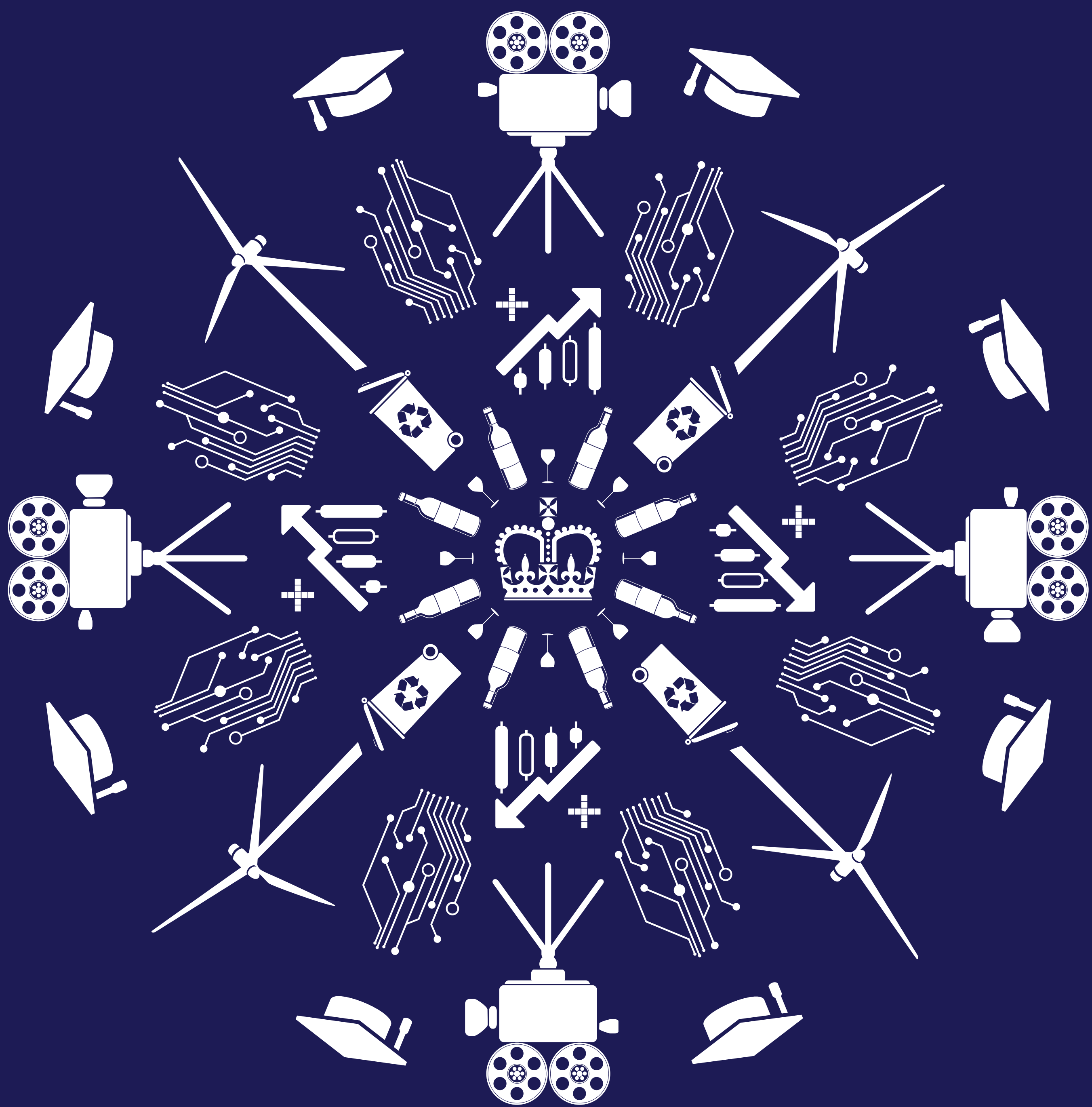
AiR 15/16

ALTERNATIVE INVESTMENT REPORT



ENDORSED CPD PROVIDER

EIS INDUSTRY REPORT 2015/16

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FOREWORD

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Welcome to our second industry report focused purely on the Enterprise Investment Scheme.

We wanted to follow up on the 2014 report by continuing to add something new for our readers, rather than covering the same ground as before, so this report will focus on a few key areas of interest.

There have been lots of changes over the last 12 to 18 months: changes to legislation; changes to pensions; the rise of crowdfunding; SEIS has been made permanent; higher limits for SITR are on the verge of being approved; new platforms are gaining traction with advisers; and more data on EIS is available than ever before. The industry is growing strongly and we are seeing new investors, advisers and providers all entering the market, as well as experienced players expanding their activities.

Taking a step back, documenting all of that activity in one place and assessing the nature of the changes are, we think, worthwhile activities. But while we are keen to assess and understand all of this excitement, it's worth remembering a few key fundamentals.

EIS remains all about channelling capital to small businesses that would struggle to raise finance otherwise. At the heart of it, the investments are simple equity stakes in businesses that hope to deliver on a plan, grow their value and pay investors back with a return that rewards them for the risk to which they have exposed themselves. When these businesses grow, we are all winners: investors earn returns, the businesses make profits and create jobs and the economy – the real economy, not the stock market – benefits.

My view is that this is the beauty of EIS. It's 'real' investing and we shouldn't lose sight of that. We think that more and more people are coming round to the benefits of EIS, and that the future is set for even more growth.

I hope you enjoy reading the report and that it becomes a useful reference tool for you. We are always keen to hear your thoughts on what else you would like us to cover and how we can develop this report.

Guy Tolhurst
Managing Director
Intelligent Partnership

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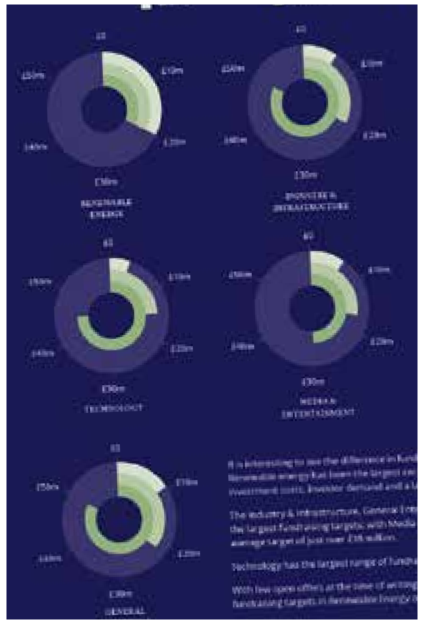

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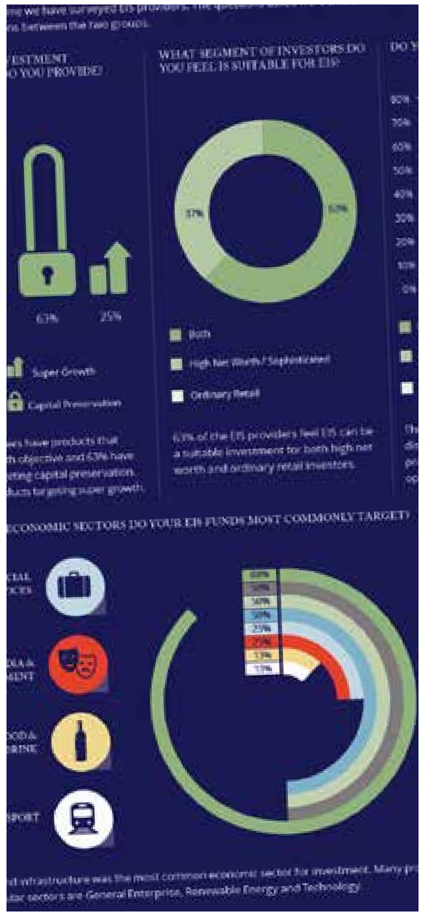

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AiR 15/16
ALTERNATIVE INVESTMENT REPORT

* Please note: unless otherwise stated, all charts and graphs have been provided by Intelligent Partnership

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AMPS

FSC is a non-profit international organisation established to promote the responsible management of the world's forests. Products carrying the FSC label are independently certified to ensure consumers that they come from forests that are managed to meet the social, economic and ecological needs of present and future generations, and other controlled sources.

OPENING STATEMENT

This has been another year of change for the EIS industry. We've had two Budgets that have ushered in modifications to the rules that govern the schemes, we've seen the end of subsidised renewable energy within EIS, the UK government has secured EU State Aid approval for the scheme, the SEIS has really gained traction and we've had a record year of fundraising.

The new rules introduced in the Budgets, which became law when the Finance Act was passed in November 2015, encourage investment into earlier stage companies. This is an area that the EIS has always specialised in and great opportunities to invest in exciting, fast growing companies that will be the giants of tomorrow can be found. The focus on high-tech firms, which have more generous provisions under the new rules, is especially welcome.

The EIS will also continue to support well-established, mid-market firms that are making significant changes to develop new products and services, or break into new markets. There is also a provision in the new rules for follow on investing. Firms that have previously received funding via tax-advantaged venture capital schemes can apply for new rounds of funding. However, investing in established firms that are over seven years old is now much harder than it was before, and the EIS Association will continue to lobby HM Revenue & Customs, HM Treasury, Government and Europe to ensure that they understand the importance of the EIS to mid-market firms as well as early stage firms.

The government has now secured EU State Aid compliance and the rhetoric coming from government is entirely positive. In all of our conversations with government, they indicate that they support the scheme and see it as a vital part of encouraging an entrepreneurial economy here in the UK. They have also indicated that they will seek further State Aid approval for replacement capital investments, allowing business owners to exit. With these changes now behind us and a sympathetic government, we can now look forward and hope for a period of stability in the regulations, allowing the EIS managers to get on with their work of raising and deploying funds to support exceptional businesses.

The mini-boom in investing in subsidised renewable energy via EIS has now come to an end, with the exclusion of 'peak-power' from the scheme on 30th November 2015 adding a note of finality. The EIS industry has been preparing for this moment for some time now and I believe that many of the new investors who have been introduced to EIS by investing in renewables will want to continue to invest in EIS opportunities after a positive experience, recycling their initial investments and investing new capital.

So the outlook is very strong. The SEIS is now gaining momentum, and we are seeing evidence that SEIS funding is being followed on by EIS funding, which demonstrates that the 'funding escalator' is working as it should, and small companies can be supported throughout their development. We've also had a record year for EIS fundraising, with £1.5 billion raised in 2013-14, supporting over 2,700 companies. Since inception, the scheme has raised over £12.2 billion and provided funding for nearly 23,000 companies. It's a great track record and I am delighted to be involved in supporting a scheme and investment sector that continues to do so much to support the UK economy.

Lord Flight,
Chairman of the Enterprise Investment Scheme Association

KEY FINDINGS

Research shows that **52% OF MPs** are unsure of whether the EIS is an effective policy to drive the growth

Since EIS was launched in 1993-1994, nearly **23,000 INDIVIDUAL COMPANIES** have received investment through the scheme

Almost all regions of the UK have increased in the amount of **EIS FUNDS** raised from 2010 to 2013, with the South East, East Midlands, Northern Ireland and the North West increasing **OVER 100%**

45 EIS INVESTMENT PRODUCT LAUNCHES in 2015

THE AVERAGE MINIMUM SUBSCRIPTION level is just under **£23,000**

THE AVERAGE FUNDRAISING TARGET is just under **£20 million**

(Slightly lower than previous years)

Only **6% OF NEW LAUNCHES** in 2015 were into **RENEWABLES**

(Down from 39% of launches in 2014)

35% OF PRODUCT LAUNCHES in 2015 were in the **MEDIA**

(Up from 17% of launches in 2014)

54% OF PRODUCTS OPEN for investment today are focused on **GROWTH** as opposed to capital preservation

THE AVERAGE TOTAL TARGETED RETURN for open offers is **127%***

GENERAL ENTERPRISE, TECHNOLOGY & MEDIA Are the three sectors seeking the most **FUNDRAISING**

91% OF ADVISERS WHO RECOMMEND EIS INVESTMENTS do so for the tax benefits as a primary reason and **76%** for their IHT benefits

*Where stated

INTRODUCTION

PURPOSE

We started reporting on the EIS industry because we could see that EIS was an asset class whose time had come, and that more advisers and investors were considering the sector than ever before. The figures have borne this out: in 2013/14 a record £1.6 billion was raised by 2,795 companies via the EIS (HMRC). So we think that it is important that advisers and investors have a resource to help them understand the EIS market and how it is changing and responding to this surge in interest.

That's the purpose of this second EIS Industry Report. We're not going to go over the same ground as the 2013/14 report and describe the scheme from inception, and we're only briefly going to look at the rules governing the scheme and the tax reliefs that are available. (For newer readers who do want to find out more about the history and context of the scheme and the rules that govern it, the 2014/15 report is available to download free on our website.)

Instead, we'll look at what has changed for the EIS industry in the last twelve months. What sort of investments comprise the market now, how newcomers and innovations such as EIS platforms have performed and what is the impact of new legislation going to be? We'll also explore some key areas in more depth: how to create recommended product lists or panels, and the types of investee companies that raise funds via EIS.

And we'll examine some of the issues that we know exercise advisers, such as charges, performance measurement and the transparency of the underlying portfolios.

Changes to legislation are something that are imposed on the industry from the outside, and have positive and negative impacts. In just the last twelve months we can see that changes to the UK pensions system have prompted increased levels of interest in EIS opportunities, whereas amendments to the rules governing qualifying companies will exclude popular EIS assets such as renewable energy. Our sense is that the industry is flexible enough, and has the intellectual capacity to cope with these kinds of changes, and we will discuss their impacts in depth in the report.

As with all of our reports, we've surveyed advisers, providers and investors to get a sense of how all of the stakeholders in the market are feeling at the moment and give us some qualitative as well as quantitative data.

So whether you are a seasoned EIS investor or somebody looking at this asset class for the first time, we think that this is invaluable information to help you get your arms around the whole-of-market. Readers of the report will be able to speak to their clients about EIS investment opportunities confident that they are up to date with the market and have the best possible guidance on how to approach the sector in hand.

ACKNOWLEDGEMENTS AND THANKS

We couldn't do this without the help and support of a number of third parties who have contributed to writing this report. Their contributions range from inputting into the scope, sharing data, giving us their insights into the market, providing copy and peer reviewing drafts. Some of them have contributed directly, and some of them were good enough to share their thoughts and ideas over coffee or at various conferences and events.

So a big thanks to: Adviser Home, Big Society Capital, Bovill, Bulletin Marketing, the EISA, Jason Butler, Jeff Cornish, Keith Robertson, Lenny Norstrand, PwC, RW Blears and various angel investor networks.

Their input is invaluable, but needless to say any errors or omissions are down to us.

We have relied upon MICAP for a lot of the data used in compiling the report. MICAP is now part of the same group of companies as Intelligent Partnership.

The report is made possible by our sponsors, who have contributed copy to the report on pages 47 to 57 and supported us by helping to meet production and printing costs. They are acknowledged in section two and three.

NOTE ON THE USE OF THIS REPORT

This report is not intended to be used to select specific products or investment providers and you should not rely on this report for your product selection process. The report is designed to help you understand the broader industry, how to approach the sector and what to look for when reviewing the market.

EXECUTIVE SUMMARY

How has the EIS market changed over the last twelve months? We think that most of the changes have been things that have been driven externally, rather than internally. Reforms to the UK pensions system are probably one of the biggest drivers of investment. Lower limits on the amounts that can be saved and the threat to higher rate tax relief (still in place at the time of writing) mean that higher earners need to find alternative tax-efficient investments, and this is encouraging many advisers and investors to consider EIS. We also find that EIS investment is being used in tax efficient decumulation strategies that are becoming more popular in the light of pension freedoms and the removal of compulsory annuity purchases.

Legislative changes to secure EU State Aid approval have had a bigger impact on the Venture Capital Trust (VCT) scheme. EIS investments were already focused on younger, high growth companies whereas company acquisitions and MBOs were much less common. Nevertheless, the new rules will have some impacts on EIS, and investing in the mid-market sized companies that qualify for EIS has become harder. The changes ensure that the scheme will remain directed at small, young, high growth companies. This could be considered a negative as it will affect some capital preservation EIS business models, or a positive from the point of view of ensuring the scheme directs capital to where it is needed most. Another positive is that the transition between SEIS and EIS funding has been smoothed out by the removal of the requirement to spend 70% of SEIS money before raising funds via EIS.

The end of the renewables story is another externally imposed change. Renewable energy products only make up 5% of the investment opportunities open today at the time of writing, compared to nearly 40% in the same period in 2014. The double benefit of being able to invest tax-efficiently into firms benefiting from renewables subsidies had been responsible for a large number of new products and subsequent investment inflows. Providers and investors both filled their boots. Now that the party is over we will have to wait and see where that money is going to go. Peak (or Reserve) Power investments were looking like a candidate that had similar features and could take the place of renewable energy, but as the Finance Bill worked its way through parliament this asset class was also excluded. However, many new advisers and investors have been introduced to EIS via renewables and we think that they will recycle that money as they exit their original investment and continue to introduce new money now they are more comfortable with the EIS sector.

There have also been some changes that have been driven internally by the EIS industry itself. The innovation of platforms to carry out research, due diligence and investment are making life easier for advisers and investors.

We've also noted a slight reduction in the number of open capital preservation EIS investments compared to the historical norm. This may well be attributed to the reduction in renewables, but the upshot is that there are more growth focused EIS to invest in than previously, at a time when the economy seems to be picking up. The average target level of return in open investments as stated in their investment memoranda has also ticked up compared to the historical average. One would expect that this is linked to the higher number of growth focused EIS, but actually there are some real anomalies in these figures: some investments with a stated objective of capital preservation are targeting higher returns than growth EIS. Perhaps the take-away is this: discuss the stated target level of returns with the investment provider and understand how they plan to achieve them.

Finally, establishing a performance track record and charging structure on a basis that allows meaningful comparisons between products remains as elusive as ever. Our guess is that as long as there are big drivers for increased EIS inflows (pension limits, IHT planning, more sophisticated clients), the EIS industry won't be overly concerned with these issues. There are good reasons why performance measurement is difficult and charges are high, and therefore every offer still needs to be assessed on its own merits. We still feel that the industry could be more transparent, but the situation is improving and there is now enough data to give advisers and investors some reference points.

Overall though, the industry continues to both raise and deploy more money and the products remain uniquely suited to meet some of the financial planning needs of wealthier clients, in areas where research has shown that clients feel advisers really add value for them.

SUMMARY OF EIS

Readers who want more detail on the basics of the scheme should refer to the 2014/15 EIS Industry Report, which has extensive sections on the history of EIS, the rules around qualifying companies, the tax reliefs, the small company investment universe and worked examples of the benefits of a portfolio based investment approach. We're just going to touch on these issues briefly here for the sake of completeness.

HISTORY OF TAX EFFICIENT INVESTMENT

HISTORY

Early 1980s
BES

1990s
VCT and EIS replace BES

Today
Key Growth Policy

The Enterprise Investment Scheme came into being in 1994, replacing the old Business Expansion scheme. It's a statutory relief designed to encourage private investment into smaller British businesses that has been supported by successive Governments, both Conservative and Labour (and of course the Coalition). Over 22,900 businesses have received £12.3 billion in funding via the EIS (HMRC).

With small businesses comprising 99% of businesses in the UK, 69% of employment and 47% of turnover in the private sector (Federation of Small Business), it's hard to imagine a scenario where any government would withdraw support for the scheme.

INVESTING IN EIS

- **Single Company:** Single company EIS investments are exactly what they say on the tin: small companies that are EIS qualifying and are raising money by issuing equity. These come in all shapes and sizes, from sensible investments to outright punts, and from the sublime to the ridiculous.

- **"Funds":** Many EIS investments will look and sound like funds, with an investment memorandum, investment manager and marketing literature to match. However, most are actually structured as discretionary investment services. Because the investor must have a direct holding in the underlying companies in order to qualify for the tax relief, there is no pooling and no legal entity that constitutes a 'fund'. In this technical sense they are not collective investments. Instead the manager will invest each investor's money directly into the underlying portfolio companies on their behalf. One investor's portfolio will look much the same as the next investor's, but it is an important distinction. Most of these 'funds' will be non-approved, which sounds negative but in fact gives them more time to raise and deploy money. We'll refer to these investments as either funds or EIS portfolios throughout this report for simplicity's sake, but readers should note that they are technically not collective investments.

- **Approved Funds:** Approved funds go to HMRC to seek approval for their proposed investments. The advantage for investors is that as soon as an approved fund closes they can claim their tax reliefs, as opposed to investors in unapproved funds who have to wait for three months after the manager makes each individual underlying investment to make their claim.

The disadvantage for the manager with an approved fund is that they only have a 12 month time limit to deploy the money, so they need a very robust pipeline. An unapproved fund has 24 months to deploy their funds. Most EIS funds are actually unapproved. We think the wording is unfortunate. Unapproved sounds quite negative, but in reality the additional time available for spending the money is a significant advantage.

- **Portfolio Services:** Some providers offer a platform for advisers and investors, with a range of EIS investments that they have curated, but they leave it up to the adviser or investor to decide which options they will pick and how much they invest.

- **Growth:** Self-explanatory. EIS investments made with the intention of growing capital.

