Isle of Man Government

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A Consultation Document

Manx Enterprise Investment Scheme

Issued by:

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Index **Page**

Manx Enterprise Investment Scheme

Consultation Document

1. Background and purpose of this document

1.1 Background

The Isle of Man Government is proposing a number of initiatives to help grow the Island's economy. One such initiative being proposed is a tax incentive scheme: the Manx Enterprise Investment Scheme ("MEIS"). This scheme is designed to help smaller higher-risk trading companies, resident in the Isle of Man, to raise finance by offering income tax relief to investors who subscribe for new shares.

The MEIS is intended to encourage individuals to invest in eligible businesses, to be complementary to the Enterprise Development Scheme ("EDS") and it is anticipated that the additional finance raised will help the businesses to grow, resulting in additional jobs being created in the Island which, in turn, will lead to growth in the Isle of Man economy.

Under the scheme, a qualifying investor will be able to reduce their Isle of Man ("IOM") income tax liability for a tax year by subscribing for MEIS-qualifying shares.

The maximum income tax relief ("MEIS relief") available for an individual in a tax year will be £20,000; this will require the individual to have subscribed for £100,000 of qualifying shares during the tax year (these amounts will be doubled for jointly assessed couples). An individual's tax liability can be reduced to £0 as a result of MEIS relief, but any excess MEIS relief will be lost.

To ensure that MEIS relief meets its objective, certain criteria must be met by both the company and the investor prior to the relief being granted. In addition, it should be noted that income tax relief will be clawed back unless certain criteria continue to be met for the three years following the date of share issue. The proposed criteria are set out in detail in section 3 of this document.

No tax relief is available to a company under MEIS.

It is proposed that Treasury will make available a maximum amount of relief to be granted annually under the scheme on a first come first served basis. This amount will be reviewed annually as part of the Budget.

1.2 Purpose of this document

The purpose of this consultation document is to:

- provide further details on the proposed Manx Enterprise Investment Scheme; and

- invite comments and suggestions on the proposed scheme.

2. Outline of Scheme

2.1 MEIS tax relief

An individual who subscribes for shares in a MEIS-qualifying company will receive a reduction in their tax liability of 20% multiplied by their investment in qualifying shares in that tax year.

The minimum investment an individual can make in qualifying shares in a tax year is £10,000 while the maximum investment in a tax year is £100,000. These amounts refer to investment in an individual company and are doubled for jointly assessed couples. The maximum tax relief for an individual is therefore £20,000 (being 20% x £100,000), while for a jointly assessed couple it is £40,000.

> Question 1 - Do you consider that the tax relief is set at a level which will incentivise individuals to subscribe for new shares in local MEIS-qualifying companies and encourage job creation and growth?

MEIS relief cannot reduce the individual's tax liability for the year to less than zero, (ie it cannot create a tax refund). In addition, there are no provisions for the carry forward or carry back of MEIS relief – it will only be available in the tax year in which the MEIS-qualifying shares are subscribed. The relief will be included in the tax computation as the final tax reduction after all other tax reliefs and deductions have been applied, eg mortgage interest relief.

MEIS relief will be clawed back if the investor sells the qualifying shares within three years of the date of subscription or if the investor or company cease to meet the qualifying conditions within those three years. In such a case the tax will be treated as being due on the original due date and interest will be charged accordingly. However, the individual will not have MEIS relief clawed back if they die or cease residence within three years of the investment if all other criteria continue to be met. Similarly, if the company enters liquidation for general commercial reasons during the three years following the date of share issue, there will be no claw back of the relief.

The MEIS-qualifying company does not receive any tax relief as a result of the scheme.

2.2 The company

2.2.1 <u>Applying for MEIS approval</u>

A company will be required to apply for MEIS-approval prior to issuing MEIS-qualifying shares. The Department of Economic Development ("DED") will be responsible for assessing whether the company meets the MEIS criteria based upon an application form, accounts and business plan provided by the company.

To apply for approval the company must download a MEIS application form from the Income Tax Division's website and send the completed form to DED.

DED will review the application to determine whether the company meets the initial MEIS criteria and must provide a response to the application within 10 working days, whether this is a request for further information or confirming or rejecting MEIS approval.

Where DED consider that the qualifying criteria are met, they will issue the company with a MEIS reference number. However, it should be noted that this initial approval from DED only confirms that the company meets the MEIS conditions at the approval date; the company must ensure that it continues to meet the relevant criteria for three years after the date of issue of shares to ensure that MEIS approval is not withdrawn.

