisions of this Schedule to:

- exclude community energy activities from the venture capital schemes; and,
- allow community groups that would be eligible for SITR, but for the fact that they are carrying out excluded activities involving the generation of energy for which a Feed-in Tariff is due, to become eligible for SITR.

15. When State aid clearance for enlargement of SITR is received, it is the Government's intention to use the power in new section 257MW of ITA 2007 to allow community organisations carrying out small-scale agricultural and horticultural activities, which will not be eligible for direct payments under forthcoming Community Agricultural Policy reforms, to qualify for SITR. Organisations with land holdings of less than 5 hectares in England and Wales and less than 3 hectares in Scotland and Northern Ireland would become eligible for SITR.

16. If you have any questions about this change, or comments on the legislation, please contact Cathy Wilson on 03000 536678 (email: cathy.wilson@hmrc.gsi.gov.uk).