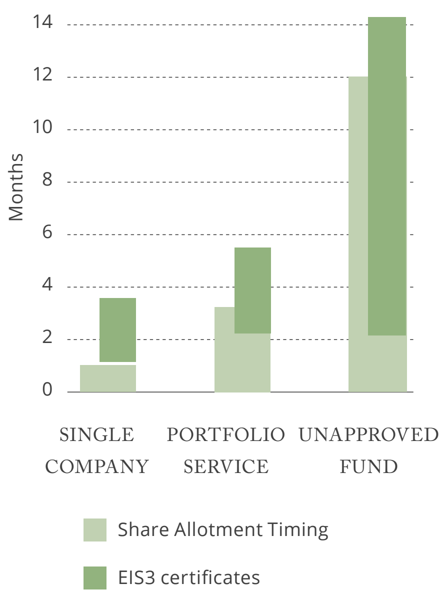
- **Capital Preservation:** These tend to be more project based EIS investments that are either asset backed or have secure, contracted revenues. They sacrifice potential returns in exchange for a lower level of risk and a more secure exit (although the exit can never be guaranteed as this would be a breach of the EIS qualifying rules).

Recent changes to the rules governing EIS were made to encourage growth EIS.

TIMING

Picking up on the point made above about approved and unapproved funds, it is worth considering the timing of share allotments and the issuing of EIS3 certificates (which allow investors to claim their income tax relief). Single companies will have the quickest turnaround, with funds being the slowest.

TIMING



Source: Rockpool

Timing probably won't be a showstopper for EIS investment, but is an important planning issue

"EIS portfolio service has come of age. Funds have been the order for the day for so long; IFAs think funds are the only alternative to a single company approach. Now many providers are increasingly offering transparent portfolio services that shorten the investment time and EIS3 certificate delivery" **Matt Taylor, Rockpool Investments**

OVERVIEW OF TAX BENEFITS

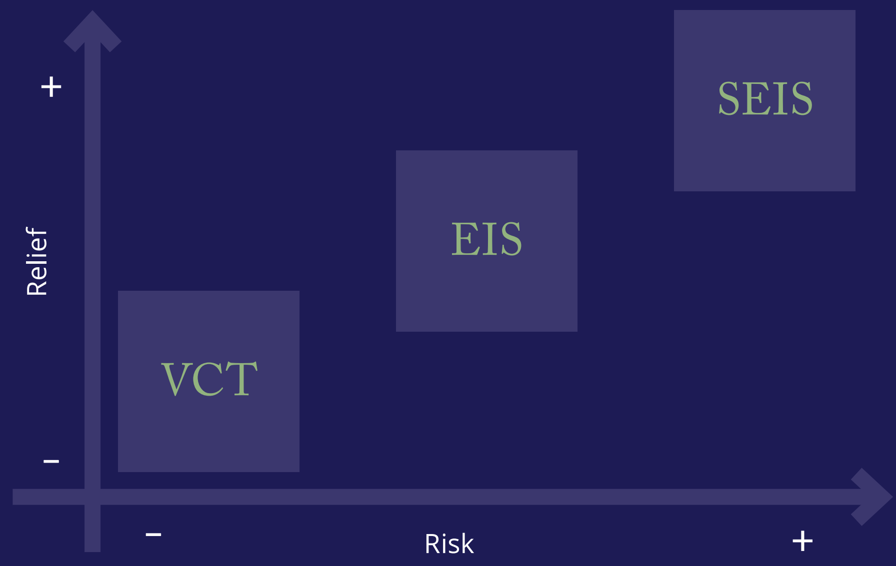
The EIS is one of three "Tax Advantaged Venture Capital Schemes" that use tax reliefs to encourage retail investors to invest in smaller businesses. The other two are Venture Capital Trusts (VCTs) and the Seed Enterprise Investment Scheme (SEIS). As a rule of thumb, VCTs are lower risk than EIS investments, which in turn are lower risk than SEIS investments and the amount of tax relief available increases in line with the risks inherent in each scheme. This is just a rule of thumb though - certainly many asset rich EIS investments can be less volatile and less risky than some VCTs are.

The EIS tax reliefs (subject to a minimum holding period of three years):

- 30% upfront tax relief
- 100% IHT relief (via Business Property Relief, so this is achieved after two years)
- 100% CGT relief on any gains
- CGT deferral if a gain made elsewhere is invested in an EIS
- Losses can be offset against either income or capital gains tax.

The tax reliefs are clearly attractive. A £10,000 investment would immediately knock £3,000 off the investor's Income Tax bill (note that it can only be offset against the income tax bill though - you can't get relief against tax you never paid!). The income tax relief can be applied to either the current or previous tax year.

Capital Gains tax incurred on gains made elsewhere can be deferred for as long as the gain is invested in an EIS (i.e. it is possible to continually defer the gain if it is rolled over into fresh EIS investments - and if the investor dies, the CGT liability dies with them) and any EIS investment will be exempt from inheritance tax via the Business Relief Scheme (commonly referred to as Business Property Relief or BPR).



COMPARING TAX-EFFICIENT INVESTMENT OPTIONS

	ISA	PENSION	VCT	EIS	SEIS
ANNUAL CAP	£15,240	£40,000	£200,000	£1m	£100,000
LIFETIME CAP	x	£1.25m / £1m	x	x	x
INCOME TAX RELIEF	x	√	30%	30%	50%
LOSS RELIEF	x	x	x	√	√
IHT RELIEF	x	Depends	x	√	√
CGT FREE GROWTH	√	√	√	√	√
CGT DEFERRAL	x	x	x	√	√
TAX-FREE INCOME	x	x	√	x	x
TAX-FREE LUMP SUM	√	25%	√	√	√

The three schemes usually compliment more conventional saving and investment wrappers such as ISAs and personal pensions.

"Managers can support advisers when considering financial planning to utilise EIS from providing educational seminars, providing case studies and assisting in technical queries" **Jerry Price, Blackfinch Investments**

LOSS RELIEF

The loss relief has a huge impact on the performance of a portfolio of EIS investments, as losses do not have to be offset against gains: investors losses are limited, but their gains are not, so if you can find a 'ten bagger' (an investment that returns 10 times capital) you can afford to have much of the rest of your portfolio underperform. This would be the strategy many growth focused EIS funds employ, knowing full well that when investing in unquoted companies they will not get it right all the time. However, capital preservation EIS investments tend to be more project based, backing fewer, lower risk opportunities.

CAPITAL GAINS TAX DEFERRAL

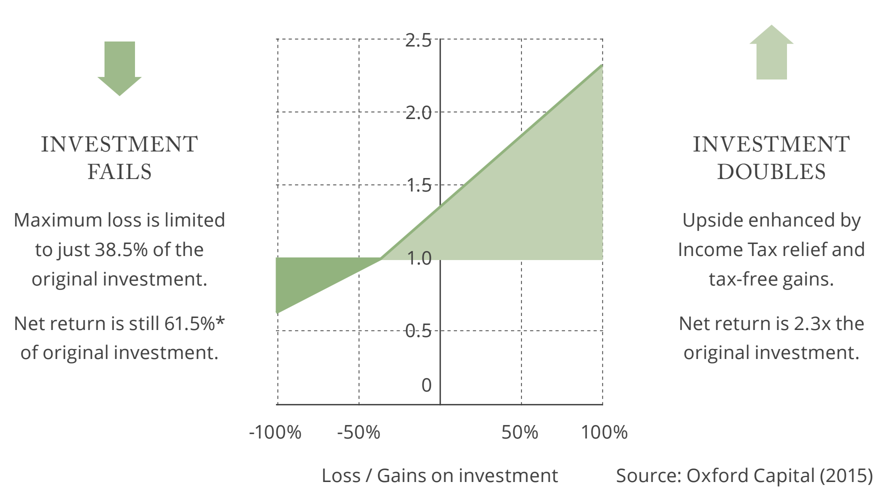
This can be applied to a gain made up to 36 months before the date of investment: so a good question to ask clients is "have you made a significant capital gain in the last three years?" The CGT liability can still be deferred.

SUITABILITY

The nature of the risk profile and tax reliefs naturally means that EIS investments are only really going to be appropriate for wealthier investors. Investors will need the requisite attitude to risk and capacity for loss to be considered suitable for an EIS investment, and although the tax reliefs are always going to be attractive, they are only relevant where significant amounts of tax have been paid. It's not worth taking on the levels of risk associated with EIS investments to offset smaller tax bills, and the "tax tail should never wag the investment dog". Our understanding is that this is very much how the Financial Ombudsman Service (FOS) views suitability when they assess complaints about recommendations to invest in tax-efficient products.

Changes to pension limits mean that many more investors are going to max out what they can save in ISAs and pensions, and are therefore going to look to their advisers to find other tax-efficient investments such as EIS.

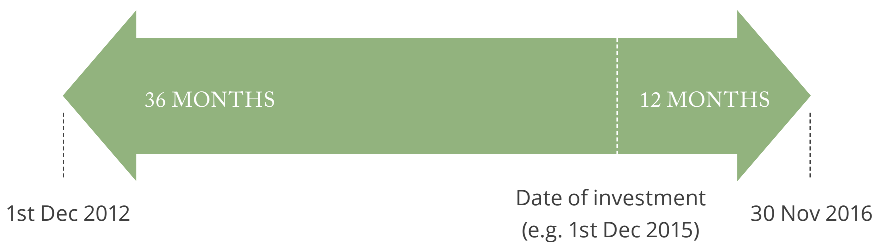
ENHANCE THE UPSIDE & CUSHION THE DOWNSIDE*



EIS protects the downside and enhances the upside. The effect is asymmetric and in favour of the investor.

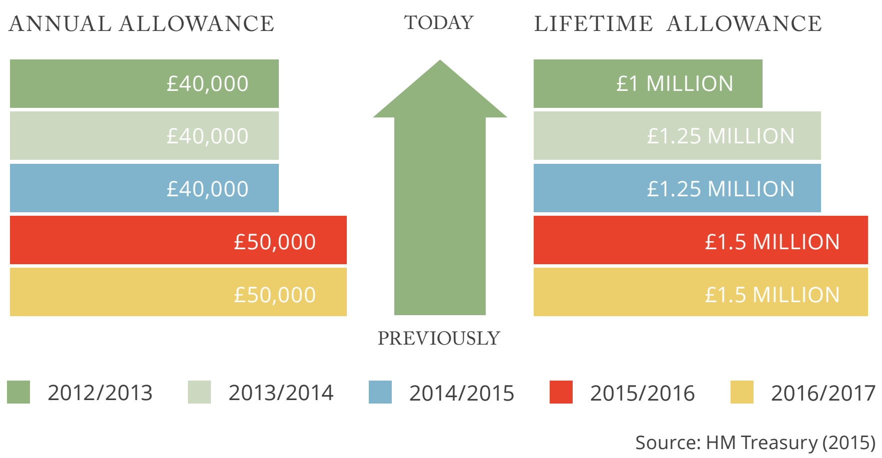
When the loss relief is considered in conjunction with the CGT relief, it is easy to see how building an EIS portfolio allows investors to minimise their risk and maximise their returns. There is a worked example of loss relief on page 58.

CAPITAL GAINS TAX DEFERRAL RELIEF



Annual CGT allowance applies at the prevailing tax rate on exit. Can be used to re-order gains and losses

AMOUNTS THAT CAN BE SAVED INTO PENSIONS BY TAX YEAR

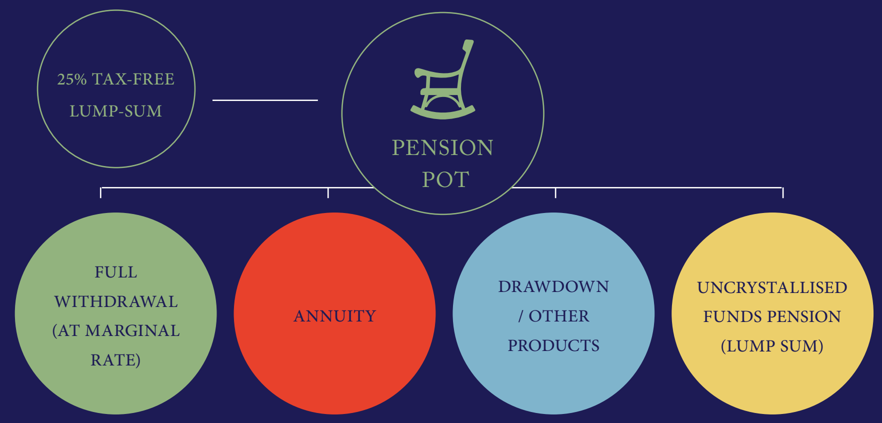


Pension limits have been decreasing for some time and that means more advisers are considering EIS

*Example based on an additional rate taxpayer

"Recently IFAs have told us that EIS is now more important for their clients than pensions. Not surprising perhaps when you think that the maximum pension contribution saves £18,000 of tax, compared to £300,000 for EIS" **Warrick Shanly, Rockpool Investments**

OPTIONS AT RETIREMENT POST THE PENSION FREEDOMS



The new pension freedoms that came into effect this year may mean that many more investors defer buying an annuity and use a drawdown solution. We cover how EIS can be used to develop tax efficient decumulation strategies on page 60.

ADVISER RESOURCES

As well as this report and the previous 2014/15 version, advisers can consult independent review providers such as MICAP, Tax Efficient Review and Tax Shelter Report. These organisations provide reviews on individual investment opportunities as well as offering online tools to research EIS investment opportunities.

The Enterprise Investment Scheme Association (EISA) is also a good source of information, and they offer a diploma in EIS for advisers, via the training provider Tolleys. The diploma is estimated to be ten hours of study time and covers all aspects of the EIS in great detail.

Finally, there are a number of face to face training events for advisers. Intelligent Partnership periodically hold EIS masterclasses around the country, and other providers and distributors also put on seminars and training to help advisers understand the market. The IFP (now merged with CISI) and PFS also often cover EIS in their regional and branch meetings.

In general, the larger providers and EIS industry as a whole have been making determined efforts to reach out to, and engage with, advisers. They understand that as alternative, unquoted investments there is more work involved for advisers and they want to do everything they can to meet advisers halfway. Many of the larger providers deliver CPD accredited educational programmes or speak at CPD accredited events, and often their content and literature is as focused on learning as much as it is focused on their product pitch. There are now lots of options for advisers to educate themselves, access more information and help them develop efficient business processes around EIS.

CONCLUSIONS

Perhaps the most important thing to say about the EIS is that it is a well-established statutory relief. The Enterprise Research Centre found that High Growth SMEs generate 20% of job growth amongst established businesses which grow. Research by the Policy Network (Supporting Investors and Growth Firms, June 2015) found that encouraging equity investment into small businesses could be a huge driver of growth in jobs and the economy. The same publication reported that the EIS is the envy of many policy makers in Europe, who feel constrained by political expediency - in a time of austerity they could not be seen to be advocating tax reliefs for the wealthy.

We're lucky to have such a scheme already in place, with a strong track record of providing capital. Compliance with EU State Aid rules and the end of the renewables story now means that we should see a period of stability, and lower pension limits and increased awareness among advisers and investors will lead to increased fundraising. With the funding gap for small businesses still estimated to be around £1 billion annually, we think that the stage is set for the EIS to play an increasingly important role in funding high growth firms and contributing to economic recovery. And the tax reliefs address financial planning needs that many advisers will recognise within their client banks.

ADVISER RESOURCES

INDEPENDENT REVIEW PROVIDERS

Advisers can consult independent review providers such as Tax Efficient Review, Tax Shelter Report and MICAP. These organisations provide reviews on individual investment opportunities as well as offering online tools to research EIS investment opportunities.

ENTERPRISE INVESTMENT SCHEME ASSOCIATION

is a good source of information, and offers a diploma in EIS for advisers, via the training provider Tolleys. The diploma is estimated to be ten hours of study time and covers all aspects of the EIS in great detail.

TRAINING EVENTS

Intelligent Partnership periodically holds EIS masterclasses around the country, and other providers and distributors also put on seminars and training to help advisers understand the market. The IFP (now merged with CISI) and PFS also often cover EIS in their regional and branch meetings.

MARKET DEVELOPMENTS

MARKET DEVELOPMENTS

As we noted in the introduction, many of the changes that have come about in the last 12 months have been driven by external forces. We'll examine some of those in more detail in this section, as well as taking a look at the latest statistics, the nascent SEIS and Social Investment Tax Relief (SITR) sectors and consider some of the more innovative developments in the market.

LEGISLATION AND REGULATION

"Governments can't create wealth, but they can create the conditions for private enterprise to flourish."
Bill Owens, American Politician

LEGISLATION: NEW STATE AID RULES

The EU State Aid Risk Capital Guidelines were updated in May 2014, and the UK Government had to apply for renewal of State Aid approval for all three of our Tax Advantaged Venture Capital Schemes (VCT, EIS, SEIS). The outcome of this process has been two Budgets that proposed changes to the rules governing the scheme, one in March 2015 and one in July 2015. The new rules proposed in July were much stricter than the rules proposed in March - we can only assume that the EU took a look at what the Treasury was proposing and decided that it didn't go far enough. The new rules came into effect with the Finance Act, which was given Royal Assent in November 2015.

STATE AID

State Aid is any advantage granted by public authorities through state resources on a selective basis to any organisations that could potentially distort competition and trade in the European Union. Some State Aid is illegal under EU rules because it distorts competition in a way that is harmful to citizens and companies in the EU. But where it is unavoidable, State Aid can be given legally by:

- Using one of a set of approved EU mechanisms for State Aid
- By getting approval for the particular scheme from the EU Commission

OUTLINE OF RULE CHANGES GOVERNING INVESTEE COMPANIES

		PRE-MAR 2015	BUDGET 2015	SUMMER BUDGET
AGE LIMIT		No limit	12 years*	7 years*
LIFETIME CAP		No limit	£15m	£12m
ANNUAL INVESTMENT LIMIT		£5m	£5m	£5m
EMPLOYEE LIMIT (FTE)		250	250	250
KNOWLEDGE INTENSIVE COMPANIES	LIFETIME CAP	No limit	£20m	£20m
	EMPLOYEE LIMIT	250	500	500
	AGE LIMIT	No limit	12 years	10 years*
USE OF EIS & VCT MONEY FOR ACQUISITIONS OF BUSINESS		Allowed	Allowed	New rules to prevent EIS and VCT funds being used to acquire existing businesses
GROWTH & DEVELOPMENT		No requirement	Require that all investments are made with the intention to grow and develop a business	Require that all investments are made with the intention to grow and develop a business
SEIS MONEY		70% of SEIS money be deployed before raising EIS	70% limit removed	No limit
EXISTING SHAREHOLDERS		No restriction	For EIS only, a requirement that investors are independent from the company at the time of the first share issue (excluding founder shares)	For EIS only, a requirement that investors are independent from the company at the time of the first share issue (excluding founder shares)

These changes represent significant upheaval for some VCT managers. The EIS sector is less affected, but it does mean that some of the lower risk EIS investments we have seen will no longer be allowable

*Unless total investment represents more than 50 per cent of the company's turnover over the preceding five years

"The UK Government and the EU have been clear – EIS policy is focused on supporting investment into businesses that might not have access to other sources of finance" **David Mott, Oxford Capital**

These changes have introduced a couple of new concepts:

Knowledge Intensive Companies have research and development costs amounting to at least 15% of their total operating costs, create intellectual property and have 20% or more of their workforce with relevant Masters or equivalent higher degrees.

Independence. For EIS relief, investors must be independent from the company at first share issue. So if an investor wishes to be involved in a company in an official capacity, then they must first invest and then, at a later date, become a director.

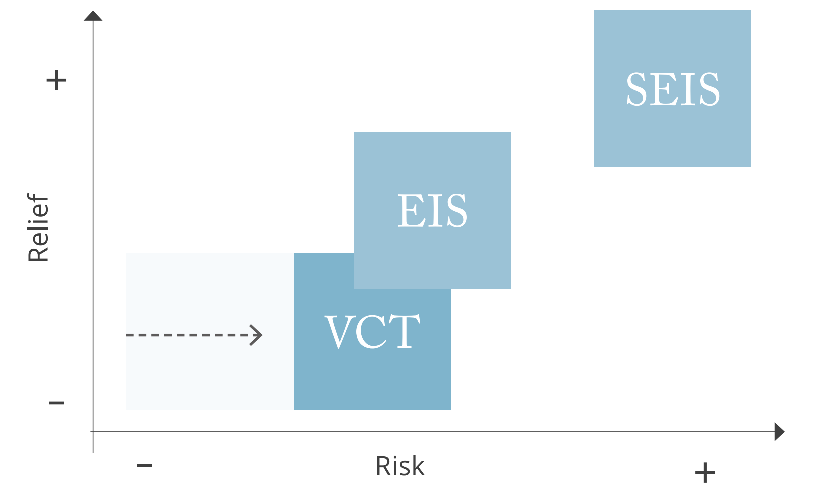
Growth and Development Test: This is a new test, and is a rather vague term - although HM Treasury promised more guidance on it in December 2015, at the time of writing nothing was published. What we have been told is that it will mean that HMRC will be scrutinising business plans in much more detail to assess if a firm or project qualifies for EIS. What form this scrutiny will take remains to be seen, but we have already heard reports that HMRC have been slow responding to requests for advanced assurance that trades will be EIS qualifying.

Removing the requirement to spend 70% of SEIS money before raising EIS money does smooth the passage between the two schemes out a bit for the investee companies.

The Financial Secretary David Gauke MP stated in Parliament on the 14th October 2015 that the government is: *"keen to introduce increased flexibility for the schemes to be used for 'replacement capital', where the amount invested in newly issued shares is at least equal to the amount invested in secondary shares. The intention is for this change to be introduced through secondary legislation at a later date, subject to State Aid approval".* This again softens the rules a little and provides a bit more flexibility.