2.2.2 Issuing MEIS-approved shares

Following approval, qualifying shares must be issued within six months of the approval date in order to be considered valid. DED will issue the company with MEIS certificates that the company must complete and provide to each investor, confirming the subscription of qualifying shares. A copy of all MEIS certificates issued to investors must be submitted by the company to the Income Tax Division ("ITD") within 30 days of the share issue – approval can be withdrawn if this requirement is not met.

2.2.3 Ceasing to qualify for MEIS

If a company ceases to meet the MEIS-qualifying criteria within three years of a qualifying share issue, it should notify ITD within 30 days of the event which has resulted in the company no longer meeting the conditions. To do this the company should download a notification form from the income tax website and send the completed form to ITD. A penalty of up to £250 for late filing and £500 for filing the form six months' late can be imposed.

2.2.4 Changes to corporate income tax return form

To reflect the introduction of MEIS, an additional section will be inserted into the corporate income tax return. The new section will ask the company to confirm whether it has issued MEIS-qualifying shares within the three years prior to the first day of the accounting period. If this is the case a number of additional questions will need to be answered by the company to confirm that the relevant MEIS criteria are still being met. In addition, the company's tax return will require any loans to shareholders to be disclosed, irrespective of the shareholding of the investor.

2.3 The investor

2.3.1 Claiming MEIS relief

When an individual makes an investment in qualifying MEIS shares they will receive a certificate from the company confirming the amount of their qualifying share subscription. Should the investor wish to claim MEIS relief, they must make the claim in their income tax return for the tax year in which they subscribed for the shares and must file the tax return on time (as per section 62(1) Income Tax Act 1970). A copy of the MEIS certificate provided by the company must be attached to the return for a valid claim. Upon receipt of the return, ITD will check that the certificate provided by the individual matches the certificate provided by the company before income tax relief is given.

2.3.2 Ceasing to qualify for MEIS

MEIS relief will be clawed back if the investor does not continue to meet the qualifying criteria for three years from the date of share issue and the investor must notify ITD of any such change in circumstances using the notification form mentioned in section 2.2.3 above. Where MEIS is clawed back, the original tax assessment in which MEIS was claimed will be reissued to exclude MEIS, and any additional tax, plus interest, will be treated as being due from the original tax due date. Similarly, if the company ceases to meet the qualifying criteria during the three years following the date of the share issue, ITD will also amend the investor's assessment in the same way.

2.3.3 Tax credits

No tax credits will be available to offset the tax payment on any dividends paid by the qualifying company.

3. Criteria for tax relief

To ensure that MEIS meets its objective, there are a number of criteria which must be met, both by the company issuing the shares and by the investor, for MEIS relief to be available. To avoid the MEIS being used only for tax planning purposes, some criteria must also be met for a period prior to and/or following the share issue.

3.1 Criteria for company

3.1.1 Criteria for company – General

The company must meet the following general criteria at the time the shares are issued:

a) The company must meet the eligibility criteria as defined in paragraph 1.2.1 of Financial Provisions and Currency Act 2011 Enterprise Development Scheme 2015 - Enterprise Development Scheme Guidance at the time of the investment.

b) The company must be IOM-resident for income tax purposes (under section 2N of the Income Tax Act 1970) from the date of the share issue and for the next three years.

c) The company must not be listed or have any arrangements in place for it to become listed at the date of the share issue. For these purposes, a company that is listed on AIM (the Alternative Investment Market) is considered to be a listed company.

d) The company must not be controlled by another company ("control" is defined as more than 50% of the company's shares being owned by another company).

e) The company must be, and must remain, up-to-date with all income tax, VAT and National Insurance contribution payments and returns for the three year period following the date of the share issue.

f) Any dividends paid by the company within three years of the share issue (where a reserves analysis has been completed) must be paid out of Box 1 reserves. Where a reserves analysis has not been completed, the dividends will be deemed to have been paid out of Box 1 reserves.

Question 2 - Do you consider that the above criteria are sufficient to ensure the MEIS meets its objectives and is not used for tax planning?

3.1.2 Criteria for company – Shares issued

Eligibility criteria need to be set for the shares issued to the investor to ensure that no special rights are attached to the shares which will reduce the risk of the shares issued. These will help to ensure that MEIS meets its objectives and is not used only for tax planning.

a) The shares issued must be new full risk ordinary shares. The shares must be fully paid up prior to issue. The shares cannot be redeemable or carry preferential rights (eg cumulative dividends/rights on winding up etc).

b) There must be no arrangements in place for the repurchase of the shares from the investor either prior to the subscription of the shares or within three years from the date that the shares are issued.

c) There must be no arrangements in place to protect the rights of the investor. The issued shares must be full market risk.

d) The maximum value of MEIS qualifying shares that a company can issue within a 12 month period is limited to £1m (being the cost of the shares plus any share premium paid). This means that investment in one MEIS-qualifying company can result in a maximum tax relief of £200,000 per year if all investors were eligible for MEIS and received full tax relief for their investment in the MEIS-qualifying shares.

