

The Seed Capital Scheme: Tax Refunds for New Enterprises

Background

THE BUSINESS EXPANSION SCHEME (BES) has been in operation since 1984 and will continue until 31 December, 2006. The scheme gives income tax relief to those who invest capital in qualifying Irish companies thus enhancing the ability of companies to attract outside investment. The tax relief is given for the year in which the investment is made.

The scope of the Scheme has widened to provide a refund of tax *already* paid by an individual who sets up and takes employment in a new qualifying business. The relief is known as the **Seed Capital Scheme and will continue until 31st December, 2006.**

The legislative basis for the Scheme is contained in Part 16 Taxes Consolidation Act, 1997 (as amended).

Introduction

If you are an employee, an unemployed person or were made redundant recently and are interested in starting your own business you may be entitled to avail of the tax refund available under the Seed Capital Scheme.

An employee who leaves employment and invests by means of shares in a company which carries on a new business, may claim a refund of income tax paid in previous years. An unemployed person may also avail of this facility.

The Refund

- You could receive all the income tax you have paid over six years, if your investment is big enough.
- You can select the tax years for which you may claim refunds from any or all of the six years prior to the year of investment. **Your investment must be claimed up to the extent of your total income in each of the selected years (subject to a max. of €31,750). There is no facility available where the investment can be spread over a number of years so as to utilise personal allowances in each year.**
- **For each of the selected years, the refund is limited to the tax you have paid, with an upper limit in any year of the tax paid on €31,750.**
- The refund may be claimed immediately the company starts to trade.
- If you have already received BES relief for any of the six years selected the amount of the relief available to you in that year is the difference between €31,750 and the amount of the original BES investment.
- You may obtain a refund in this manner for two investments in the company made within a three year period. Both investments, however, **must** be made in the same company and both must be made after 2 June, 1995. Your total investment is subject to an overall maximum refund of the tax paid on €82,240.

Appendix 1 to this leaflet shows an example of how a refund is calculated. To calculate your refund **you must take account of your own tax free allowances and other reliefs if any.**

What Conditions Apply?

The Investor:

- The scheme is designed for those who are or were in PAYE type employment. To ensure that this intention is achieved the sources of your income over the four tax years immediately before the year in which you invest in the company are reviewed. In the tax year immediately before the year in which you invest, your income may come from any source (that is, it may be from self-employment, rental, investment, PAYE or other). *In the other three tax years, your non PAYE income should not exceed the lower of €25,000 or your total PAYE type income.*

- These income limits do not apply in the case of an individual who invests in a company which is set up to trade on an exchange facility established in the Custom House Docks Area.(now no longer a qualifying trade)
- **You must enter into a full-time employment contract for at least one year with the company as an employee or a director** starting either within the tax year in which the investment is made or if later, within 6 months of the date on which the relevant investment is made.
- Your investment in the company may be made in two stages, the second investment must be made within two years following the tax year in which your first investment is made. The facility to claim relief under the scheme in respect of a second investment is only available to investors who make both investments in a qualifying company on or after 2 June, 1995.
- It should be noted that where a second investment is planned the scheme will only be available up to 31 December,2006.
- You must buy shares in the company.
- You must acquire at least 15% of the issued share capital of the company and you must maintain the level of your shareholding at this percentage for at least two years, even if the share capital of the company should expand. This condition will apply in the case of both a first and a second investment.

The Company:

- The company must be set up with the intention to carry on qualifying trading operations. Qualifying trading operations are
 - (1) the manufacture of goods
 - (2) the operation of certain tourist traffic undertakings
 - (3) internationally traded services
 - (4) certain activities which have the potential to become internationally traded services
 - (5) the cultivation of mushrooms
 - (6) the micro-propagation of plants and plant cloning
 - (7) the cultivation of horticultural produce in greenhouses
 - (8) research and development activity which is undertaken with a view to carrying on certain of these qualifying trading operations and which are certified as such by an industrial development agency
 - (9) commercial research and development activities
 - (10) The production, publication, marketing and promotion of a qualifying musical/video recording
- The company must obtain a certificate from an appropriate body or person certifying that the qualifying trading operations to be carried on by the company will be a bona-fide new venture, which having regard to certain criteria may be eligible for grant aid or financial assistance from the certifying body or person. The grant aid or financial assistance requirement does not apply to the activities listed at (6) above.

It should be noted that the actual payment of a grant or the receipt of an equity investment from one of the industrial development agencies, is required in the case of internationally traded services. In the case of activities which have the potential to become internationally traded services, an industrial development agency must have provided financial support of not less than €2,540 towards the carrying out of a feasibility study by a person approved of by the agency into the commercial viability of the services to be rendered.

Who Certifies What Activities?

- **Manufacturing generally**
Enterprise Ireland, SFADCo, Udaras na Gaeltachta or County Enterprise Boards, as appropriate.
- **Fish farming (Aquaculture) and fish processing**
An Bord Iascaigh Mara.