While the changes do impose new restrictions on the EIS industry, they are by no means showstoppers. By and large EIS funds have always been focused on providing development

IMPACT OF THE CHANGES PROPOSED IN THE SUMMER BUDGET



Some VCTs will now have to change their business model - pushing them closer to EIS in terms of risk, although some EIS that target capital preservation will also be affected

capital to young businesses and have not relied upon acquiring established businesses. We think that it is certain parts of the VCT industry that are going to have to make bigger changes - some funds based their model around MBOs.

Intelligent Partnership's view is that the driver for all of these changes was complying with EU State Aid Rules, and therefore was as much a question of politics as economics - as we posted in our blog at the time:

"The government's stated aim is to ensure that the schemes continue to support economic growth and provide value for money for the UK Taxpayer. We're not sure that the:

- *Age of business criterion,*
- *Cap on total investment and*
- *Limit on number of employees for the investee companies serve either of these objectives.*

An arbitrary seven year limit on funding doesn't seem to serve any logical purpose. It penalises firms with long R&D periods, or firms that have traded on a small scale for a number of years but then identified the potential to grow.

The cap on total investment penalises firms where there is a need to raise very substantial amounts of working capital to finance a long term development programme before investors see a profit, or where expensive capital assets need to be acquired in order to commence business.

And the size of a company's workforce will be a reflection of the type of trade carried on by the business, not an indication of its stage of development and how easy it can access finance.

Removing or amending these rules could let more capital flow to where it is needed – plugging the equity gap for SMEs and helping to create jobs. At the moment, the rules are putting a brake on economic growth and therefore they do not represent good value for money for taxpayers.

However, these rules are not down to the UK government's decision making. They are there to ensure compliance with European State Aid rules. As the Policy Network identified in its recent publication "Supporting Investors and Growth Firms", although the UK's schemes are well regarded on the continent, politicians shy away from them as they fear that they will be perceived as giving tax reliefs to the rich at a time of austerity for the majority."

Finally, there is a "sunset" clause on the legislation - it will be reviewed in April 2025. This should not be interpreted as the proposed end for the schemes by any means: we think it is more of a signal of their intention to pause and assess the state of play. Whilst HM Treasury have clarified that they reserve the right to amend this date, hopefully it indicates

"Tax-advantaged venture capital schemes are there to meet the government's aim of providing valuable support to small and growing businesses seeking finance to develop, to grow and to create employment. That's what it says on the tin" **Ian Battersby, Seneca Partners**

that things are going to be left pretty much as they are for the next decade and usher in a welcome period of stability.

A side point suggested to us by RW Blears, lawyers active in the EIS and VC industry, all of these various tests: the gross assets test, the number of employees, the age of the business etc., are designed to ensure that the money raised via these tax-advantaged venture capital schemes is directed to businesses who struggle to raise capital elsewhere. Wouldn't it be simpler just to ask businesses to provide evidence that their requests for funding have been turned down by the banks?

POLITICAL CLIMATE

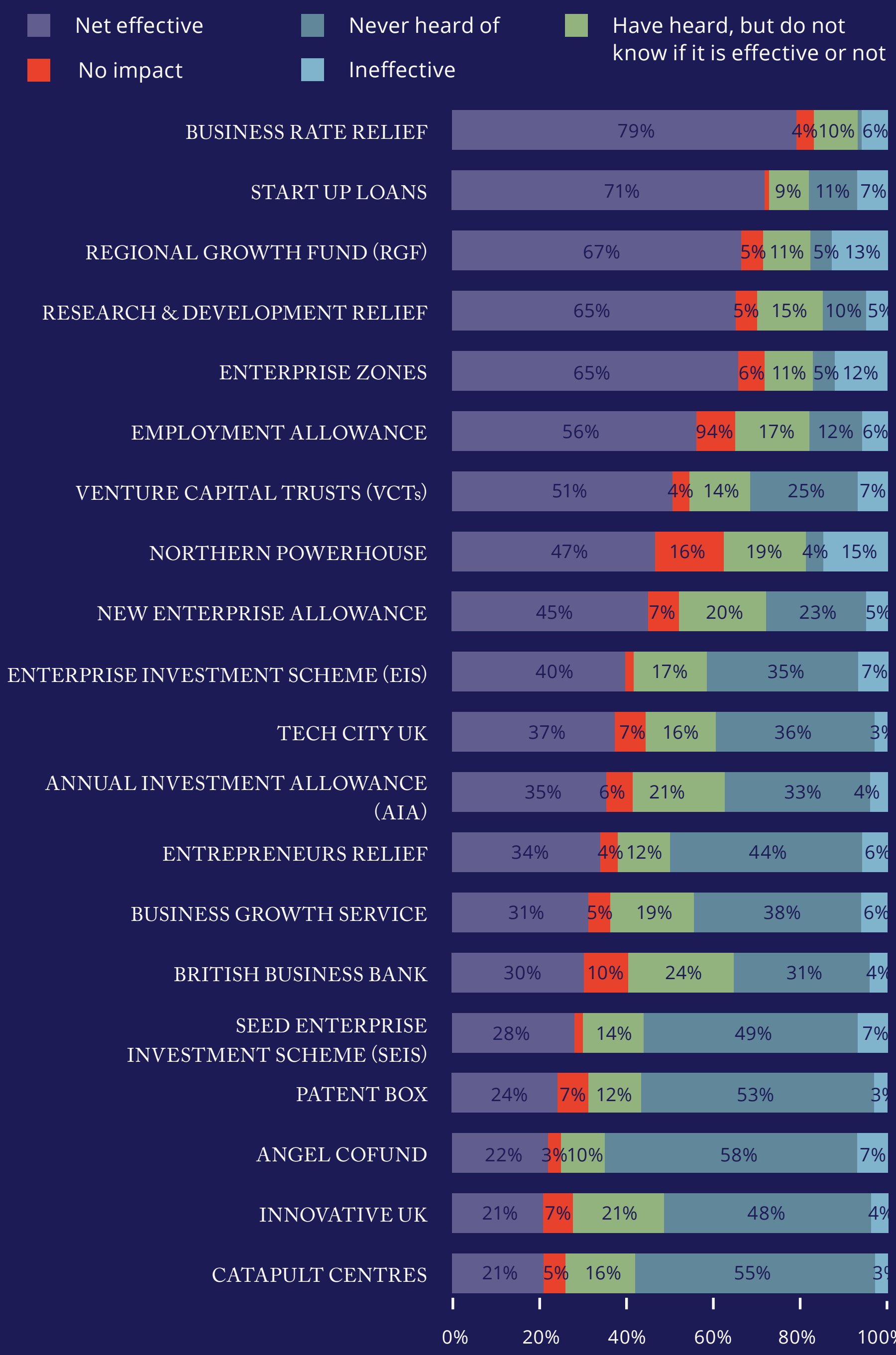
Despite the new restrictions that have been brought in to ensure compliance with EU State Aid Rules, we think that the political climate for EIS is actually very positive The determination to ensure State Aid compliance is just one indicator of the Government's determination to see all three of the statutory Tax Advantaged Venture Capital Schemes continue. The rhetoric coming out of Government also demonstrates their commitment to the schemes:

"The government's aim is to make Britain the best place in Europe to do business. The tax-advantaged venture capital schemes continue to be an important part of meeting this aim, providing valuable support to small and growing businesses seeking finance to develop and grow." David Gauke, Financial Secretary to the Treasury, July 2015

Previous Labour governments also supported and strengthened the EIS regime (although it remains to be seen how policy on this topic will develop under the new Labour leadership). And we should be careful - while there is clearly strong support for EIS at ministerial level, the scheme is not well understood among the wider population of MPs.

This isn't necessarily a big problem, MPs have a lot to deal with and why should they have heard of EIS? However, it does indicate that the scheme could do more to publicise itself and the good work it does supporting small business.

MPs' SUPPORT FOR INITIATIVES



Source: The Entrepreneurs Network

SEED ENTERPRISE INVESTMENT SCHEME (SEIS)

- 63% of MPs have never heard of it or don't know if it's effective
- 56% of Conservative MPs have never heard of it or don't know if it's effective
- 69% of Labour MPs have never heard of it or don't know if it's effective

ENTERPRISE INVESTMENT SCHEME (EIS)

- 52% Never heard of or don't know if it's effective
- 46% of Conservative MPs have never heard of it or don't know if it's effective
- 57% of Labour MPs have never heard of it or don't know if it's effective

“The very nature of the investment universe (private investors, unquoted companies, low levels of coverage by analysts, low levels of liquidity, no central “authority” such as FTSE or the LSE) means that meaningful data is hard to come by”

AVOIDANCE, EVASION AND MITIGATION

There has been a clampdown on tax evasion over the last few years, with over £1 billion invested into the Treasury to help them track down and challenge tax dodgers and the lines between avoidance (legal) and evasion (illegal) have become a little blurred. Here's how we see HM Revenue & Customs' current interpretation of the rules:

- **Tax Evasion** is a criminal offence. Tax Avoidance is not, but you can be taken to a tax tribunal
- **Tax Avoidance:** bending the rules to gain a tax advantage that was never intended. Operating within the letter, but not the spirit of the law. Tax Avoidance is no a criminal offence, but you can be taken to a tax tribunal
- **Tax Evasion:** escaping paying taxes illegally. When a person misrepresents or conceals the truth. Tax Evasion is a criminal offence

An EIS investment is never going to fall into the category of evasion. It is possible for an EIS to be considered a tax avoidance scheme, but only if it is deemed that the underlying investment is not genuinely trading and not being run for a profit, and instead simply exists to manufacture a loss and qualify for the reliefs. There haven't been any high profile cases of the EIS being used in this manner that we are aware of.

However, film production partnership investments that have been accused of tax avoidance have had a high profile - largely due to the number of celebrities that invested in them. Some investors have been hit with Advance Payment Notices (APNs), controversial new powers that allow HMRC to claw back tax prior to the decision of the tribunal. HMRC expects to issue around 64,000 such notices by the end of 2016, a move which it said would bring forward £5.5 billion in payments for the Treasury by March 2020.

Readers should be clear that these investments were nothing to do with EIS, but were based on a different regime of tax reliefs designed to stimulate investment into the British film industry (principally ‘section 42’ and ‘section 48’ reliefs) and a number of schemes are suspected of exploiting the rules. Some providers have vigorously challenged HMRC on this and cases are still working their way through the judicial system. Rulings on the legality of three of Ingenious Media's schemes were due at the end of 2015. However, at the time of writing there was no decision made. Unlike EIS, it's not possible to secure HRMC's advance assurance that film partnership schemes are compliant with the rules.

All of this really supports the case for EIS. It's a statutory scheme, that's well established and has been supported by both Labour and Conservative governments in the past. There is no evidence of widespread abuse of the EIS rules and the crackdown on tax avoidance has been focused on schemes that pushed the boundaries of a different set of reliefs.

RELIEFS AND EXPENDITURES

When we talk about tax reliefs, technically we are really talking about two different things:

- A tax relief is designed to ensure that a tax is only applied to the group it was originally intended for. Cabin crew do not have to pay air passenger duty – the duty is intended to apply to paying passengers and it would be unfair to apply it to the crew! So this is a relief.
- Tax expenditures are an alternative to a public spending program and are designed to have similar effects – to incentivise certain behaviour through the tax system. Tax relief on pension contributions is a tax expenditure that encourages us to save for our retirement.

In the investment world, we tend to encounter tax expenditures – incentives to either save (think ISAs and pensions) or to put capital to work where it is needed most (think VCTs and EISs). However, both expenditures and reliefs are colloquially referred to as reliefs.

INVESTING IN SMEs

RESEARCH INTO PERFORMANCE

There is still a lack of data on the performance of investments into small, unquoted businesses, whether those investments are made by using an SEIS, EIS, VCT, Crowdfunding platform, Angel Investor network or by investing privately. The very nature of the investment universe (private investors, unquoted companies, low levels of coverage by analysts, low levels of liquidity, no central “authority” such as FTSE or the LSE) means that meaningful data is hard to come by. Instead we are reliant upon research, but even this is slow and can only ever present us with a snapshot of a certain time and certain sample of investments.

The best piece of research that we have is still “Siding with the Angels”, a report by NESTA and the British Business Angels Association - but this goes all the way back to 2009. It found that:

- The most likely outcome in any one angel investment is failure, but ‘winning’ investments are very attractive. Fifty-six per cent of the exits failed to return capital, while 9% generate more than ten times the capital invested
- Because the 44% of investments that generate positive exits win at a larger multiple than the costs of the negative exits, the overall return to business angels investing in the UK is 2.2 times the invested capital
- These 9% large investment exits produced nearly 80 per cent of all the positive cash flows. Given the holding period of just under four years, this is approximately a 22 per cent gross Internal Rate of Return (IRR).

A more recent paper is the 2015 “A Nation of Angels” by the Centre for Entrepreneurs and UK Business Angels Association. The report was focused on the makeup and activities of the UK angel community rather than trying to measure investment performance, but it did survey the angels expected returns from their investments:

“This year EIS investors should focus more than ever on the investment than on the tax relief. Now that Government subsidised investments are excluded from EIS, there is no such thing as a low risk EIS” **Nigel Ashfield, TIME Investments**

“Angels reported a lower rate of low returns and a higher rate of expected higher returns than in previous research, which shows considerable confidence in the market. Over 4 out of 10 investments were expected to generate a return in the range 1-5 times the initial investment. A further 2 out of 10 investments were expected to produce a return of 6-10 times the initial investment and 1 out of 10 expected to achieve returns in excess of 10 times their initial investment. This is a higher rate of expected higher returns than found in earlier studies”.

Finally, Oxford Capital researched the impact of diversification and the portfolio effect for our 2015 EIS masterclass roadshow. Looking at a sample of typical qualifying companies that would be selected for a growth EIS (note, not capital preservation), just picking one investment has a 25% chance of returning zero. There's something like a 1% chance of getting 4 times capital back.

When that investment is spread across a portfolio of 12 companies, the chances of getting 3-4 times capital back actually decrease, but the chance of getting nothing back at all falls to zero and there is a strong probability of getting a return of between 1 and 2 times capital.

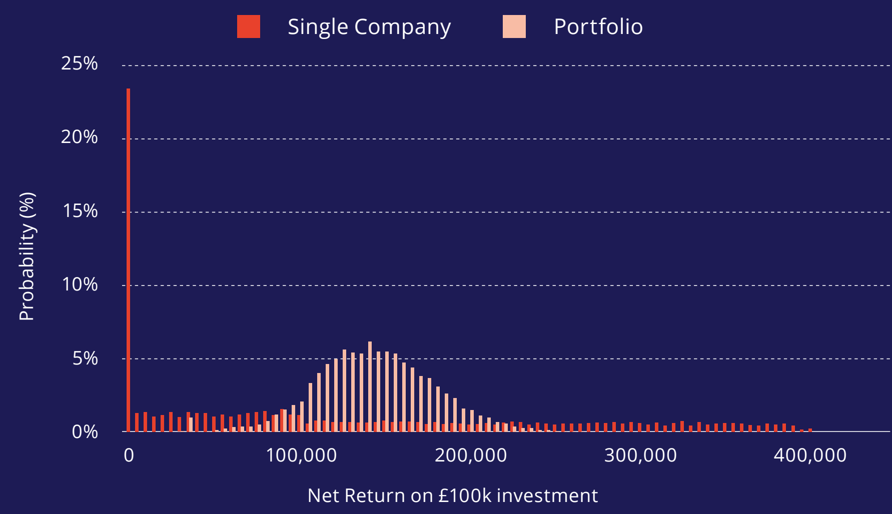
When the various tax reliefs are added to the analysis (income tax relief, loss relief and CGT relief), the effect is to basically move everything to the right in the diagram above. In both the single company and portfolio scenarios the possibility of getting nothing back is eliminated, and in the portfolio scenario the probable returns are clustered around 1.5–2.5 times capital.

Interestingly, Oxford Capital's research found that more than 12 companies in a portfolio started to limit the potential upside, with appreciable effect on limiting losses on the downside: “di-worse-ification” perhaps!

The findings from the available research are not a million miles apart from each other (but we must not get carried away - they all had small samples and different methodologies). It seems that the commonly applied heuristic that half of all small companies fail to return 1x capital has some truth to it, and the expectation that one in ten investments into a SME will be a stellar performer also makes sense. These numbers suggest that statistically you need a portfolio of 30 investments to give you a 95% chance of having that stellar performer that returns greater than 10 times capital in there. For many investors, the quickest and easiest way to get diversified exposure is though EIS investment managers and their products.

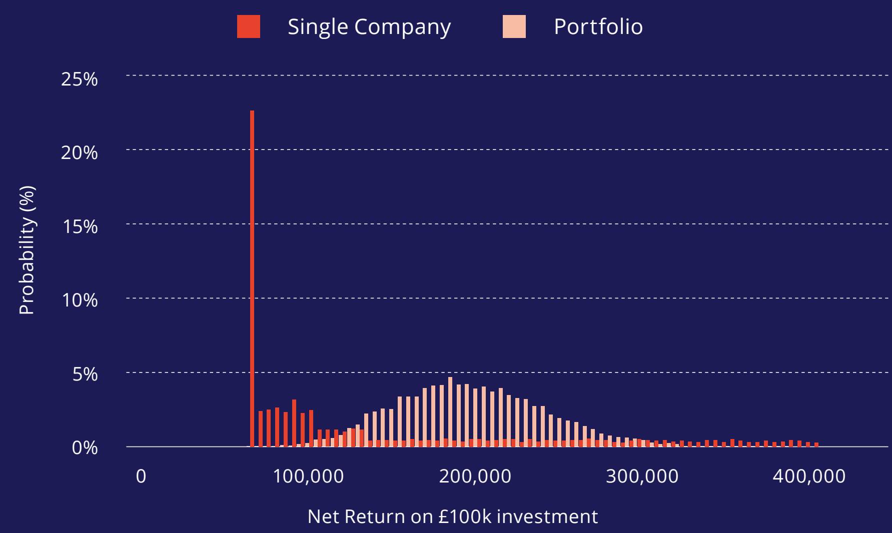
In summary, investing in small companies is risky, but has the potential for high returns. The EIS scheme tilts the risk reward profile back in favour of investors. The tax reliefs are well understood, but the power of loss relief within a portfolio should also be highlighted: being able to make tax free gains on winners while putting a floor under any potential losses makes investing in this universe much more attractive.

PROBABILITY (%) OF NET RETURN WITHOUT TAX RELIEF



Source: Oxford Capital

PROBABILITY (%) OF NET RETURN WITH TAX RELIEF



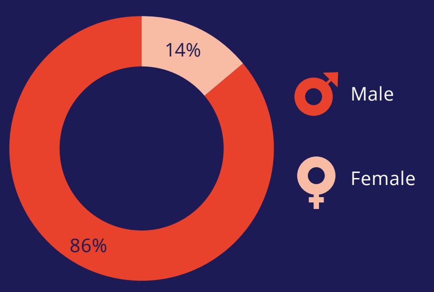
Source: Oxford Capital

"Professional investors have targeted private companies for many years; witness the multi-billion dollar private equity industry. Now individuals can access this area directly using EIS to reduce risk and enhance returns. We're seeing a huge increase in appetite for quality EIS companies" **Mark Pearson, Rockpool Investments**

WHO ARE ANGEL INVESTORS?

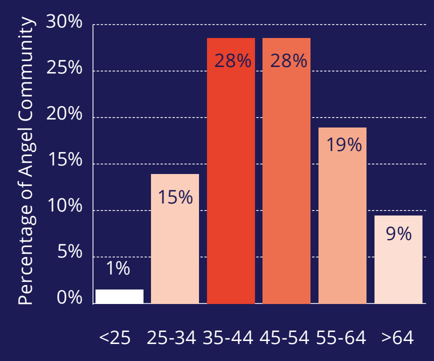
The Nation of Angels report gave us much more information on who comprises the business angel community. We've presented some of their findings here, but we won't make too many comments on them, suffice to say that we would expect many advisers' client banks to have a similar composition. Another noteworthy point from the report - 79% of angels say that they reinvest their gains in further small business opportunities. (The full report can be downloaded from the UK Business Angels Association, along with a lot of other high quality research on related topics. Another useful resource is the Enterprise Research Centre).

