HM Treasury

Autumn Budget 2017: Patient Capital Review

BVCA Town Hall, 9 January 2018

Context

- Background to the Review and role of the industry panel
- The consultation and responses
- Autumn Budget response

HMG commitments (1)

The Budget now announces an action plan to unlock over £20 billion to finance growth in innovative firms over 10 years by:

- *Establishing a new £2.5 billion Investment Fund incubated in the British Business Bank with the intention to float or sell once it has established a sufficient track record. By co-investing with the private sector, a total of £7.5 billion of investment will be supported.*
- *Significantly expanding the support that innovative knowledge-intensive companies can receive through the Enterprise Investment Scheme (EIS) and Venture Capital Trusts (VCTs) while introducing a test to reduce the scope for and redirect low-risk investment, together unlocking over £7 billion of new investment in high-growth firms through EIS and VCTs.*
- *Investing in a series of private sector fund of funds of scale. The British Business Bank will seed the first wave of investment with up to £500m, unlocking double its investment in private capital. Up to three waves will be launched, attracting a total of up to a total of £4 billion of investment.*
- *Backing first-time and emerging fund managers through the British Business Bank's established Enterprise Capital Fund programme, supporting at least £1.5 billion of new investment.*
- *Backing overseas investment in UK venture capital through the Department for International Trade, expected to drive £1 billion of investment.*

HMG commitments (2)

We will support long-term investment by:

- *The Pensions Regulator will clarify guidance on how trustees can include investment in assets with long-term investment horizons, such as venture capital, infrastructure and other illiquid assets in a diverse portfolio. HM Treasury will establish a working group of institutional investors and fund managers to increase the supply of patient capital, including tackling continuing barriers holding back Defined Contribution pension savers from investing in illiquid assets.*
- *Changing the qualifying rules in Entrepreneurs' Relief to remove the disincentive to accept external investment and consulting on the detailed implementation of that change.*
- *Carrying out a feasibility study on a new guarantee programme modelled on the US 'Small Business Investment Company' programme.*

HMG commitments (3)

And we will promote successful investment in all parts of the economy by:

- *Launching a commercial investment programme run by the British Business Bank to support developing clusters of business angels outside London.*
- *Identifying ways to tackle barriers faced by female-led firms in accessing venture capital through new behavioural research commissioned by the British Business Bank.*
- *Working with businesses, lenders, insurers, the British Business Bank and the Intellectual Property Office to overcome the barriers to high growth, IP-rich firms, such as those in the creative and digital sector, using their intellectual property to access growth funding.*

Tax: consultation responses

- The importance of the schemes in supporting the early stage investment market.
- Calls for the extension of limits. Knowledge intensive companies (KICs) were highlighted by some, including Sir Damon’s Industry Panel.
- Continued concerns over use of the schemes for tax planning and capital preservation strategies.
- A large number of responses from the Film and Television industries.
- Calls for simplification and improvements to HMRC’s Advance Assurance service.
- Mixed responses on SEIS.

Government response

Policy issue	Action	Scheme	Implementation dates (subject to State aid)
Annual company limit for KICs	Doubled to £10m	EIS and VCTs	6th April 2018
Annual investor limit for KICs	Doubled to £2m	EIS	6th April 2018
First commercial sale difficult to identify for KICs	Age flexibility (turnover test)	EIS and VCTs	6th April 2018
Knowledge intensive EIS fund structure	Consultation	EIS	Consultation published Spring 2018
Capital preservation	Risk-to-capital preservation	EIS, SEIS, and VCTs	Royal Assent of Finance Bill / Advance Assurances from 4th December 2017

Risk-to-capital condition

- A principles-based test based on whether ‘having regard to all the circumstances existing at the time of the issue of the shares, it would be reasonable to conclude:

  - The company has objectives to grow and develop its trade in the long-term.
  - There is significant risk that there will be a loss of capital of an amount greater than the net investment return.’

- A gateway to the schemes, assessed first in any application.

Changes to VCT rules

Change	Implementation
VCT loans: unsecured, on commercial terms and justified above a 'safe harbour'.	Royal Assent of FB 2017-18
30% of funds invested within 12 months	Fundraises on or after 6 April 2018
80% of VCT funds invested in qualifying holdings	Beginning on or after April 2019
Reinvestment period for gains doubled from 6 to 12 months	April 2019
Removal of grandfathered provisions (see next slide)	April 2018

HMG will also review concerns that VCT status can be disproportionately imperilled.

Grandfathered provisions removed

Legislative reference	What will change	Funds protected
Paragraph 69 of Schedule 2, ITA 2007	Will apply the 'no guaranteed loans requirement' to VCT qualifying loans	Raised before 2 July 1997
Paragraph 70 of Schedule 2, ITA 2007	Will apply the "proportion of eligible shares requirement" to require minimum 10% by value of investment to be in shares	Raised before 2 July 1997
Paragraph 81 of Part 8 of Schedule 2, ITA 2007	Will cease to allow: property development; farming or market gardening; holding, managing or occupying woodlands, any other forestry activities or timber production; operating or managing hotels or comparable establishments or managing property used as an hotel or comparable establishment; operating or managing nursing homes or residential care homes, or managing property used as a nursing home or residential care home	Raised before 17 March 1998
Paragraph 3(6)(b) of Part 1 of Schedule 16 to the Finance Act 2007	Will apply a limit to the number of employees in a qualifying company (250/500)	Raised before 6 April 2007
Paragraph 12(b) of Schedule 11 to the Finance Act 2008	Will cease to allow: shipbuilding; producing coal; producing steel	Raised before 6 April 2007
Paragraph 6(2)(b) of Schedule 2 to Finance (No. 3) Act 2010	All new investments will count towards the 70% eligible shares condition (at least 70% of qualifying holdings by value must be shares, instead of 30% rule)	Raised before 6 April 2011

HMRC's Small Companies Enterprise Centre

- Work to digitise the advance assurance service, reducing the administrative burden for companies using the schemes.
- Improvements to written guidance on the advance assurance service, including a checklist of documents and information.
- No advance assurances for applications failing the risk-to-capital condition after 4th December 2018 (the date draft guidance was published).
- From 2 January 2018 HMRC have stopped providing advance assurances for speculative applications.
- Target of dealing with the vast majority of cases within 15 working days by Spring 2018.

4 December 2017

- HMRC published guidance on the risk-to-capital condition.
- HMRC began denying Advanced Assurances to investments that fail the condition.

6 April 2018

- Extension of EIS/VCT schemes for Knowledge Intensive Companies, and
- Changes to VCT rules covering grandfathering and speed of deployment come into effect.

Early 2018

- Royal Assent of FB17/18: Formal introduction of capital preservation test and regulation of VCT loans

Finance Bill 17/18

31st January

- HMRC accepting comments on draft guidance until the end of January.

Spring

- HMT launch consultations on Entrepreneurs' Relief (ER) changes and Knowledge Intensive Companies' EIS Fund.

6 April 2019

- Amendments to ER qualifying conditions come into effect as announced at AB18,
- Required qualifying holding for VCTs rises from 70% to 80% and,
- Reinvestment of gains period doubled

Late Spring 2018

- ER and EIS consultations end