- **Internationally traded services and services with the potential to be internationally traded services**
Enterprise Ireland, SFADCo, Udaras na Gaeltachta or County Enterprise Boards, as appropriate.
- **Tourist traffic undertakings**
Failte Ireland.
- **Micro-propagation of plants, plant cloning, mushroom and horticultural cultivation**
The Minister for Agriculture and Food.
- **Activities to be carried on in an exchange facility established in the Custom House Docks Area**
IDA - Ireland.
- **Commercial research and development**
Enterprise Ireland, SFADCo, Udaras na Gaeltachta, or County Enterprise Boards, as appropriate.
- **Musical/Video recordings by a new artist produced in the State**
The Minister for Arts, Sport and Tourism.

Conditions To Prevent Abuse

- **You must not within the 12 months before your first investment in the company, have held either directly or indirectly, more than 15% of the share capital or of the loan and share capital of any other company, or 15% of the voting power in any other company.**
- However, this prohibition is waived where you own more than 15% of only one other company provided that:-
 - the turnover of the other company in each of that company's three accounting periods prior to the company's accounting period in which the investment is made in the seed capital company did not exceed €127,000, and
 - the other company is a trading company (other than a company trading in land or financial services).

This prohibition is also waived where you own more than 15% of a shelf or dormant company.

- The company must not have any special trading arrangements with your former employer. Normal business transactions are, however, acceptable, provided these are conducted on the same terms as with any other unrelated company.

The Seed Capital Scheme and the BES

The Seed Capital Scheme forms part of the BES. If you think that you may qualify for the Seed Capital Scheme it is also necessary for you and your company to comply with the requirements of the BES. The most important of which are

- A company that raises both Seed Capital and BES may raise a maximum of €1,000,000, up to a maximum of €750,000 in any one six-month period.
- The shares issued in respect of your investment must not carry any preferential rights to dividends, assets or redemption.
- **You must not dispose of the shares for at least 5 years.**
- You must not enter into any agreement, arrangement or understanding which could reasonably be considered to eliminate the risk from your investment.
- There must be no attempt to pass back your investment to you.
- The company must be an unquoted company resident in the state or is resident in the European Economic Area with an establishment in the state carrying out qualifying activities.
- The company must be regarded as a micro, small or medium-sized enterprise within the European Commission definition for the relevant period.
- The company must not be regarded as a firm in difficulty for the purposes of the Community Guidelines on State Aid for rescuing and restructuring firms in difficulty
- The company must use the amounts invested for the purposes of qualifying trading operations.
- At least 75% of the income of the company must derive from qualifying trading operations.

- The company (unless it has qualifying subsidiaries) must not control or be controlled by any other company and it must not carry on a trade which is similar to another trade where both trades are under common control.

NO REFUND WILL BE GIVEN IF ANY CONDITION OF THE SCHEMES IS NOT FULFILLED.

Claiming A Refund

The refund of tax in respect of an investment made can be claimed as soon as the company has obtained the appropriate certificate from the relevant agency and commences to trade. A refund will normally be made within four weeks of receipt of an **adequately** completed claim. You can help us to meet this deadline by supplying full information.

What You Have To Do

- Complete an application form (which is available from the appropriate agency) for a certificate and submit it to that agency.
- If the agency is satisfied that the company meets its requirements the necessary certificate will be issued if the company has already been incorporated.
- If the company is not yet incorporated a conditional certificate will be issued.
- The agency will also issue the tax refund application forms RINE C and RINE I.
- When the company has been incorporated, all the shares have been issued (including those you will purchase yourself) and the company has commenced trading, the forms RINE C and RINE I should be completed and submitted.

Further Investments

If you wish to expand your company in the future you may be entitled to BES relief in respect of any further investment which **you** may make in the company.

In addition, BES relief may be available to any outside investors you may wish to take into the company provided the investments and the investors comply with the requirements of the BES. You must, notwithstanding any outside investment in your company, ensure that the continuing conditions of the Seed Capital Scheme are not contravened.

However, this option is **not** available in the case of trading operations which qualify for the Seed Capital Scheme but not the BES. The activities concerned are:-

- trading on an exchange facility established in the Custom House Docks Area, and
- potential internationally traded services.

Forms To Be Completed	
RINE C	Supplies information concerning the company.(form supplied by the certifying agency)
RINE I	<p>Supplies information concerning the individual investor.(form supplied by the certifying agency)</p> <p>A separate RINE I form must be completed by each investor claiming a refund.</p> <p>Each RINE I form should be accompanied by relevant P45s/P60s, Form P21 (Balancing Statements), copies of Form B5 (proof of share issue and receipt), Capital Duty paid, the company's Bank Statement showing the amounts paid in respect of qualifying shares and certificate of incorporation. Also required is a bona fide new venture certificate from the certifying agency plus a copy of the grant including evidence of payment(where feasibility/employment grants are required)</p>

- Send the completed forms with the certificates to:

Office of the Revenue Commissioners
Business Incentives
Direct Taxes Interpretation and International,
1st Floor Stamping Building,
Dublin Castle,
Dublin 2.

Further information can also be obtained from the above address or by telephoning 7024107. Alternatively you might consult your professional adviser who should be able to provide any further details you require. The Industrial Development Agencies/County Enterprise Boards may also be willing to help.