BY GENDER



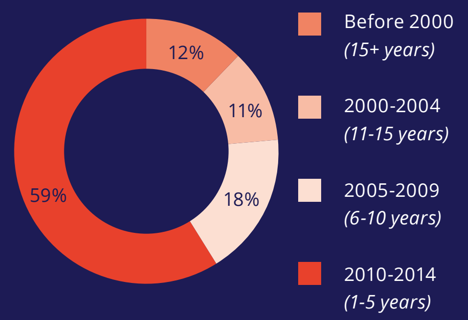
Source: ERC Nation of Angels Survey (2014)

BY AGE



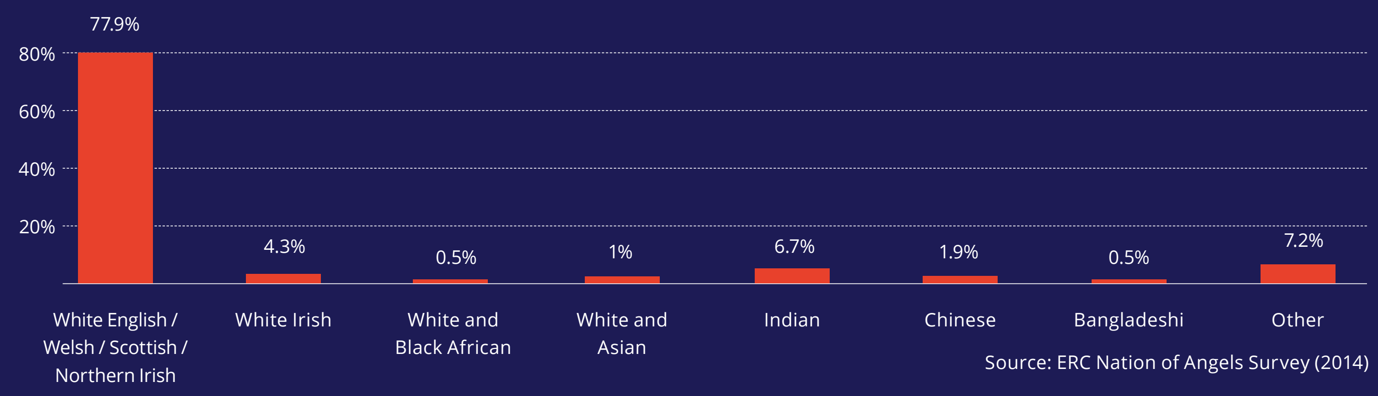
Source: ERC Nation of Angels Survey (2014)

BY YEARS OF EXPERIENCE



Source: ERC Nation of Angels Survey (2014)

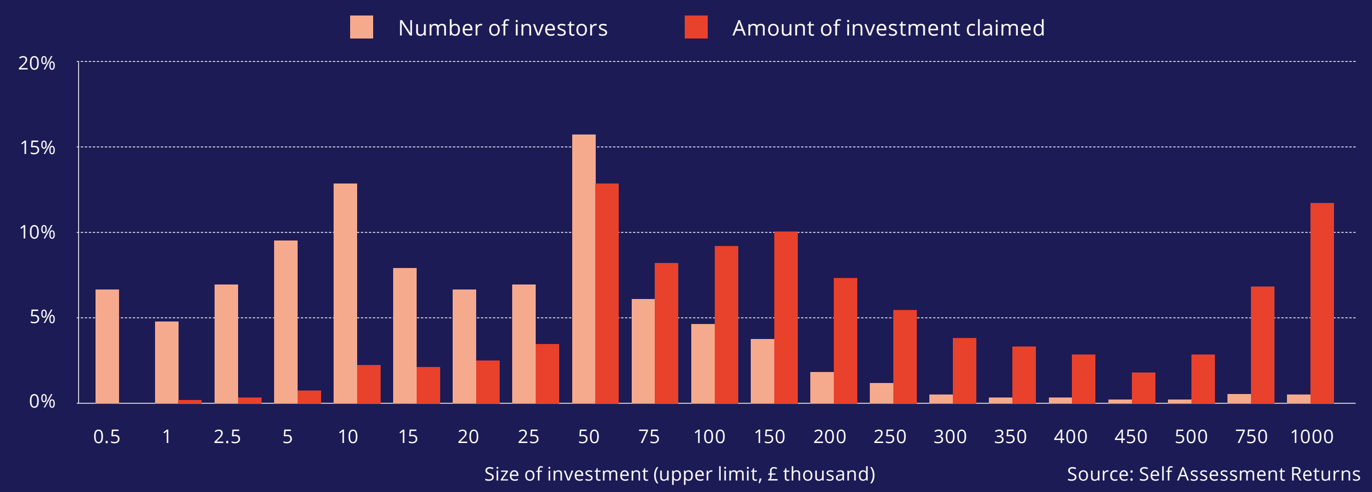
BY ETHNICITY (2014)



Source: ERC Nation of Angels Survey (2014)

We can also speculate about who is investing and why based upon the figures that HMRC collect on self-assessment returns and publish annually in October:

% OF INVESTORS AND AMOUNT OF INVESTMENT BY SIZE OF INVESTMENT (2013-2014)



Source: Self Assessment Returns

"HMRC is keen to support EIS opportunities that target investment in sectors that have the Government's backing" **Nigel Ashfield, TIME Investments**

The number of investors claiming Income Tax relief on Self Assessment forms under EIS increased from 21,730 in 2012-13 to 26,275 in 2013-14 (an increase of 21%). In the same period the total amount of funds raised has risen from £1.03 billion to £1.53 billion (an increase of 48%). So we have more investors, and the investor base is investing much more money in EIS.

The majority of the investors claiming Income Tax relief tend to invest smaller amounts of money into companies qualifying for EIS. In 2013-14, 79% of EIS investors made a claim for tax relief in respect of an investment of less than £50,000. This was unchanged from the proportion for 2012-13.

The number of investors claiming Income Tax relief for an investment of less than £500 continued to grow: after more than doubling from 2011-12 to 2012-13 (from 550 to 1,200), the number of investors grew to 1,785 in 2013-14. We can probably attribute this to the growth in popularity of crowdfunding, which sources lots of smaller investments into (usually) small fundraising efforts by firms.

Investors were able to claim Income Tax relief on an investment of up to £1 million from 2012-13, compared with a previous limit of £500,000. The investments of £500,000 to £1m contributed to 16% of the total amount of EIS investment raised on which claims were made in 2012-13 and 19% of the total amount in 2013-14. Investments of £25,000 to £500,000 contributed to 69% of the total amount of EIS investment raised on which claims were made in 2013-14.

LACK OF EQUITY CULTURE

Equity financing is still only rarely the first choice of SMEs looking for funding.

Business owners not wanting to give away equity is understandable, but in many cases equity would be a much more suitable source of funding than debt, which imposes an ongoing liability of interest payments on a business, as well as the need to ensure that they can repay the principal at the end of the term. Equity finance can and should be much more flexible: although this is dependent upon getting the "right" equity investors who understand the business and its objectives.

IMPORTANCE OF SMEs

"It's important to acknowledge the key role played by growth investors in helping small businesses start, expand, and reach their full potential. The government provides a range of support to encourage this type of investment, including through the tax-advantaged venture capital schemes which have supported more than 22,000 companies to access over £17.5 billion of investment. Without access to the finance they need to develop their vision, companies with great ideas would struggle to fulfil their potential, and Britain would lose out." - David Gauke MP, Financial Secretary to the Treasury, Growth Investor Awards, October 2015

However, the same research also identified difficulties ahead for SMEs. Access to finance was still one of their concerns (although it is no longer the biggest, which now appears to be recruiting skilled employees) and, despite the UK's success at encouraging small businesses, it still seems as though debt, rather than equity, is used as the primary source of capital for small businesses, and there is still a significant funding gap.

APPLICATION RATE FOR EQUITY FUNDING BY COMPANY SIZE

No. OF EMPLOYEES	APPLICATION RATE
0	0.4%
1-9	0.6%
10-49	0.7%
50-249	1.0%

Source: SME Finance Monitor (Q2 2012 to Q3 2014)

IMPORTANCE OF SMEs

99% of **UK businesses** are SMEs. They comprise the vast majority of the private sector (by no. of business)

4,500 **new jobs** created per week in 2014 by High Growth Small Businesses*

3x **more than FTSE 100** SMEs drive job creation in the UK

Almost **20%** of the **economic growth** is from High Growth Small Businesses

50% of **gross value** added in the UK comes from SMEs

SMEs are flourishing right across the UK, and they are optimistic about the future.

**The Octopus High Growth Small Business Report 2015*

"The number of entrepreneurs approaching us for EIS funding has doubled over the past year, and many of them are developing valuable, innovative solutions to commercial, technological or scientific problems" **Tom Bradley, Oxford Capital**

FUNDING GAP

The "Funding Gap" is one of those terms that is used a lot without being examined in detail. It is generally taken to mean the gap between the level of funding small and medium sized businesses in the UK would like each year, and the level that they get. The gap is estimated to be around £1 billion annually and much of it can be attributed to the withdrawal of banks from lending to small businesses since the financial crisis of 2008.

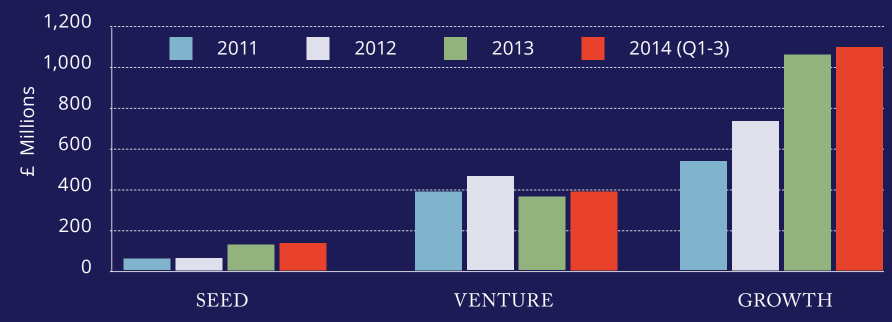
The funding gap, and the retrenchment of banks, does represent something of an opportunity for EIS managers as it means there are more opportunities around for them to invest in.

We also have to consider that the funding gap may be regional. As the chart below shows, there is a much higher concentration of high net worth investors, EIS investment and high growth firms in London and the South East compared to the other regions. It's hard to ascertain whether this pattern is driven by a concentration of demand for EIS investment, or a concentration of supply - but we suspect it is more down to demand. (Note, however, that many firms will have their headquarters in London, even if their activities are outside London: this skews the figures somewhat, but won't change the overall trend).

IS EIS ADDRESSING THE FUNDING GAP?

Most EIS investments are in the £1 million to £5 million range – servicing the size of deals that are too small for venture capital (VC) and private equity (PE) firms, and addressing the funding gap.

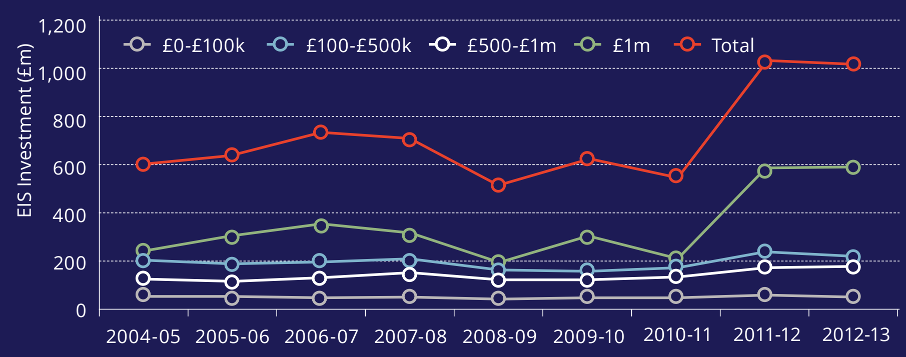
INVESTMENT BY STAGE (UNQUOTED EQUITY INVESTMENTS)



Source: Beauhurst

The chart below shows EIS investment between 2004-05 and 2012-13. Total investment increased up until 2006-07, after which point there were generally weaker years (particularly at the height of the crisis in 2008-09). Investment increased sharply in 2011-12 to more than £1 billion, and remained at a similar level in 2012-13; if the £84 million of SEIS investment is included the total funding can be seen to have increased further.

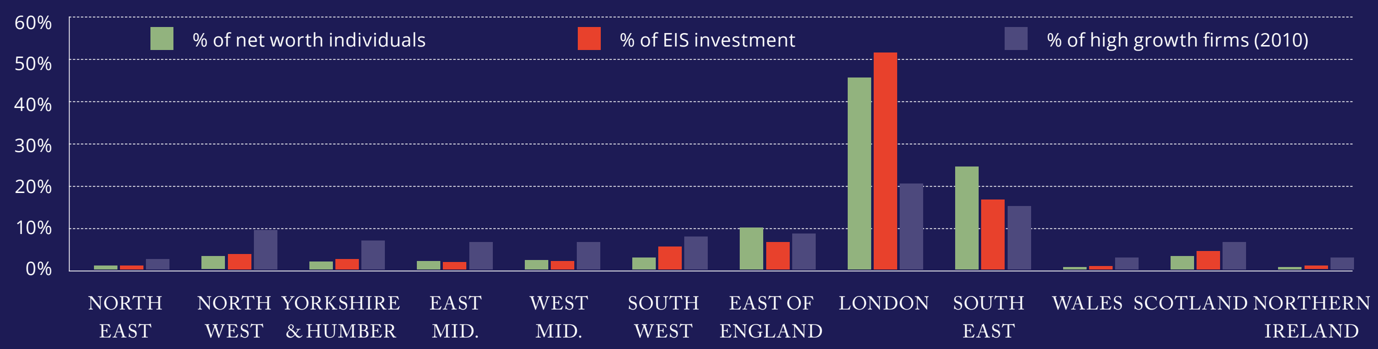
EIS INVESTMENT BY SIZE OF DEAL



Source: HMRC

What is notable in the chart above is the extent to which total investment is driven by the very largest deals. Throughout the series it is the £1 million+ investment sizes that determine the growth of the overall series; these account for around 10% of deals but more than 50% of investment. Below £100,000 there is a relatively long tail of smaller deals: more than 40%; but between them they account for less than 10% by value.

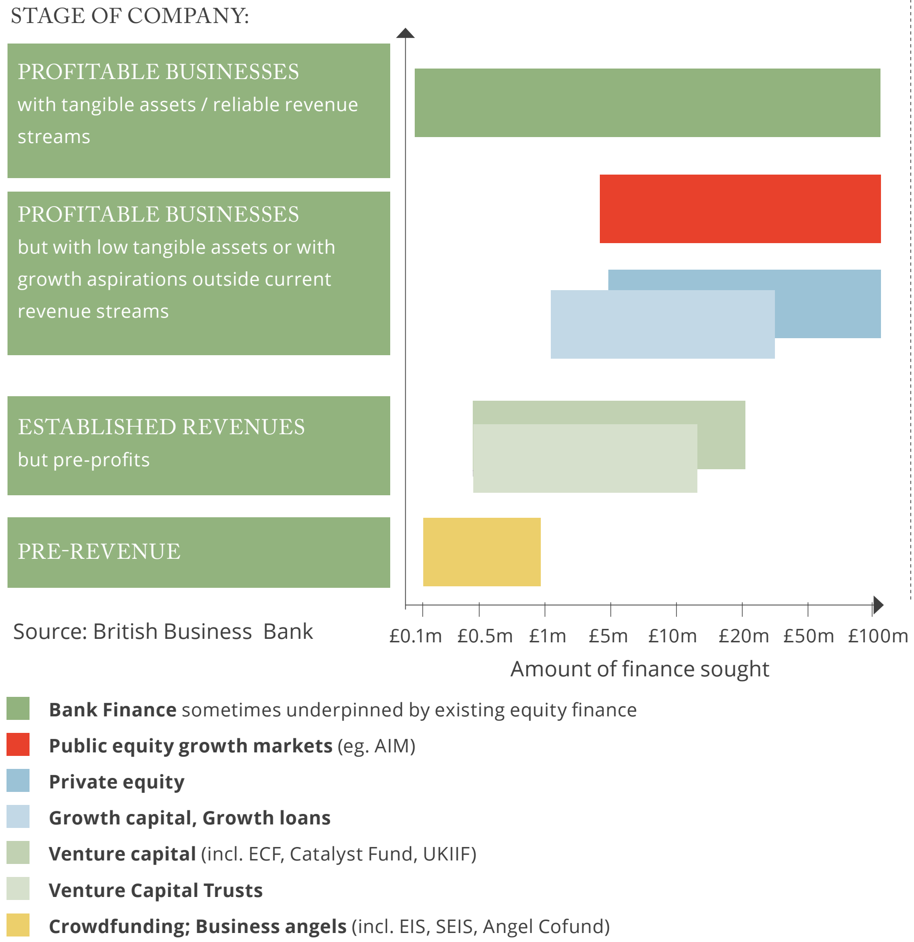
DISTRIBUTION OF WEALTH, EIS INVESTMENT & HIGH GROWTH FIRMS BY REGION (2009/10)



Source: ONS; HMRC; Datamonitor

"Tax reliefs potentially available via EIS should be considered a bonus and should not be taken in to account when considering the validity of an underlying investments. EIS investments should stack up as a credible investment opportunity whether providing tax reliefs or not" **Andrew Aldridge, Deepbridge Capital**

THE FUNDING ESCALATOR



Source: British Business Bank

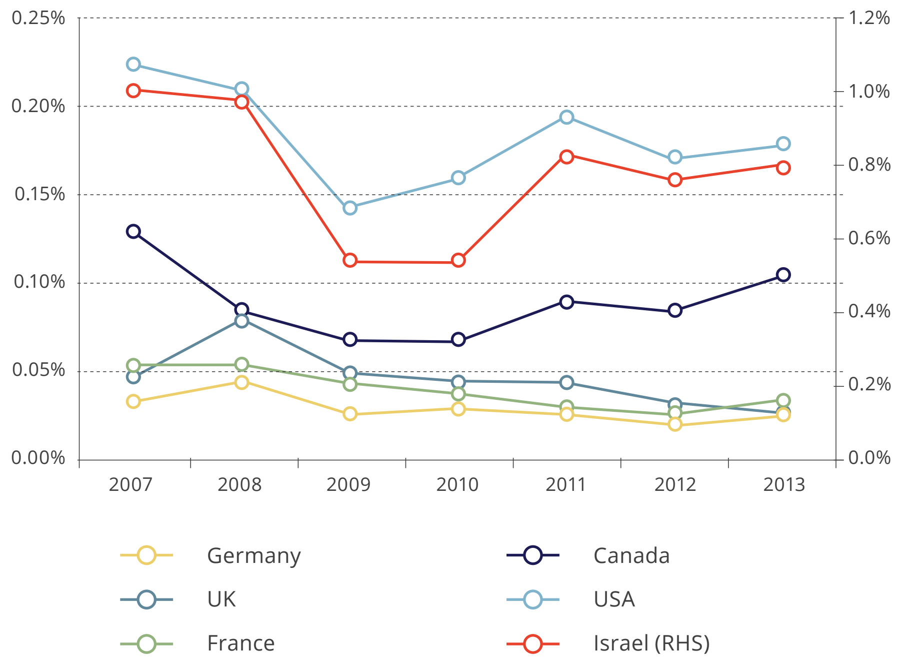
THE FUNDING ESCALATOR

There has traditionally been a "funding escalator" that companies would climb as they grew and matured, with EIS investments near the bottom of that escalator.

Viewing EIS and its place on the funding escalator helps to put it into context. One can easily make a few important assumptions looking at this diagram:

- EIS is more risky than most mainstream investments
- EIS funding is important for a healthy, growing economy
- EIS lends itself to smaller funds and smaller deal sizes

INVESTMENT AS % OF GPD, SELECTED COUNTRIES (2007-2013)



Source: EVCA; NVCA; Industry Canada; IVC; OECD

INTERNATIONAL PICTURE

As an interesting aside, despite the seemingly low amounts of equity fundraising, the UK actually has a better developed equity culture than much of the rest of the world, but still lags behind the US, which also has a much better record of developing businesses – in particular growing business to much larger sizes than we do in the UK.

The overall picture is one where the UK has historically been slightly above the major European nations, but significantly behind North America and Israel. It is clear that much more can be done to increase venture investment, in the UK and elsewhere in Europe, to close the gap to the leaders. This is an issue that has been identified by think-tanks and policy makers such as the Policy Network and the British Business Bank and points to the possibility of more initiatives to grow the market.

HMRC STATISTICS

The most reliable source of information for the amounts raised via EIS are the statistics HMRC collects from the EIS1 and SEIS1 forms that companies submit to HMRC whenever they issue EIS qualifying shares. The statistics provide information on the number of companies raising funds, number of subscriptions and amounts raised through the EIS and SEIS.

Previously they were published annually, but in 2015 HMRC started publishing them quarterly in response to the growing interest in the scheme - another indicator of the rising popularity of EIS.

The figures are subject to small (usually upward) revisions due to the late submission of forms (companies have a period of several years to submit their forms, but the vast majority are received within three years). The data that follows is based upon the October 2015 and January 2016 publications (the latest available at the time of writing).

AMOUNTS RAISED

From 2000-01, there was a gradual decrease in the amount of investment post the 'dot-com' bubble, up to 2004-05 when the amount of investment started increasing again. From 2007-08 to 2008-09 there was a sharp decrease in the amount of investment, most likely due to the economic recession and to additional eligibility restrictions for qualifying companies (from 19 July 2007, limits on company investment of £2 million and the number of employees, of fewer than 50 employees, were introduced). The change in the Income Tax relief from 20% to 30% in 2011-12 and the introduction of the Feed-in-Tariffs (FiTs) initiative from April 2010 (resulting in large amounts of investment into the renewable energy sector) both attracted investment into EIS.

In 2012-13 most trades attracting FiTs or overseas equivalents were excluded from eligibility for EIS, and companies benefiting from alternative energy subsidies have not been able to benefit from venture capital schemes since July 2014. The expansion of VCTs in 2012-13, such as the increase in the annual EIS investment limit for companies of £5 million, also attracted significant investment.

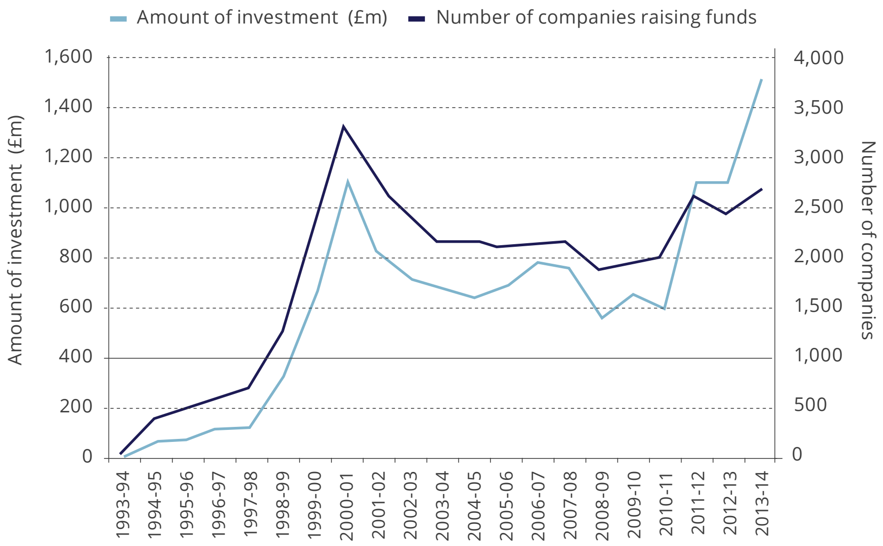
KEY POINTS

Since the Enterprise Investment Scheme (EIS) was launched in 1993-94, over 22,900 individual companies have received investment through the scheme and over £12.3 billion of funds have been raised.