This criterion does not mean that only £1m of shares (being shares plus share premium) can be issued within a 12 month period. The company is not limited in the number of shares that can be issued in a 12 month period, however, only £1m of issued shares can be deemed to be MEIS-qualifying shares and the MEIS criteria must be met at the date that these qualifying shares are issued.

e) Qualifying shares must not be issued under any 'reciprocal' arrangements, ie where company owners agree to invest in each other's companies in order to obtain tax relief.

f) The investor will not be able to receive distributions as a result of a reduction in share capital or share premium reserves (or the equivalent reserves) within three years from the date of the share subscription.

Question 3 – Are there any other share criteria you believe should be included?

3.2 Criteria for investor

3.2.1 Criteria for investor- General

The investor needs to consider whether they will qualify for MEIS relief. The criteria to be satisfied by a qualifying investor are:

a) The individual must be IOM-resident for income tax purposes for the whole of the tax year in which the shares are purchased.

b) The individual must not be a tax capped individual for the year in which the shares are purchased.

c) The individual must be purchasing shares on their own behalf, not as a nominee.

d) An investor who makes a claim for MEIS relief, or a person connected to that investor (a "connected person"), must not be an employee or director of the company at the time of the share issue nor for the period two years before and three years after the share subscription.

However, to ensure that a company is not prevented from benefiting from the knowledge and experience of a "business angel", an investor, or a person connected to that investor, can become a director of the company after the investor has purchased MEIS-qualifying shares without relief being clawed back from the investor provided director's remuneration is paid to the director and the remuneration (including all benefits) is reasonable and is set at the market value rate. The "business angel" cannot have any other connection to the company if they are to meet this "business angel exemption".

The definition of "connected person" is set out in section 119C of the Income Tax Act 1970.

e) An investor must not have any arrangements in place to sell the shares at any time.

f) The investor must have subscribed for the shares for genuine commercial reasons and not as a part of a scheme or arrangement the main purpose or one of the main purposes of which is the avoidance of tax.

Question 4 - Do you consider the general investor criteria to be adequate and appropriate?

3.2.2 Criteria for investor- Connection by financial interest in company

Criteria are required to ensure that the investor is not connected to the company in the period two years prior to the share issue or three years after the share issue. The criteria relating to the investor's financial interest in the company are as follows:

a) The investor must have less than 30% ownership (when taking into account their ownership and the ownership of connected persons) of any of the following: ordinary shares, assets on winding up, loans, voting power.

The only exception to the above is in the period between the date of incorporation to the earlier of the date the company first issued shares (other than the founder shares) and the date that the company first began to trade.

b) The investor, or any connected person, must not have received a loan from the company or group which would not have been made, or would not have been made on the same terms, were it not for the MEIS investment.

c) The investor, or any connected person, must not receive any payments or value from the company except on commercial terms. This includes, but is not limited to, buying goods from the company or selling goods to the company and any consultancy fees paid by the company.

d) The qualifying company must not be linked to an existing company of a connected person.

Question 5 - Do you think these “connection” criteria are sufficient or are there any others you believe should be included?

Question 6 - Would you use the MEIS to subscribe for shares in an Isle of Man company, and/or would you advise a client to do so?

4. Publication of data

It is proposed that each year the Treasury will publish the following -

- the amount of revenue forgone attributable to the scheme;
- the names of companies that have benefited from the scheme and the value of investment generated;
- the number of additional jobs in each company since the investment.

5. Anti-avoidance

The Income Tax Act 1970 already contains a general anti-avoidance provision which will be used to prevent MEIS relief being granted where it is considered that the investment is not being made for commercial reasons (eg where the shares are not issued for the purpose of business growth). In addition, a number of key risks will be managed by the introduction of appropriate anti-avoidance legislation.

6. Guidance

The Assessor recognises the importance of clear guidance and will ensure that advice and assistance are made available.

It is proposed that guidance will be available on the Division's website. Officers within the Division will also be available to assist.

7. Comments and suggestions

Responses to the questions raised in this document, together with any comments or suggestions concerning the proposed Manx Enterprise Investment Scheme, would be welcomed.

8. Submissions

Anyone wishing to submit a response to this consultation is invited to do so by 5 February 2016.

Responses should be sent to:

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In any consultation exercise the responses received do not guarantee that changes will be made to what has been proposed.

Following the consultation period, the responses will be reviewed and the conclusions, together with a summary of the comments received, will be published.

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