IMPORTANT

**IF THE CONTINUING CONDITIONS OF THE
SCHEME ARE BROKEN THE REFUND MAY BE
WITHDRAWN IN WHOLE OR IN PART**

This leaflet does not purport to be a legal interpretation of the provisions on which these reliefs are based, nor is it intended as a comprehensive guide. It should be used for general information purposes only.

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Appendix (1)

Example:

Jack Gere who has been made redundant and with his redundancy money sets up a manufacturing company on 19th September, 1998 and invests £70,000 in £1 shares in it. The company has received advance approval from the Appropriate Agency/County Enterprise Boards etc. and has commenced trading. Jack owns 70% of the issued share capital and has taken up full-time employment in the company.

Jack's income and tax payments for the previous five years were as follows:

	93/94	94/95	95/96	96/97	97/98
	£	£	£	£	£
Salary	25,000	27,000	30,000	34,000	36,000
Other Income	Nil	1,000	3,000	2,000	2,500
Tax Paid	8,823	10,069	12,320	13,650	14,526

Jack decided to claim the Seed Capital Relief on his **£70,000** investment against his total income for the tax years **1993/94, 1994/95 and 1995/96**. He is single and entitled to the PAYE and PRSI allowance.

The relief is calculated as follows:

Income	1993/94	1994/95	1995/96
	£	£	£
Salary	25,000	28,000	33,000
Other Income	Nil	1,000	3,000
Total	25,000	28,000	33,000
Less Seed Capital Relief	25,000	25,000	20,000
Income Net of Relief	Nil	3,000	13,000
Less Tax Free Allowances	3,261	3,436	3,440
Taxable Income	Nil	Nil	9,560
Tax Due – A	Nil	Nil	2,720
Tax Actually Paid – B	8,823	10,068	12,320
Refund due (B – A)	8,823	10,068	9,600

On 1st May, 1999 Jack decides to make a second investment. He invests a further £45,000 in £1 shares. On this occasion he decides to claim the relief in **1996/97 and 1997/98**.

Reief for his second investment is calculated as follows:

Income	1996/97	1997/98
	£	£
Salary	34,000	36,000
Other Income	2,000	2,500
Total	36,000	38,500
Less Seed Capital Relief	25,000	20,000
Income Net of Relief	11,000	18,500
Less Tax Free Allowances	3,450	3,700
Taxable Income	7,550	14,800
Tax Due – A	2,039	4,926
Tax Actually Paid – B	13,650	14,526
Refund due (B – A)	11,612	9,600

Overall, Jack has been able to avail of **£49,704 in tax refunds** to help his company prosper in the new millennium.

Appendix (2) Here is an example of someone making a Seed Capital investment of €175000.00 in 2003 spread over the previous 6 years.

	1997/98	1998/99	1999/00
Salary	£40,000	£42,000	£40,000
Rental	2,000	Nil	1,500
Income			
Gross Income	42,000	42,000	41,500
Expenses	<u>200</u>	<u>200</u>	<u>200</u>
<i>Total Income</i>	<i>41,800</i>	<i>41,800</i>	<i>41,300</i>
Seed Capital Relief	<u>£25,000</u>	<u>£25,000</u>	<u>£25,000</u>
	<i>16,800</i>	<i>16,800</i>	<i>16,300</i>
Personal Allowance	2900	3150	
<i>Paye Allowance</i>	800	800	
	<u>3700</u>	<u>3950</u>	
<i>Taxable income</i>	<i>13,100</i>	<i>12,850</i>	
	9900 x 26%	10,000 x 24%	14,000 x 24%=3360
	3200 x 48%	2850 x 46%	2300 x 46%
			Tax Due 4418.00
			Personal credit 1008
			Paye credit 240
Tax Due	4110.00	3711.00	3170.00
Tax Paid (per P60)	<u>16,110.00</u>	<u>15,211.00</u>	<u>14,670.00</u>
Refund	<u>£12,000</u>	<u>£11,500</u>	<u>£11,500</u>

		2000/01	2001 (short tax year)	2002
Salary		£37,000	£36,640	€46,250
Rental		1000	Nil	1500
Income				
Gross Income		38,000	36,640	47,750
Expenses		<u>200</u>	<u>148</u>	<u>200</u>
<i>Total Income</i>		<i>37,800</i>	<i>36,492</i>	<i>47,550</i>
<i>Seed Capital Relief</i>		<u>£25,000</u>	<u>£18500</u>	<u>€20,000</u>
<i>Taxable Income</i>		<i>12,800</i>	<i>17992</i>	<i>27,550</i>
Tax Due	12,800 x 22%= 2816.00		14,800 x 20% = 2960 3192 x 42%= 1340.64	27,550 x 20% = 5510.00
<i>Total Tax Due</i>		<i>2816.00</i>	<i>4,300.64</i>	<i>5510.00</i>
<i>Less Tax Credits</i>				
Personal	1034		814	1520
PAYE	220		296	660
Tax Paid (per P60)	11,638	<u>12,892.00</u>	10,960.64	11631.00
Refund		<u>£10,076.00</u>	<u>£7770.00</u>	<u>€8301.00</u>