The data for 2013-14 shows that 2,795 companies raised a total of £1.6 billion of funds under the EIS scheme. In 2012-13, 2,470 companies raised £1,033 million of funds.

Revised data for 2013-14 shows that companies raising funds for the first time under the scheme raised a total of £872 million compared with £576 million in 2012-13.

AMOUNT OF FUNDS RAISED VS. No. OF COMPANIES (1993-2014)

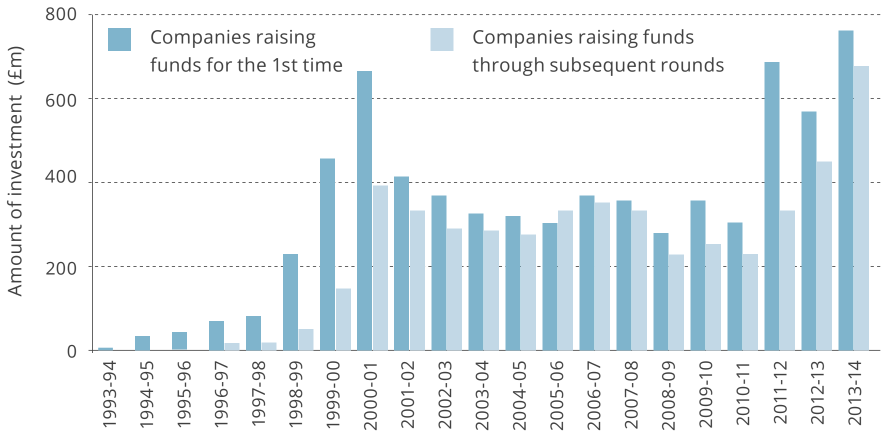


Source: EIS1 forms

EIS: NEW INVESTMENT

The majority of investment through the scheme (58%) since the inception of EIS was invested into companies raising EIS funds for the first time. The exception to this was 2005-06 when a slightly higher proportion of EIS investment was into already established companies (53%). The proportion of funding raised in 2013-14 by companies using EIS for the first time was 56%.

AMOUNT OF INVESTMENT RECEIVED THROUGH EIS (1993-2014)



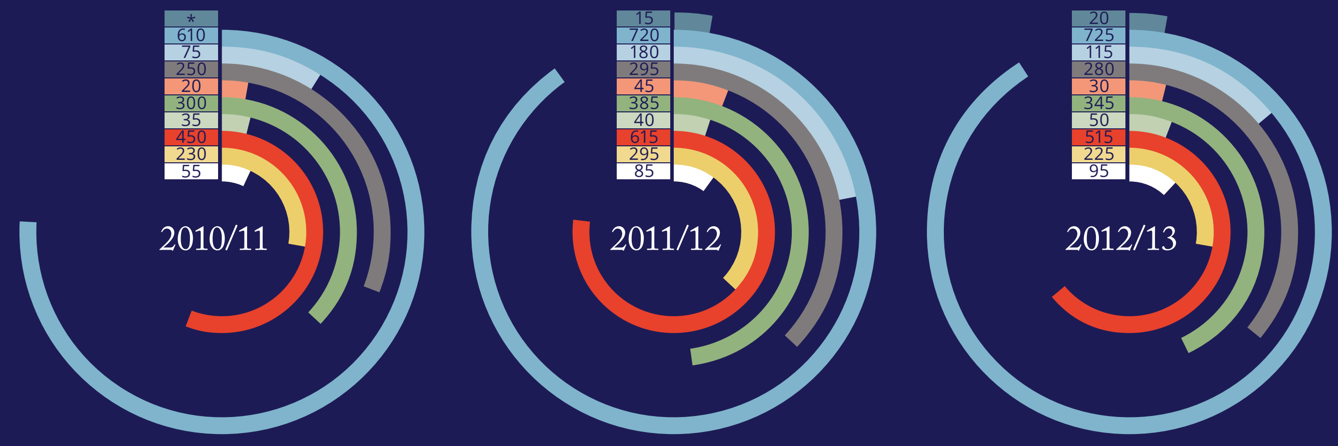
Source: EIS1 forms

The rules are designed to ensure that all the money flows to companies that would struggle to raise capital otherwise, but of course it is gratifying to see so many new businesses being helped by the scheme.

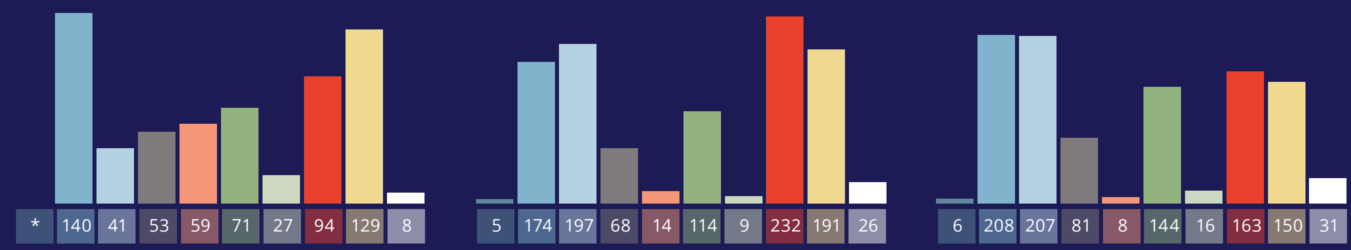
TOTAL No. OF COMPANIES VS. AMOUNTS RAISED (£M)

	2010/2011	2011/2012	2012/2013
No. of companies	2,025	2,675	2,395
Amount raised	548,8	1,032	1,015.5

No. OF COMPANIES AND AMOUNTS RAISED BY INDUSTRY* (2010-2013)



FUNDS RAISED BY INDUSTRY (£M):



Source: HMRC

EIS INDUSTRY

The following analysis looks at the data published by HMRC covering the number of companies and funds raised for the 2010/11, 2011/12 and 2012/13 tax years. Looking at the data, we have tried to pull out some interesting trends.

The table shows the number of companies and amount of EIS funds raised by each industry over the period 2010-2013. In those three years, there have been a large proportion of hi-tech companies that raised EIS funds, with business services and distribution, restaurant and catering industries not far behind.

In total, there has been a growth of 18% in the number of companies raising EIS funds from 2010 to 2013. However this hides the 32% growth from 2010/11 to 2011/12 and then a 10% drop in the subsequent tax year. In the amount of funds raised there has been an 85% growth over the whole period, with 88% growth in the first period and a small 2% drop in the second. The declines in fund raising are coming from industries such as construction, which experienced a 45% drop in the amount raised and a 33% drop in the number of companies raising funds from 2011/12 to 2012/13, along with business services and recreational activities seeing drops. Much of the company and funds raised growth has come from transportation & communication in the 2012/13 tax year. The renewables story can be seen in the growth of funds raised in the energy and water supply sector, and although there are still opportunities to get exposure to this sector via EIS (for example, by investing in companies who carry out the installation and maintenance of renewable energy projects) we expect to see this sector's share of funds raised to decline from this point onwards.

There are EIS managers out there who have developed specialist EIS funds that focus on particular sectors, such as hi-tech companies, manufacturing or restaurants.

We can also use this data to estimate the average funds raised by each company.

AVERAGE FUNDS RAISED BY INDUSTRY: (£M)

	2010/11	2011/12	2012/13
AGRICULTURE, FORESTRY & FISHING	*	313	280
HIGH TECH COMPANIES	210	243	287
ENERGY & WATER SUPPLY	549	1095	1807
MANUFACTURING	214	233	288
CONSTRUCTION	2950	329	270
DISTRIBUTION, RESTAURANTS & CATERING	237	296	419
TRANSPORT & COMMUNICATION	771	238	328
BUSINESS SERVICES	210	377	316
RECREATIONAL ACTIVITIES	561	646	668
OTHER SERVICES	1509	305	325

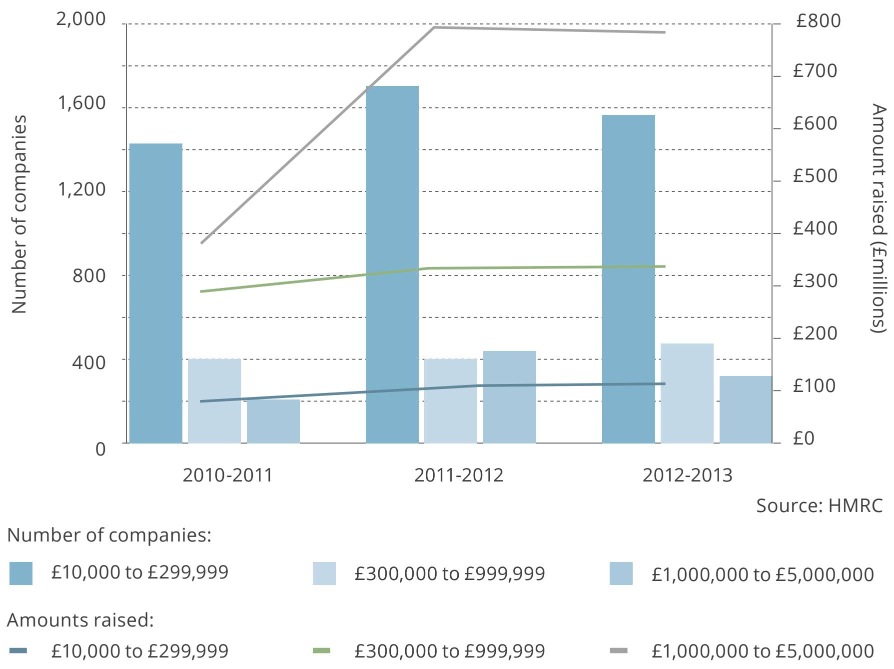
*Figures published in January 2016 by HMRC, latest annual statistics available in December 2015

"The EIS industry has seen a lot of changes over the last 12 months. However, it remains the UK's flagship policy for incentivising investment into smaller businesses" **Andrew Sherlock, Oxford Capital**

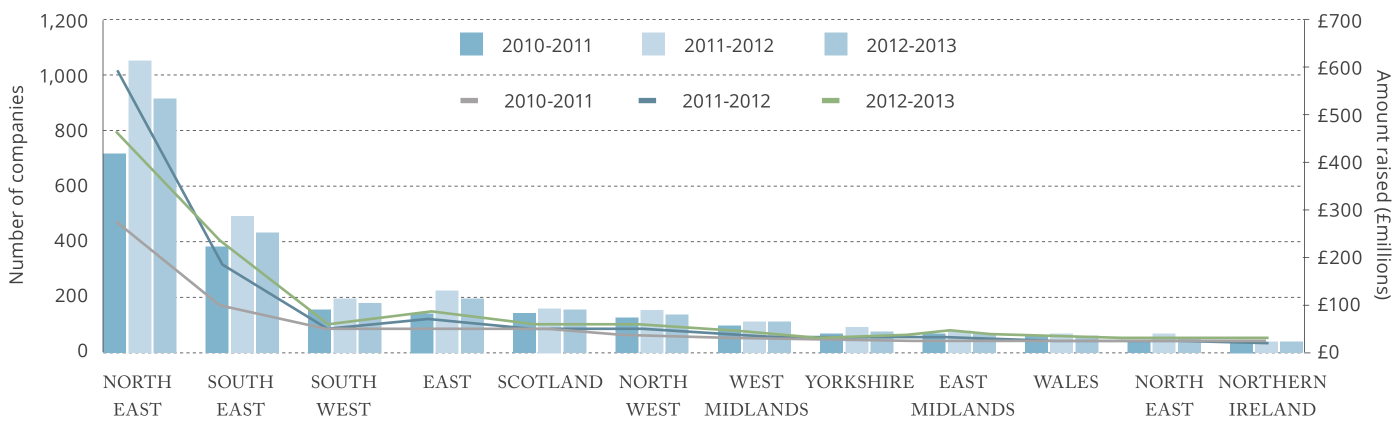
The majority of industries have increased the average funds raised by each company, with the exception of construction, business services, agriculture, forestry & fishing and other services. The significant growth in the amount of funds raised by the transportation & communication mentioned earlier isn't necessarily to do with more companies entering this sector but the fund raise sizes getting larger for each company. This proves that EIS is a valuable source of growth funding for this industry.

The chart to the right covers the number of companies and amounts of funds raised by size of funds from 2010-2013. The majority (66%) of companies raising funds over the entire period have raised £10,000 to £299,999 each year. On the other hand, we can observe that the greater volume of funds raised occurred at the £1,000,000-£5,000,000 range.

No. OF COMPANIES & AMOUNT RAISED BY FUND SIZE (2010-2013)



No. OF COMPANIES AND AMOUNTS RAISED BY REGION (2010-2013)



Source: EIS1 forms

The chart above shows the number of companies and amount of funds raised in EIS investments by region in the UK from 2010-13. London and the South East take the lion's share. As we pointed out earlier, this could be skewed by the number of businesses that have their registered headquarters in London, but it would not change the overall picture.

However, looking at the percentage increase by region, it does indicate that there are areas outside of London that are gaining in popularity and confidence for economic growth. The South East, North West, East England, East Midlands, Wales and Northern Ireland have all had a significant increase in the total funds raised from 2010/11 to 2012/13. It is possible to find EIS managers who specialise in a particular region, giving investors options to invest in their own region, or perhaps to diversify geographically within the UK.

% CHANGE IN FUNDS RAISED BY REGION 2010/2013

S.E. ENGLAND	156%	E. ENGLAND	87%	SCOTLAND	45%
E. MIDLANDS	141%	W. MIDLANDS	82%	SOUTH WEST	44%
N. IRELAND	139%	LONDON	73%	YORKSHIRE	37%
N.W. ENGLAND	111%	WALES	71%	N. ENGLAND	-12%

CONCLUSIONS

- Overall, there has been a growth of 18% in the number of companies raising EIS funds from 2010 to 2013
- Declines in fund raising from 2011/12 to 2012/13 came from industries such as construction (45%), business services (30%) and recreational (21%)
- 66% of companies raising funds over the 2010 to 2013 period have raised £10,000 to £299,999 each year
- Growth seems to be happening in virtually all parts of the UK

INNOVATIONS

There have been a number of innovations in the market over the last few years. These have been aimed at making EIS investment quicker, simpler and easier for advisers and their clients. We asked some of these innovators to outline their propositions here. They are co-sponsors of the report, along with the headline sponsors on pages 47 to 57. As mentioned at the beginning of the report, these sections are provided to help cover the cost of production and printing of the report.

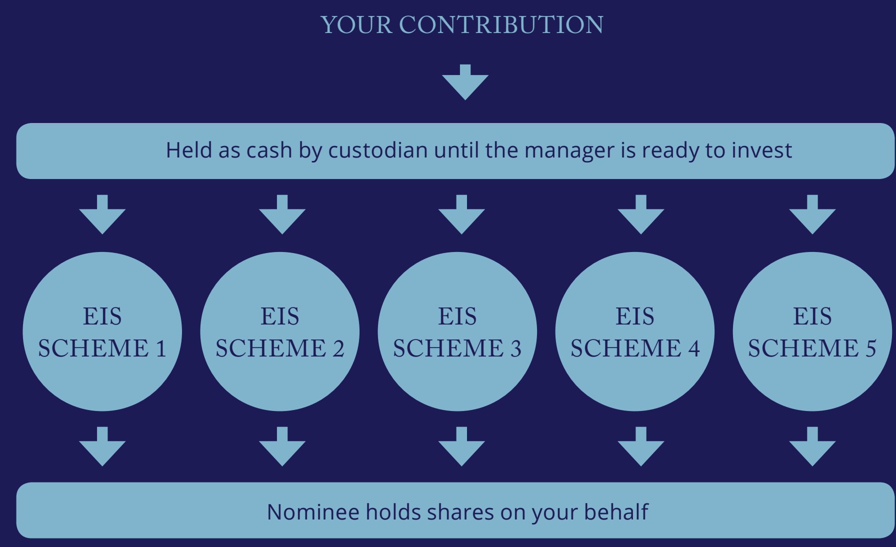
We also touch on promoters of EIS products at the end of this section and the EIS diploma. The diploma is well established, but included here as another resource for advisers to go to, to help get a more technical grounding of the sector.

KUBER VENTURES

Launched in 2012, the Kuber Ventures alternative investment platform provides advisers and high net worth investors with the ability to create portfolios across different Fund Managers for EIS, SEIS, and BPR investments. Through a single application investors can create a diversified spread of qualifying investments with complete confidence.

They operate a single portal through which investors can access a number of EIS/SEIS/BPR funds and create well diversified portfolios and benefit from simplified administration, robust investment governance and consolidated online reporting. Accessing this via the platform Investors may select individual funds or choose to achieve further diversification by investing in one of the Kuber strategies available. The strategy choices include: Diversified Growth, Business Property Relief, Asset Backed, Seed & Early Stage Growth, Mature Growth, Long Term Investment Focused, Media and Seed EIS Strategy.

In our view the Kuber platform offers some distinct advantages. The administration of an EIS portfolio is greatly simplified, with only one application form and payment required it provides the ability to see a client's portfolio, with half yearly valuations, all in one place. They have also negotiated much lower minimum investment levels with the investment providers, making it much easier to build a diversified portfolio. There is an option for investors to make monthly contributions, a first in the EIS market as far as we know. Finally, they also research and curate their panel of funds,



from the outset Kuber has worked with Allenbridge and more latterly with Hardman & Co, providing advisers with an additional layer of due diligence.

The Kuber platform is competitively priced. They charge an initial fee of 1.5%, an AMC of 0.24% and £9 per investment, plus some flat fees for the administration of regular contributions. This will be on top of the EIS fund manager's charges, although where possible Kuber do negotiate discounts with the managers who are listed on the platform. At the time of writing most of the established managers on the platform had reduced their initial charge by 0.99%, but some discounts were as high as 4.43% (actually making it cheaper to invest via Kuber).

Kuber undertakes due diligence on its participating managers and while this does not represent the whole market, it is the flip side to having a third party curate the investment panel, nonetheless an added value to the adviser. From a compliance perspective, we think that advisers have to remember that it is their panel (if they use Kuber as such) and therefore they need to be confident that it is representative of the market. At the time of writing, Kuber offered a mix of Project Finance (investing in companies specifically created to carry out an EIS qualifying trade by the fund or portfolio) and Private Equity (EIS managers investing in companies which are not directly connected to the fund or portfolio according to their mandate) spread across the Media, Technology, Retail, Renewables and Generalist sectors. This was across 26 offers from 14 different managers, which we think is adequate to build a diversified portfolio, but advisers would need to keep this under review and have an awareness of the other offers available in the market.

"Advisers need to manage their clients' affairs efficiently and transparently. Having the tools to control risk and build portfolios of EIS investments, allows them to focus on their core business – providing advice"
Dermot Campbell, Kuber Ventures

LAWSON CONNER

MARKET LEADING **66%** year over year client growth*	REACH Compliance offering covers 22 jurisdictions	TRUST Integrated custody solution through Custody partner firm
LATEST REGULATIONS **AIFMD** comprehensive compliant fund management solutions	DIRECT ACCESS Competitive pricing & direct market access through Sapia (member of the London Exchange since 2013)	EXPERTISE Successfully launched a number of EIS/SEIS funds across different investment strategies
GLOBAL SOLUTIONS **USA** tailored solutions for US counterparties	EFFICIENCY One integrated compliance platform with dedicated legal, onboarding, monitoring, structuring & process teams	

Lawson Conner's platforms in the SME space have significantly reduced the barriers to the establishment of funds, both increasing fund choice for investors and improving the chances of obtaining funding for SME investee companies. At the same time, their platforms have reduced the risks of investing in EIS products by providing an established compliance infrastructure.

The EIS fund management industry was traditionally dominated by a number of established managers. The choice of managers was limited and large funds were focused on growing even larger, limiting choice for investors. Newcomers were typically prevented from entering the market by high launch and operating costs (which can run into the £400K-£1m range). Lawson Conner have attempted to address this issue by incubating 13 new funds, giving investors more choice and also helping to provide British companies more capital in niche areas which previously may have not been viewed as a prospective investment opportunities. Funds such as the Cyrus Precision Engineering EIS Fund II, specialising in British engineering, show how more niche investments can be brought to market.

Lawson Conner's risk management team operates some of the investments, providing an additional layer of governance and independence and reducing some operational risks. For small investment manager teams, perhaps raising their first and second round of funds, the level of fixed costs usually cannot be met by management fees from the fund. This cost can be reduced by using the Lawson Conner Platform: they have a team of more than 15 people who are actively involved in the administration, regulatory oversight and ongoing compliance. They also use a two tier investment committee model - the investment committee is completely independent and not incentivised by management fees or performance fees. The members of the Investment Committee are experienced Private Equity/ VC investors, Corporate Finance and M&A veterans. This level of expertise in the Investment Committee is not always found within emerging managers and should help to ensure better governance for the fund and protection for investors. They also help businesses navigate the complex regulatory landscape, helping to reduce time-to-launch and costs.

COINVESTOR

The CoInvestor platform allows investors to 'self-select' their own portfolio of EIS investments in a similar manner to the way they use major investment platforms to build their own portfolio of listed investments and funds in ISAs and SIPPs.

It does this by enabling private investors to co-invest alongside established EIS managers on a deal by deal basis - i.e. the investor invests in the individual EIS company, not the EIS fund. This represents a significant change from established practice whereby investors would only benefit from fund manager expertise on a discretionary management basis. Investors are able to retain freedom of choice when selecting their own portfolio but at the same time benefit from the stewardship of a professional fund manager with aligned interests.

For fund managers the platform is a way to access the increasingly large pool of 'DIY' or 'non-fund' investors. Managers can maintain control over the information that they display and the profile of investor that they wish to market their opportunities to. It also gives them the opportunity to leverage the investments that they are making via their funds to grow their business overall.

Financial advisers benefit from being able to assist those clients with whom they have an agreed EIS investment allocation requirement but who prefer to select their investments directly and not via funds. Subject to client agreement advisers are able to receive a 'facilitation' fee and are able to maintain oversight of their clients' direct EIS investment activity without straying into the territory of 'providing investment advice'.

*1 March 2014

"There is an increasing interest from Advisers looking for a new solution where they have advised their clients to utilise EIS as part of a wider investment allocation but those same clients are averse to investing in a fund structure" **Charles Owen, CoInvestor**

The language of the site is heavily tilted towards understanding investment risk and providing tools to mitigate it, primarily via co-investment and the adoption of a portfolio approach. The intention being to drive investment activity back towards the stewardship of professional fund managers. We see this as a good thing.

Of course the service comes at a cost. The platform itself charges 1% per transaction, but on top of that the fund manager may charge a transaction fee of between 0% and 5%, and a performance charge in line with that charged to fund investors. Notably, however, there is no ongoing annual charge and over the life of a typical EIS investment we would assess that investing via the platform is likely to be in the region of a third of the cost of investing in an EIS fund.

At the time of writing the platform has only just launched so we can't check the level that fund managers will be seeking to charge but CoInvestor inform us that some managers have already committed to charging 0% via the platform. If this turns out to be correct then the platform looks like a good value alternative to investing via a fund.

Again, as the platform is new, it was not possible to see individual investment offers, but we do think CoInvestor has a unique business model. This does have some of the risks of DIY investing attached to it, primarily around whether investors construct sufficiently diversified portfolios, but on the whole using CoInvestor would seem to mitigate a number of direct investment risks. Investors can take comfort that they are investing at a valuation on terms that the fund manager has negotiated, and benefit from the manager's due diligence and ongoing oversight.

It certainly takes the vast majority of the legwork out of single company investing, with the added flexibility of not having to commit to investing in an EIS fund.

GO IT ALONE	USE COINVESTOR
Where are you going to find good EIS investment opportunities?	Fund managers use tried and tested origination processes and review hundreds of opportunities each year.
How do you pick which company to invest into?	Fund managers carefully select the business they want to invest into having firstly fully understood the sector, the competition, the strength and experience of the management team and the real opportunity for growth and exit.
Are you investing on the right terms?	Fund managers have wide experience of negotiating appropriate investment terms.
Can you ensure that the company is properly funded?	As part of ensuring that their investee companies are likely to be successful fund managers will undertake a detailed assessment of financial forecasts, and if necessary invest a larger sum than was originally requested in order to ensure that the company is properly funded.
Do you know the right questions to ask before making an investment decision or can you afford to pay someone who does?	Having agreed terms fund managers commit to extensive and expensive due diligence prior to making a final investment committee decision.

More information can be found on their website *coinvestor.co.uk*

"Advisers need access to quality, consistent and transparent portfolio information to help build stronger relationships and add greater value to their clients" **Dr. Mark Payton, Mercia Technologies**

MERCIA TECHNOLOGIES

Mercia has developed a new innovation in the EIS market which recently won the 'Industry Game-Changer' award at the Growth Investor Awards. The platform, the Virtual Share Exchange ('VSE'), is designed to offer a degree of liquidity to investors within their tax efficient technology funds through providing a mechanism for allowing investors the opportunity to sell a portion of their EIS & SEIS shares held without a sale of the company itself – a key barrier within EIS investing into growth enterprise.

The VSE facilitates buyer and seller through an easy to navigate platform, allowing Mercia's investors and their advisers to quickly review all offers available on the portfolio companies held and, should they choose, opt for how many shares they would like to sell against the offer. The buyer of existing shares is Mercia's parent business Mercia Technologies PLC (backed by key institutions including Invesco, Woodford Investment Management and Baillie Gifford), which seeks to invest into the emerging stars from Mercia's portfolio as part of their 'Complete Capital' investment model. The platform, that has been built into Mercia's award winning Investor Centre (EISA Innovation Award), is supported by a messaging system which keeps the investor updated as to offer progress, amongst a range of other tools. Offers on the VSE are made at a discount to the current valuation, which is clearly illustrated to investors and advisers on the VSE for transparency.

"The role of the Virtual Share Exchange is not to provide investors with an early exit path, but to increase flexibility and provide a degree of liquidity. Some investors may need access to capital, others may want to release some of their gains after the qualifying period for EIS purposes; the offers available through the VSE simply give investors and their advisers more choice and control." Dr Mark Payton, Managing Director Mercia Fund Management and CEO Mercia Technologies.

There are currently 9 live offers on the VSE with an average return of 2.7 times initial investment (excluding all tax advantages), however all these investments were made less than 3 years ago which would mean a loss of tax reliefs if accepted. As an example, there is currently an offer for LM Technologies on the VSE for 4.8x return which reaches its three year holding point in March 2016. Here, the holding represents circa 20% of the total EIS portfolio and therefore should an investor opt to sell in a compliant manner at the 3 year point, can receive a near full return of capital whilst keeping their tax reliefs and maintaining the rest of their portfolio.

SEED EIS PLATFORM

Seed EIS Platform began when the Seed Enterprise Investment Scheme first launched in 2012. The platform uses crowdfunding technology to connect investors and advisers with tax efficient investments and allows users to filter opportunities by tax relief, stage of funding, investment sector and funds raised so far.

Within three years the platform has invested in 30 businesses with 40 rounds of investment, and has expanded their deal flow into EIS offerings, so it does appear that they have some momentum behind them.

As well as the online functionality, Seed EIS Platform also provide an additional layer of due diligence on the investments they offer. This is available in three tiers: bronze, silver and gold.

- Bronze offers confirmation of HMRC compliance, a test of the rationale of the business proposition and ensures the creditworthiness of the business;
- Silver receives a review by an external third party analyst and summary report;
- The Gold tier investments are reviewed by industry recognised analysts, such as MICAP, and give a whole of market report on the investment.

The due diligence report costs are covered by the investee company, and where no due diligence has been carried out advisers can request a report. It is also possible for advisers to contact investee companies directly via the platform.

The business faces the same conflict of interest that all crowdfunding platforms do – they take their fees from the sell-side and therefore much their focus is necessarily on distributing the investment opportunity and ensuring that fundraising targets are met. However, advisers and sophisticated investors of the kind who will be considering SEIS are familiar with this distribution model and comfortable with it. They understand the role the Seed EIS platform plays in the supply chain and know that if they want to build a long term business than they will be keen to ensure a good experience on the buy side as well.

We think that the online functionality works well and takes some of the burden off advisers who want to invest in this space. Intermediaries can add clients and act on their behalf, monitor their clients' activity within the platform, or view aggregated portfolios of tax efficient investments (whether they were made via the platform or not). Advisers can even have a mandate to approve transactions made by their clients.

There are a wide range of investments available and comparatively low minimum investments mean that building a diversified portfolio is relatively easy. We would suggest that this is absolutely necessary, given the high rates of failure for investments in early stage businesses such as these.

From a business process point of view, RDR compliant adviser fees can be agreed on (up to 3%) and commission reports are also available.

A development to look out for in 2016 will be the launch of their first discretionary managed portfolio. Advisers that may not be comfortable selecting investments for their clients may be happier placing their clients in the discretionary portfolio.

We think that Seed EIS Platform has identified that information flow is a problem for advisers in this space, and their hope is that centralising and aggregating information and administration will take some of the burden off advisers. Anything that reduces friction in the investment process must be a good thing, with the usual caveat that the investments remain high risk – no matter how easy the process gets!

"EIS and SEIS tax reliefs mitigate investment risk significantly, increasing access to seed capital and driving growth within the UK. Advisers looking to offer a single company approach for their clients will need the necessary tools" **Dan Rodwell, Seed EIS Platform**

PROMOTERS

There are also some distributors operating with advisers in the EIS marketplace. The biggest are RAM Capital and LGBR Capital. These firms will work with a small portfolio of EIS (both fund/portfolio offers and single company EIS) and do the leg work of going out and engaging with advisers on behalf of the managers. From the manager's perspective this saves them time and effort spent on non-core activities, and from the adviser's perspective the distributors offer product training, an additional layer of due diligence and a single point of contact for their EIS business. The cost of the service is borne by the investment provider (as part of their distribution costs) rather than the client or adviser. Both RAM and LGBR also offer VCT and BPR investments. Advisers only using these distributors will of course be limiting themselves to their offers and therefore need to keep an eye on the rest of the market.

THE ADVISER DIPLOMA

For advisers who are keen to extend their knowledge of EIS, the EISA in conjunction with tax and accountancy training provider Tolleys have developed an EIS diploma. The diploma consists of a home study course followed by an online examination and consists of four modules: an Introduction to EIS, an Introduction to UK Taxes, the Tax Reliefs and EIS Funds and Regulation. It is expected to be around ten hours of study time followed by a 30 question exam and costs £335. It's also possible to register as an EISA affiliate for £100 annually to receive notifications of any changes to the regulations as well as updates from the EISA spring and autumn technical seminars. The obvious benefit is that advisers can evidence to clients and compliance departments that their technical knowledge on the topic of EIS is up to date.

SEIS ANALYSIS

This section takes a look at the SEIS portfolio investments in the market, to give advisers a better idea of what the market looks like. Data has been provided by the MICAP Fund Finder, where an up-to-date register of the whole tax-advantaged investment market can be found.

Although this report focuses on the EIS sector, the Seed Enterprise Investment Scheme (SEIS) came into the market in 2012 to provide tax-advantaged investment into smaller, earlier stage companies than EIS. After an initial 'probation' period the scheme was made permanent in 2014.

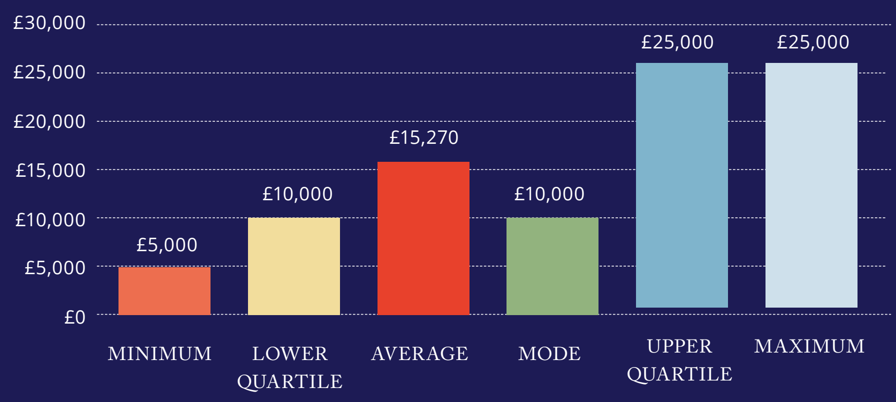
Qualifying companies must have fewer than 25 employees, less than £200,000 in gross assets prior to investment and must have commenced a new trade less than two years ago. They can only receive £150,000 of investment via SEIS. Previously they had to have spent at least 70% of their SEIS money before they could raise funds via the EIS, but this rule was removed in 2015.

SEIS attracts Income Tax relief at 50%, and up to 50% of the tax liable on a capital gain can be written off if the gain is invested in a SEIS. This is in addition to CGT deferral. The other reliefs are the same as EIS. These reliefs are obviously very generous and reflect the increased risk of investing in these companies. There is an annual limit of £10,000 for investors.

SEIS Tax Reliefs:

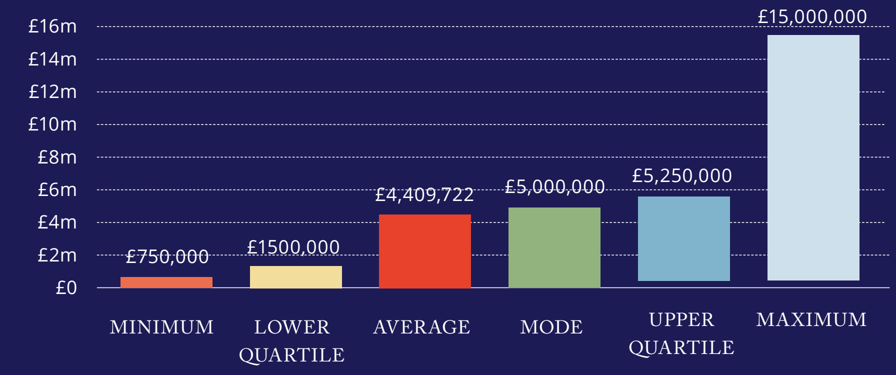
- 50% upfront tax relief
- No Capital Gains Tax
- 50% CGT exemption if the gain is invested in an SEIS qualifying investment
- Loss relief
- IHT relief (via Business Property Relief after a two year holding period)

MINIMUM SUBSCRIPTION AMOUNT (2015)



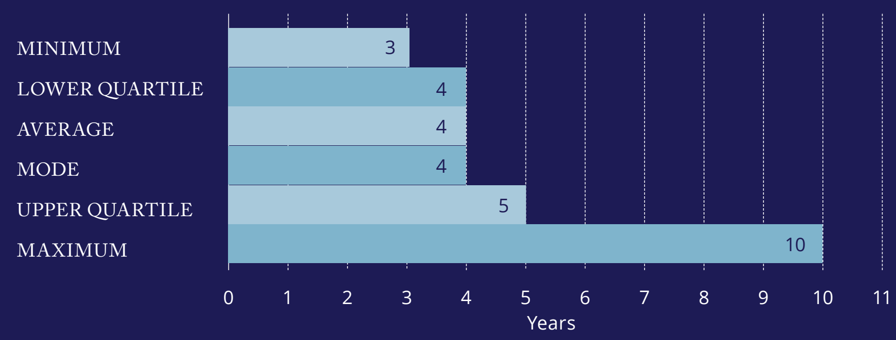
The annual investment allowance for SEIS tax relief is lower than EIS, at £100,000 per year and the investee company limit is also lower, however the minimum subscription levels are similar to the EIS investments. Single company investments will most likely come at a smaller subscription level, especially if they are accessed through a crowdfunding platform – the role of crowdfunding platforms can be found on page 35.

FUNDRAISE AMOUNT (2015)



Fundraising targets for SEIS funds are much lower than their EIS counterparts, with the average target just over £4 million and the largest fundraise in the market being £15 million – much smaller than the largest EIS fund at £53 million.

EXPECTED INVESTED DURATION (2015)



SEIS shares also have a 3 year holding period for the reliefs to be retained. Most portfolio investments aim to exit around 4 years, with one looking at a 10 year investment horizon. SEIS funding is often followed on by EIS or VCT funding, so if an investee is growing and performing well, it may make sense to invest in them again.

SECTOR SPLIT (2015):

- 36% MEDIA & ENTERTAINMENT
- 31% TECHNOLOGY
- 3% PHARMACEUTICALS & BIOTECHNOLOGY
- 23% GENERAL ENTERPRISE

SUCCESS TO DATE

At the time of writing, according to HMRC, £250 million has been raised for over 2,900 companies since the inception of the scheme. Overall data looking at the types of single companies can be found in the HMRC statistics website, but there are also portfolio services (referred to as funds, although as with EIS they are technically managed portfolio services) that can give investors an exposure to a diversified holding of SEIS qualifying companies and benefit from the expertise of a fund manager.

Many SEIS investments do not take an initial charge and deal fee, though those that do tend to take a large percentage. Most funds charge fees to the investee companies rather than the investors.

Exit hurdles and performance fees are similar to EIS portfolio investments. Finding investments that can consistently perform extraordinarily is likely to be more difficult with SEIS than EIS, but of course the potential for growth is much higher than EIS.

Looking at the targeted returns, none of the portfolio investments pay out dividends (this is expected, SEIS shares do not qualify for tax-free dividends). Instead, fund managers aim to return capital at the end of the investment period. In order to make returns more comparable, we annualised the stated targeted returns for 3, 5 and 10 years, as well as their target investment duration periods.

Over the short term, a 3 year annualised targeted returns ranges from 28% to 138% per annum. In the 10 year holding period, annualised returns range from 8% to 30% per annum. Compared to the target returns of EIS portfolio companies, the low end of the targets seems to be very similar, but the higher end of the market looks very different – with SEIS companies targeting higher returns (as it should be).

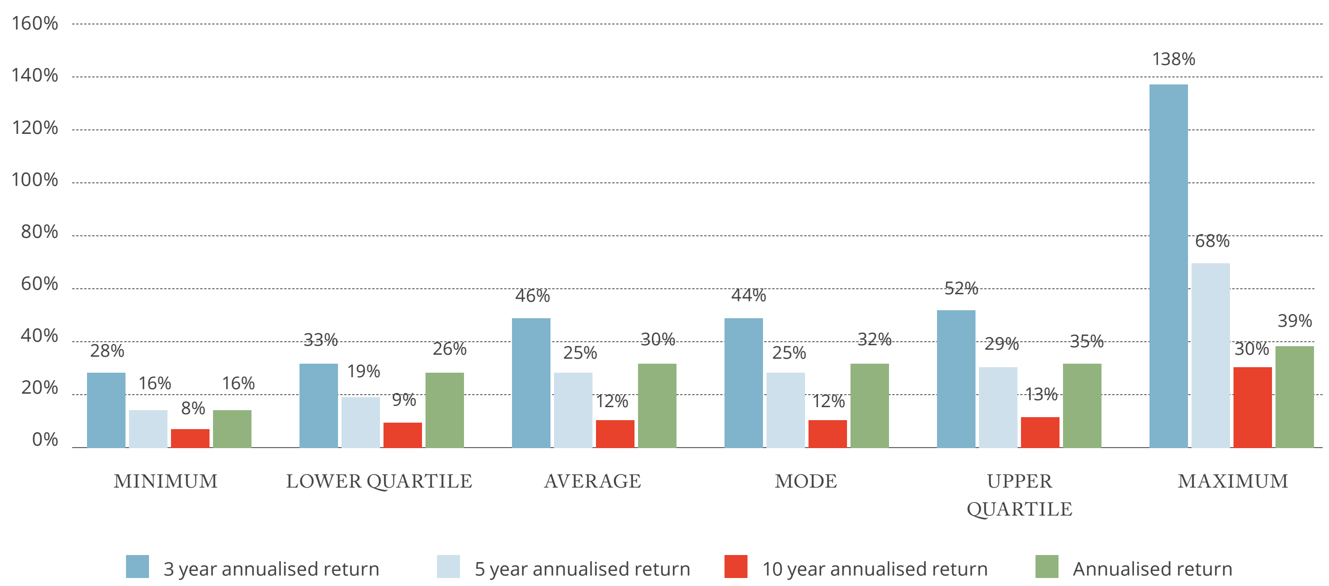
SEIS PORTFOLIO INVESTOR CHARGES AND FEES (2015)

	MIN	LQ	AVG	MODE	UQ	MAX
INITIAL CHARGE (%)	0	0	3.0	0	5.4	10
INITIAL DEAL FEE (%)	0	0	0.2	0	0.0	3
ANNUAL AMC (%)	0	0	1.5	0	2.0	5.6
ANNUAL ADMIN CHARGE (%)	0	0	0.3	0	0.4	3
EXIT PERFORMANCE FEE (%)	0	20	23.2	20	30.0	50
EXIT HURDLE (%)	0	100	124.3	110	112.5	1125

CONCLUSIONS

Despite the smaller investment and larger tax reliefs, the details for SEIS and EIS funds do not look too different. The potential returns and the tax reliefs are higher for the same (or even lower) costs than EIS, but of course the risks are much greater owing to the size of the qualifying companies. The big issue for investment providers is spreading the cost of sourcing and securing opportunities across such small fund raising amounts.

ANNUALISED TARGETED RETURNS (2015)



SOCIAL INVESTMENT

SOCIAL INVESTMENT TAX RELIEF

Social Investment Tax Relief (SITR) is based on the existing EIS reliefs, so it is worth mentioning the developments in this nascent sector in this report. At the moment the limit on the amount and investee organisation can receive is capped at £250,000 - £275,000 (the actual limit is set at €344,827 and so depends upon the prevailing exchange rate).

However, the government is proposing to lift the limit on the maximum investment per investee organisation to £5 million per year (up to £12 million in total), subject to EU State Aid approval. This change could open up the market and make specialised SITR funds a viable proposition for the first time.

THE RELIEFS

The reliefs are the same as EIS, subject to a minimum three year holding period:

- 30% upfront tax relief
- No Capital Gains Tax
- CGT deferral if the gain is invested in an SITR qualifying investment
- Loss Relief
- IHT relief (via Business Property Relief after a two year holding period)

The intention was that by designing SITR around an existing set of reliefs, it would speed up acceptance, both by the EU and advisers and investors.

QUALIFYING INVESTEE ORGANISATIONS

Again, the qualifying criteria are based on EIS - there is a maximum of 500 employees and £15 million gross assets. However, to qualify for SITR each investee organisation must have the legal status of one of:

- Registered Charity
- Community Benefit Society
- Community Interest Company
- Accredited Social Impact Contractor

The aim of this is to ensure that any investment is put to work in genuine social impact organisations that are already regulated in some way - so there is no additional workload for HMRC. The maximum limit on the number of employees is somewhat controversial: it feels rather artificial as it is the legal status that is the guarantee that the organisation is genuine. Indeed, many social impact organisations have high numbers of employees (these will often be low paid, part time staff).

QUALIFYING INVESTMENTS

Here is where SITR really differs from EIS. As equity investment is very often not suitable for charities, SITR also allows investment into unsecured debt. The debt, however, must not be secured against any assets, must not be repayable within the first three years and must not be preferred to any other investment instruments in the event of a winding up.

SITR AND EIS MANAGERS

We wanted to find out if EIS managers were preparing to enter this market and so, in conjunction with the social impact investment champion Big Society Capital, we surveyed the managers to ascertain their levels of knowledge and readiness to develop SITR funds, and then held a roundtable event in October 2015 to discuss the findings.

In the survey we encountered a range of responses, from those who had never heard of SITR, via those who had considered it and decided that it was not for them, to those who have a product ready to launch, subject to approval for the new higher limit. The full survey results can be found on our website, *www.intelligent-partnership.com*, but the key question around firms' readiness to enter the market is summarised in the chart on the right.

At the roundtable event itself, Greg B. Davies from Barclays kicked off by talking about some of the behavioural drivers for investors who are interested in social impact funds. His research makes it clear that there is a demand for these products, provided that the industry makes it easy for investors.

SURVEY TO EIS MANAGERS

"All of the current social investment fund managers agreed that when sourcing deals it was crucial to start with the quality of the investee organisation's management, and the impact they wanted to make – and then look at the economics"

In our opinion this will require joined up thinking on the part of both providers and advisers, and we can easily see how the tools Greg and his team have developed could eventually be used by advisers to determine how much a client might want to allocate to social impact investing. The other thing that jumped out from his research was that many investors expect market-level returns from social impact investments - which to date has not been possible by and large, and is something that consumers will have to be educated on.

Perhaps the most encouraging thing to come out of the research is that many consumers would make allocations to social impact investments from their current cash holdings. This is a win-win-win. The consumer (traditionally overweight cash) will put money to work, society should benefit (via the social impact organisations) and the investment industry brings new money under management. Social Impact investing won't cannibalise charitable donations OR traditional investments.

We also had a spokesperson from HM Treasury. Practically everybody in the room agreed that the single most important change that could be made in order to encourage the development of SITR retail investment products would be the lifting of the limit that can be invested, but today's update from HM Treasury suggests this change is at least a year away (which would be October 2016). After focusing on achieving State Aid approval for the VCT and EIS schemes, HM Treasury think that it's unlikely we will get approval for the higher limit on SITR in the next six to twelve months. A Social VCT would then be considered once the limit for SITR was agreed. Securing approval for these schemes remains a priority for HM Treasury.

Finally, some of the current managers of social investment funds shared their experiences to date. They have not had a problem securing deal flow in terms of volume, but getting larger deals that make the business more scalable has been harder for them. We also learned that there is a point where returns flatline - very, very roughly at a level of return of around 10%, taking on more risk doesn't necessarily increase the level of return. This makes portfolio construction harder (there are no stellar performers that offset losses). However, the underlying investments might be less risky than intuition would suggest, because the management teams are so committed. In one case study that was shared with us the investee organisation failed, but still raised additional funds to pay back a small, unsecured debt simply because they felt it was the right thing to do.

All of the current social investment fund managers agreed that when sourcing deals it was crucial to start with the quality of the investee organisation's management, and the impact they wanted to make - and then look at the economics.

In summary, the UK is seen as a leader in this space with the combination of the Big Society Capital as market champion (and cornerstone investor) and the tax reliefs. There is demand from investors, there are organisations that can put the capital to work and some EIS managers are ready to launch products to bridge the gap between the two. However, while there are some funds already operating, approval for increasing the limit on investment will have to happen before launching retail SITR funds becomes viable for EIS managers. But when that does happen, advisers will find an interesting new range of products to invest in.

CROWDFUNDING AND EIS

Equity crowdfunding has been disruptive in the venture capital space, opening up early stage, small company investing in the UK since the first platform, Crowdcube, launched in 2010. The ease of an online platform, lower entry levels and the non-financial benefits has driven over £183 million (though not all EIS qualifying) at the time of writing through UK platforms (AltFi Data). Crowdfunding has also opened up to EIS and SEIS tax reliefs, as the companies offering investment opportunities often fit within the qualifying criteria. We wanted to find out just how the advent of online investment platforms has influenced EIS and SEIS investment.

Data has been provided by Crowdnetic, a market data provider in the US and Europe. Their technology allows users to analyse market data by sector, security type and geography. This tool gives users the ability to view real time listings across several UK platforms, tracking how much and when an investor chooses to commit capital to a company. You can also view company valuations by the same criteria. We've looked at equity crowdfunding fundraises from May 2014 to October 2015 across 9 platforms in the UK.

In total there were 191 fundraises that were eligible for EIS or SEIS tax relief. 88% of EIS and SEIS offers on the platforms successfully met their target fundraise, with over £63 million of capital committed to EIS qualifying companies and £105,202 committed to SEIS qualifying companies. According the HMRC statistics, £1,563 million was raised by EIS companies in the 2013/14 tax year. It is likely that even with fastest growing crowdfunding platforms they will only play a small role in EIS fundraising for the time being. However, that is not to say they can't be a great way to access these tax reliefs for smaller retail investors.

In our research of alternative finance platforms we found 31 crowdfunding platforms in the UK, with 20 offering access to these tax reliefs. If you consider that the minimum investment levels for these platforms ranged from £1 to £2,500, investors can use this route to diversify across a large number of EIS or SEIS companies. However, accessing these investments in this way means you don't benefit from the expertise of a professional fund manager and additional due diligence is needed to be carried out on each opportunity and platform. You can read about the risks, mitigations and considerations that need to be kept in mind when looking at crowdfunding by reading our Alternative Finance Industry Report 2015 by visiting *www.intelligent-partnership.com.*

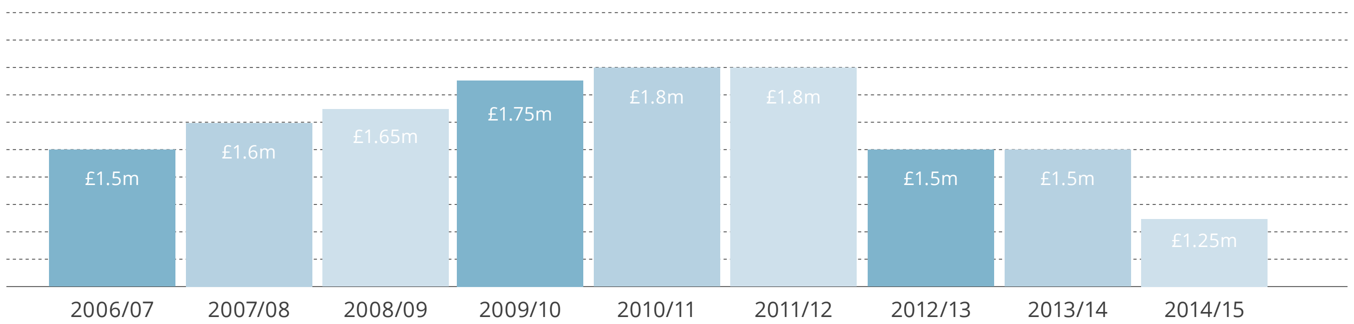
CHANGES TO PENSIONS

It is worth considering EIS and pensions, and how they interact with each other - especially in the light of so many recent changes to the rules and regulations governing pensions.

LIFETIME ALLOWANCE

The lifetime allowance has come down from a peak of £1.8 million in 2011 to just £1.25 million today (note that technically this allowance can be exceeded, but anything above the allowance will be subject to a hefty 55% tax charge.

LIFETIME ALLOWANCE (2006-2015)



The limit will be reduced even further to £1m in 2016/17, and then linked to the Consumer Price Index. Interestingly, if the original £1.5 million had been linked to RPI, the limit would be approximately £2 million.

Source: HMRC

£1 million might sound like a lot of money, but at current rates it would only buy an annuity worth approximately £33,000 a year (before tax) for a 65 year old - for many people that might not be enough for the lifestyle they want.

The following two charts show that advisers will have many clients who will potentially reach, or breach, the £1.25 million limit (note that both assume no further contributions).

FUTURE PENSION POT SIZE

YEARS TO RETIREMENT	FUND GROWS AT:			
	2%	4%	6%	8%
3	£ 1,177,902.92	£ 1,111,245.45	£ 1,049,524.10	£ 992,290.30
5	£ 1,132,163.51	£ 1,027,408.88	£ 934,072.72	£ 850,729.00
7	£ 1,088,200.22	£ 949,897.27	£ 831,321.39	£ 729,362.99
10	£ 1,025,435.37	£ 844,455.21	£ 697,993.47	£ 578,991.86
15	£ 928,768.41	£ 694,080.63	£ 521,581.33	£ 394,052.13
20	£ 841,214.17	£ 570,483.68	£ 389,755.91	£ 268,185.26

ANNUAL GROWTH RATE REQUIRED TO FUND FOR £ 1.25M

EXISTING FUND VALUE	TERM TO RETIREMENT			
	5 YEARS	10 YEARS	15 YEARS	20 YEARS
£100,000	65.72%	28.73%	18.24%	13.46%
£200,000	44.27%	20.11%	13.00%	9.60%
£300,000	33.05%	15.34%	9.98%	7.40%
£400,000	25.59%	12.07%	7.89%	5.86%
£500,000	20.11%	9.60%	6.30%	4.69%
£600,000	15.81%	7.62%	5.01%	3.74%
£700,000	12.30%	5.97%	3.94%	2.94%
£800,000	9.34%	4.56%	3.02%	2.26%
£900,000	6.79%	3.34%	2.21%	1.67%
£1,000,000	4.56%	2.26%	1.50%	1.12%
£1,100,000	2.59%	1.29%	0.86%	0.64%
£1,200,000	0.82%	0.41%	0.27%	0.20%

Growth rate shown is the compound annual rate payable at the beginning of each year

Source: Axa Wealth

"The reduction in the lifetime allowance means that many savers and investors will have to look for other tax-efficient options, beyond pensions and ISAs - such as EIS"

Of course, what the reduction in the lifetime allowance means is that some wealthier savers and investors may have to look for other tax-efficient options, beyond pensions and ISAs - such as EIS.

And a recent Freedom of Information request by Suffolk Life gives us an insight into just how many people have breached the lifetime allowance over the last few years - the data on the right shows the tax take from the tax charge on assets held in pensions above the lifetime allowance.

TAX ON PENSIONS ABOVE THE LIFETIME ALLOWANCE (2009-2015)

TAX YEAR	TOTAL
2009/10	£24,858,248
2010/11	£31,404,737
2011/12	£46,953,535
2012/13	£52,995,280
2013/14	£98,013,014
2014/15	£94,200,118

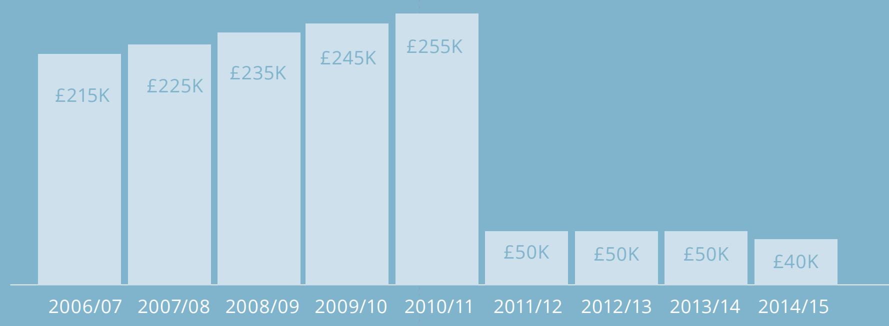
Source: Suffolk Life

The rise in the tax take may indicate that as the lifetime allowance has declined, more investors have been caught out by it - this is the group that should have been utilising other investment options.

ANNUAL ALLOWANCE

At the same time, the annual allowance has been reduced quite dramatically. This might have the effect of making it less likely that today's younger savers will reach the lifetime limit, but it does mean that some wealthier investors could well find that they need to look for other tax-efficient investments as they are fully utilising their pension and ISA limits each year.

ANNUAL ALLOWANCE FOR TAX RELIEF ON PENSIONS (2006-2015)



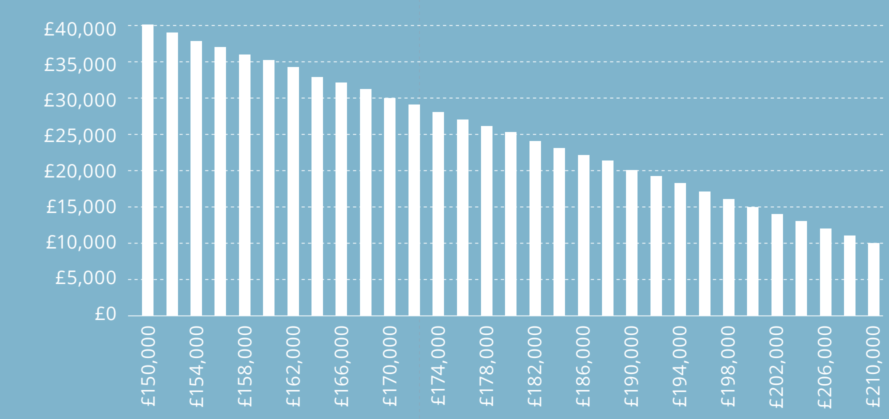
Source: HMRC

HIGHER EARNERS

Recent changes mean that anybody earning between £150,000 and £210,000 has a reduced annual allowance and anybody earning greater than £210,000 has an annual allowance of just £10,000.

So although pensions higher rate tax relief has survived (for the moment), this sliding scale of reduction in the annual allowance significantly reduces the opportunity of pensions for higher earners and once again makes other tax efficient options, such as EIS, more attractive.

ANNUAL ALLOWANCE OF HIGHER EARNERS



Source: HMRC

KEY POINTS

- Changes to the legislation announced in the 2015 Budgets will have a bigger impact on VCTs than EIS
- However, indications are that there is strong support from government for all the UK's Tax Advantaged Venture Capital Schemes
- Developments in the landscape include Social Investment Tax Relief, Seed EIS and the advent of crowdfunding
- There have been a number of innovations in the market to support advisers, such as platforms and review sites
- Changes to the limits on what can be saved into pensions may prompt more interest in EIS

CONCLUSIONS

The EIS sector is going through a lot of change, most of it positive. Changes in the rules governing the scheme are always on the agenda, as the government seeks to ensure that the funds raised are allocated to productive companies who would struggle to raise capital otherwise. The scheme therefore represents value for money for the taxpayer.

The big change over the last few years has been the end to the renewables story. Lots of new money has been attracted to the EIS sector by the double benefit of the reliefs and the renewable subsidies, and it will be interesting to see where that money goes once those investments come to the end of their life.

The other driver for changes is ensuring ongoing compliance with EU State Aid rules. This was behind a number of changes to all of the UK's tax advantaged venture capital schemes announced in the two 2015 Budgets. Although the government did not secure as generous provisions as they would have liked (we're making that assumption based on the differences between what was announced in March and July) the new rules will have a bigger impact on the VCT sector. If this has the impact of making VCTs more risky, it may even push more people into EIS. We also think that it signals the Government's determination to retain these schemes.

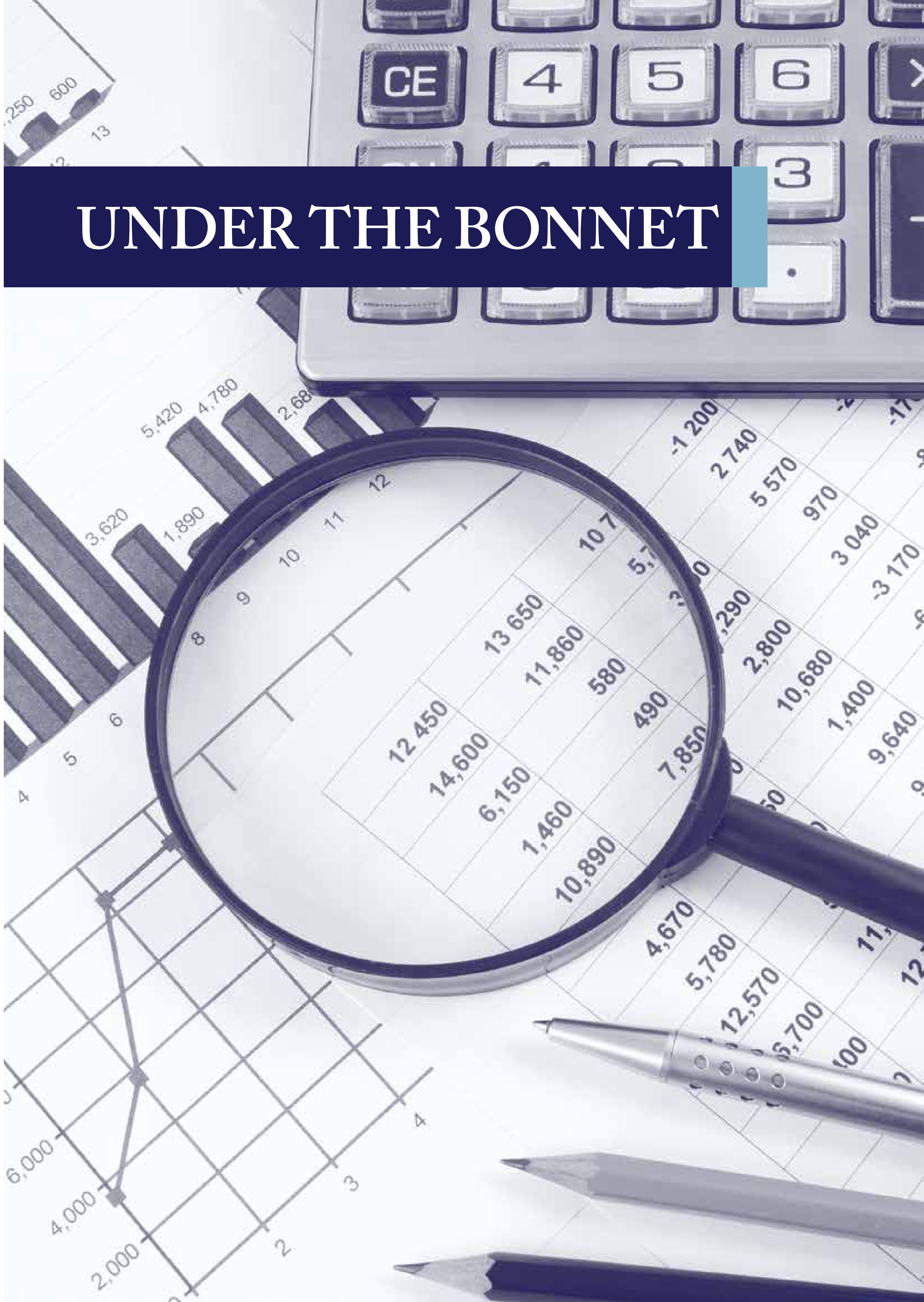
Other push factors include changes to the limits on pension saving. As limits come down more people may decide to find additional tax-efficient investments, which of course will include EIS. New retirement freedoms also mean that some clients will be looking for more sophisticated at-retirement options, and we'll look at how EIS can be used for tax-efficient drawdown later on in the report.

A growing market has also attracted new service providers, who have launched new platforms, review services and comparison sites to assist advisers.

Finally, the landscape of the sector is changing. SEIS and SITR are new sets of reliefs that are very close to EIS and will, we think, both complement and compete with the sector. These are exciting developments that we'll be monitoring closely. Crowdfunding has also brought a lot of new, much smaller scale players into the market - both investors and fundraisers. We're not convinced it will have any impact on the EIS managers, but it may well do them a favour by raising awareness of the scheme.

"Enterprise Investment Scheme investment opportunities are becoming an increasingly common tax-planning and investment tool in a financial adviser's proposition. With other tax-efficient savings vehicles seeing individual limits being reduced, there is a genuine need and desire to look at other opportunities, where appropriate. Similarly, there appears to be increased appetite from high net worth clients to have an exposure to largely uncorrelated investments which means unquoted shares available via EIS opportunities are being considered"

Kieran O'Gorman, Deepbridge Capital



UNDER THE BONNET

FEES, CHARGES & PERFORMANCE

In this section we'll take a look in more detail at some of the more pertinent issues that advisers need to be aware of when considering EIS.

Many advisers might feel that they are groping in the dark somewhat when it comes to assessing the performance of EIS funds, and trying to compare fees.

PERFORMANCE MEASUREMENT

On the performance side, for a fund raising money for the first time there obviously won't be any performance history. It is of course possible to check the manager's track record, but advisers need to establish how closely what the manager did previously relates to what they plan to do next! This is especially pertinent now that the industry is adapting to the end of the renewables story: a good track record in renewables will not necessarily translate into a good track record in other fields.

Also, very often it's not possible to have sight of the underlying portfolio if funds have not been deployed yet. The managers will of course state their intention in the investment memorandum and supporting literature, but if they can't implement the proposed strategy they usually reserve the right to invest in a different one.

This is a stark contrast to what advisers and investors are used to with mainstream stock market based funds, where performance history, top ten holdings, performance attribution and many other pieces of information are available to help advisers.

However, in many cases the managers' hands are tied and producing this kind of information is either impossible, or at the very least counterproductive. Any kind of ongoing performance will of course be based upon the valuation of the underlying portfolio, but managers justifiably do not want to disclose valuations that might compromise the sale of companies that they are looking to exit in the future.

Valuations are also infrequent, and somewhat esoteric: of course all the managers use standard accounting practices to value their portfolio companies, but certainly with young firms there can be an element of judgement about this. It is hard to put a value on potential, intellectual property, goodwill or a forthcoming patent for example.

It's also true that it's really only exits that count in an EIS. EIS funds don't pay income (this would be taxed, unlike any gains which are tax-free in an EIS of course) so the interim performance of an underlying investment is rather immaterial. Think perhaps of a company that is not profitable for several years working on research and development, but then secures a crucial patent. The valuation shoots up and the EIS manager can exit - the valuation in the preceding years has no bearing on the total return to investors in that EIS fund.

For a new EIS, while they will undoubtedly have a pipeline of investment opportunities set up, it is difficult or impossible to say exactly what the underlying portfolio will look like before they go ahead and deploy the funds they have raised. This varies from fund to fund. Some of the more project based EIS funds (think renewables or infrastructure projects) which will back a smaller number of opportunities will have a great deal of clarity on what the underlying portfolio will eventually look like. More generalist, growth focused EIS funds will still have a pipeline of deals that fit their criteria, but they won't have the same degree of certainty about the final makeup of the fund.

None of this is unreasonable. It is down to the constraints that the managers are operating under, and it is one of the reasons why investing in smaller companies is more risky (and therefore why it is harder for them to raise capital). It just feels very different to mainstream, stock market based equity investing. For advisers we think this means that they need to read the fund literature and talk to the EIS managers to develop a very strong understanding of how and when the manager will deploy the funds, what the nature of the underlying trades are how they will generate returns and how they will exit the underlying portfolio.

The manager's track record with previous EIS funds and track record of successful exits should also be examined.

All of this should be part of advisers' due diligence process. They should also check the wording in the investment memorandum: as we noted above, sometimes it gives the manager the option of doing something different with the funds they raise ("pivoting" in Silicon Valley speak) should they not be able to follow the intended strategy for some reason. This could be an issue if a client ends up invested in something that does not fit their risk profile or match the rest of their portfolio. Again, the answer is to engage with the manager and establish how confident they feel about their pipeline and what plan B will be should it be needed.

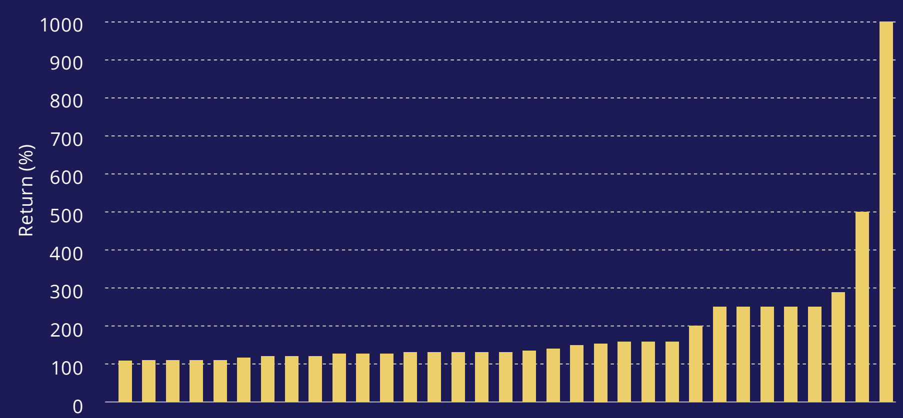
Many of the managers publish their target return (perhaps more realistically we should refer to this as their "hoped for" return). This is also useful for advisers, which should be understood in the context of the underlying trade and the likelihood of the fund achieving that return. A headline number is eye-catching but we think that perhaps understanding the distribution and probability of possible outcomes is more important.

By looking at the range of target returns that are typically on offer, advisers can now have some kind of reference point. The following data was compiled from MICAP and is based on EIS offers that were open in November 2015. The returns do not take into account charges or tax reliefs.

Note - with all of these charts, we are basing them on the targeted return, and not all funds declare a target return, so the sample is incomplete. We also have not accounted for the proposed term of the investment, which is another factor to take into account. What we think this kind of analysis does is create much needed transparency and it gives us a reference point; we think it is significantly better than what has gone before, but we have to acknowledge there are still limitations.

"With contracted revenue streams and the potential to access strong levels of underlying intellectual property, media and entertainment offers investors established and predictable returns within a defined time frame and access to a dynamic investment sector" **Richard Cook, Blackfinch Investments**

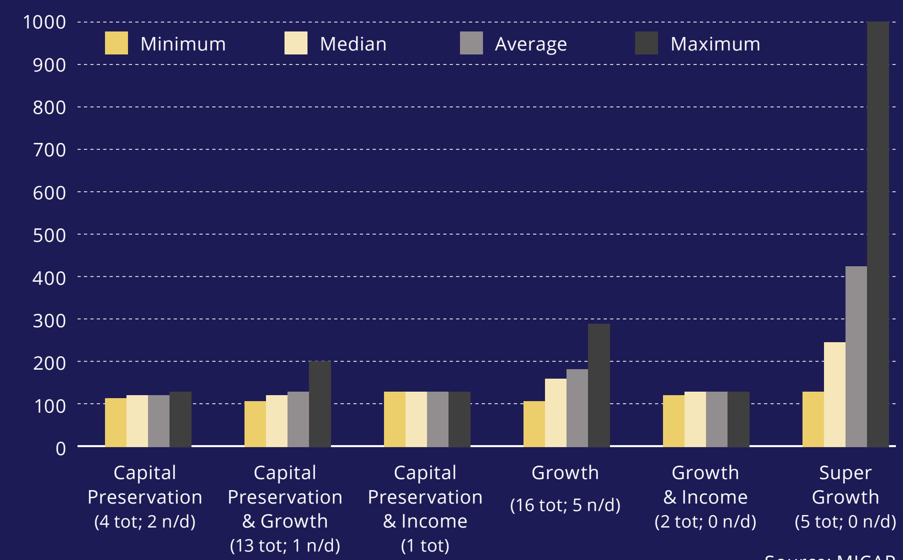
OFFERS BY RETURN (INCL. SINGLE COMPANY EIS) (Nov 2015)



Source: MICAP

We can see that the majority of EIS open investments in November 2015 were looking to return between 1.1 and 2.5 times capital. The outliers were single company, hi tech EIS investments.

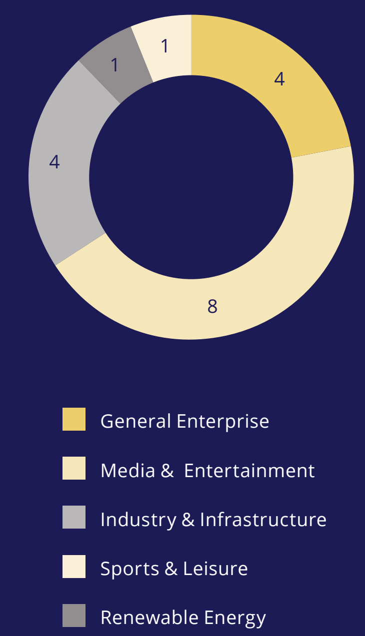
OFFERS BY RETURN (INCL. SINGLE COMPANY EIS) (Nov 2015)



Source: MICAP

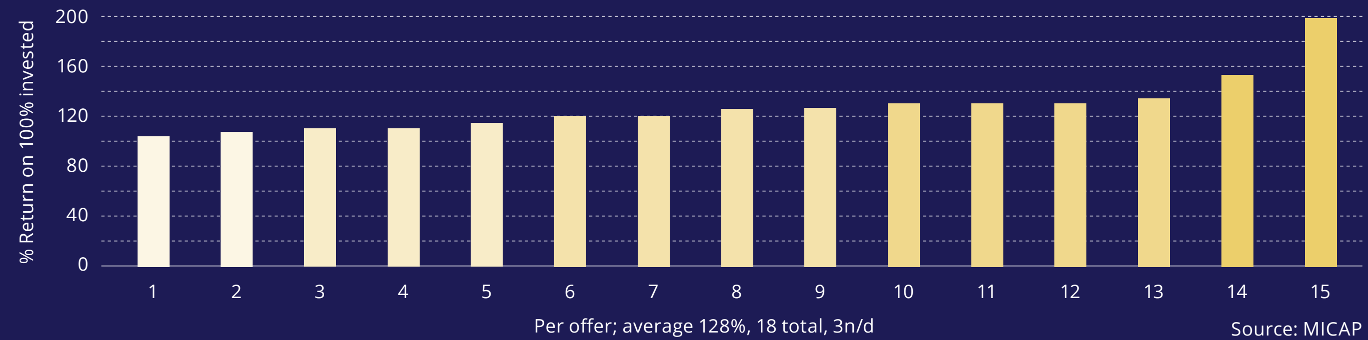
Looking at those targeted returns by strategy (where the total (tot) in the sample is shown, with the number which did not declare (n/d) a return), what is noticeable is that there is not always much difference between something that labels itself 'capital preservation' and something that labels itself 'growth'. Are investors in some growth funds taking on more risk than they need to?

PRESERVATION STRATEGIES



Perhaps surprisingly, Media and Entertainment is used as an asset in capital preservation strategies - but with so many media channels now there is a huge demand for content and media projects have a short lifecycle, returning to cash very quickly. The decline of Renewable energy is apparent here, and some of the capital preservation strategies based on industry and infrastructure that were open at the time of writing will have been based on reserve power installations - barred from EIS from 30th November 2015 and no longer open for investment.

CAPITAL PRESERVATION STRATEGY OFFERS BY RETURN (INCL. SINGLE COMPANY EIS) (Nov 2015)

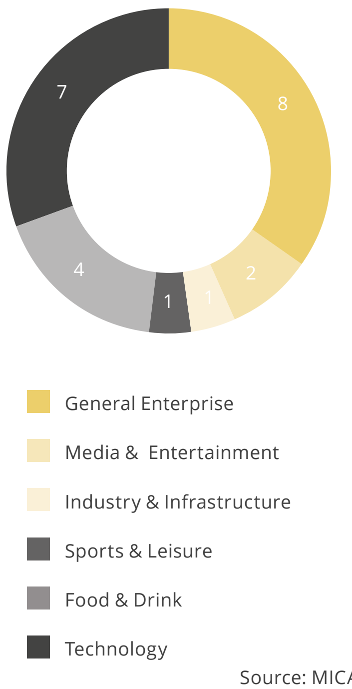


Source: MICAP

If we take out the outlier on the right, the average return is around 1.2 times capital, which feels about right for a capital preservation fund.

"Many of the managers publish their target return. This is also useful for advisers, and should be understood in the context of the underlying trade and the likelihood of the fund achieving that return" **Andy Marris, MICAP**

GROWTH STRATEGIES (Nov 2015)



Source: MICAP

As you might expect, growth strategies are dominated by General Enterprise and Technology.

FEES

EIS funds have a reputation for high fees. Fund management charges are much higher than those charged by active managers of listed share portfolios. Initial charges, (where charged) of 5% of the value of the investment are typical, with annual management charges normally ranging between 1.5% and 2.5%. Performance related fees of about 20% of realised returns (above a hurdle) are also commonplace.

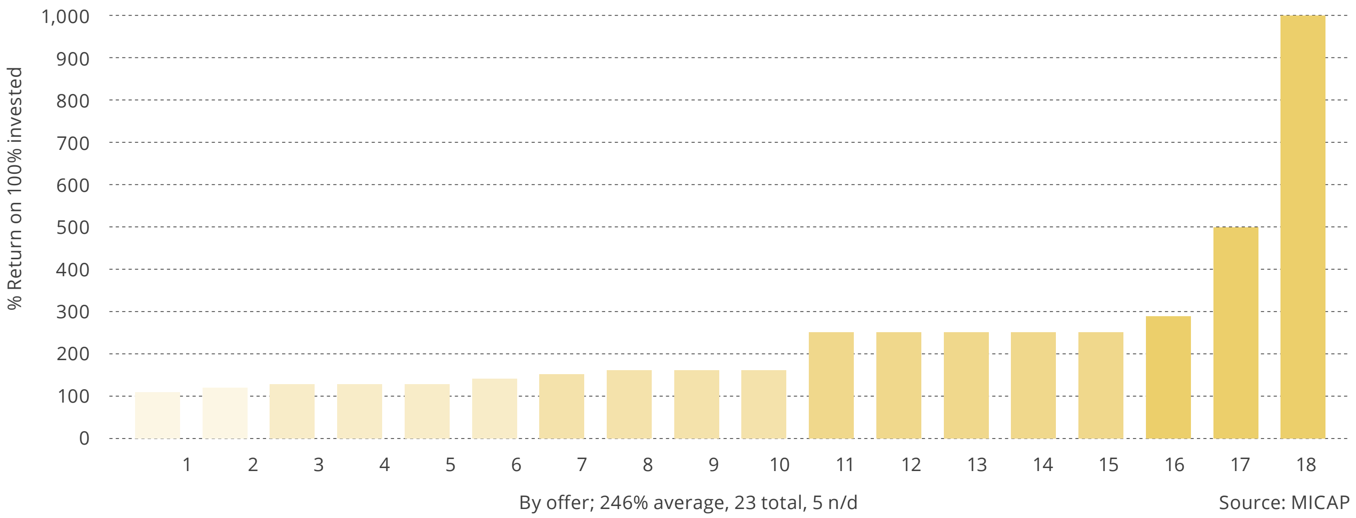
The higher fees support the extensive due diligence that small company investment requires. Sourcing opportunities and executing deals is a much longer process and is more resource intensive than in the world of stock market based funds. Very often the EIS manager continues to be 'hands-on' with their investee companies after they have made an investment, taking a seat on the board to ensure that the company is growing in the right direction and looking after their investors interests (i.e. ensuring their investors do not get diluted, that the company continues to qualify for the EIS and negotiating the eventual exit).

Performance fees can be controversial, as managers are often accused of taking too much of the upside and not enough of the downside. The justification is that the performance fee incentivises the manager to keep adding value to the investee, to negotiate the best possible exit and to secure investors' ongoing interests. Advisers need to assess if the manager represents value for money here. Many of them do not charge performance fees: for example at the time of writing 12 out of 35 open offers do not charge a performance fee. And the size of the performance hurdle also varies - from 100% to 150% net return at the time of writing.

The other variation of fee structures is where providers take the initial fees from the investee company rather than the investor. This leaves the full amount of the investment available to claim tax relief on. Some providers also choose to take their ongoing fees from the investee, and only take a performance fee from the investor. This makes their proposition seemingly fee-free to the investor until the manager has exceeded their performance target, although the fees may impact the performance of the investee.

Advisers need some context for the fees, because as we have noted above they are not comparable to mainstream fees and charges. Our research shows the minimum, maximum and average fees for both the initial and ongoing charges. Today they are slightly lower than their historical averages, perhaps a reflection of increased competition and scrutiny.

OFFERS BY RETURN (INCL. SINGLE COMPANIES) (Nov 2015)



Source: MICAP

Growth strategies have a much broader range of returns (and extreme outliers!) but 1.5 times capital to 2.5 times capital seems a fair level of return to target.

OTHER CONSIDERATIONS FOR FEES

There are a number of other considerations that advisers need to bear in mind - or things to look out for - when examining the fees charged on an EIS:

- Administration fees. Circa 0.35%, although some are flat fees (which obviously are more detrimental for smaller investors)
- Performance fees based on £1 invested, even if only 90p went into the deal
- Custodian and/or depository fees. Essential to ensure investors funds are not co-mingled with the managers
- Dealing fees. Can be applied on purchase and exit, circa 1%
- Ongoing fees that rise with inflation
- Ongoing fees that continue if the company runs beyond its expected term (eroding unrealised gains)
- Fees applied to the investee companies. Sometimes taken as shares or warrants as well
- Non-executive director fees. To pay for board representation
- All fees may be subject to VAT
- Some managers defer ALL ongoing and performance fees until the investor is in profit
- Some annual fees are based on the subscription and not the NAV

FEES AND TAX

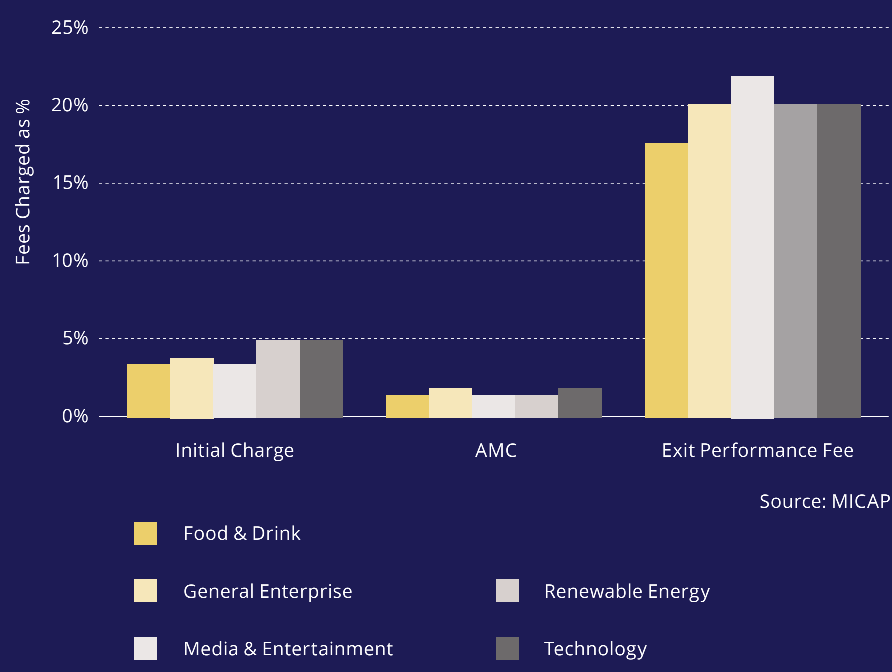
Depending on when and where the fees are taken from, they can have an impact on the net amount that is actually invested in the deal. It is this amount - not the total subscription that the investor writes the cheque for - that qualifies for the tax relief, so the larger the net amount invested the better. This is why it can be more favourable for investors if managers take their fees from the investee companies for example. Charging the investee company is usually easier with project based EIS investments, where there is more certainty over the finances.

CONTEXT FOR FEES (Nov 2015)

	OPEN NOW		1994-2014	
	INITIAL	ONGOING	INITIAL	ONGOING
MINIMUM	1%	0.5%	1%	0.5%
MAXIMUM	5.5%	2.5%	6.5%	3%
AVERAGE	3.9%	1.66%	4.3%	1.82%

Based on products where initial and ongoing fees are applied

FEES BY SECTOR (OPEN EIS) (Nov 2015)



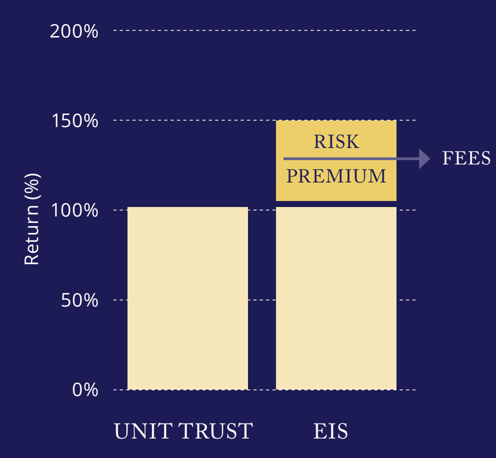
Source: MICAP

FEES AND RISK PREMIUM

The final issue to check is that the fees don't wipe out the investor's risk premium. There should be a substantial risk premium when investing in an EIS in comparison to a conventional stock market based investment. If the fees wipe out too much of this risk premium, then a conventional investment might have been a better choice on a risk-adjusted basis.

We'll caveat that somewhat - of course with EIS there is a dual purpose with the tax benefit and project based EIS investments can argue that their risks are well managed.

RISK PREMIUM VS. FEES



Source: MICAP

GROWTH EIS

The recent changes announced in the summer Budget to comply with EU State Aid were primarily designed to ensure that capital flows to smaller, growing companies that would otherwise struggle to raise funds - so it seems appropriate in this report to dedicate a section to growth focused EIS funds.

According to MICAP, there were 21 EIS investment opportunities in 2015 structured as either a Discretionary Portfolio Service, Investment Company or Portfolio (which we will refer to as 'funds' in the loosest sense of the word) that have an objective either 'growth', or 'super growth'.

Of our 21 growth funds, nine are general enterprise, seven are in the Technology sector, two in the Food & Drink sector, two in Renewable Energy and one in Transport. The Food & Drink EISs is focused on Bars and Restaurants and the Technology EISs are spread between the Medical Sector, Low Carbon and Sustainable Technologies, UK University Spin Outs and Media and Telecoms, as well as Disruptive Tech and a blend of all of the above. We can start to see how growth EIS target specific sectors and firms that have the potential to make a real difference - not just in terms of financial returns, but by bringing new products and services to market that have broader social impacts.

They are raising between £250,000 and £3 million and the minimum subscription ranges from £10,000 to £25,000. The total targeted return ranges from 150% to 500% and in every case the exit strategy is a trade sale, management buy-out or initial public offering. The minimum timeframes range from three years (the bar and restaurant EIS - the Food & Drink sector does have a record of quick exits) to five years, although we would stress this is the minimum - with these kind of growth opportunities it is likely that it will take much longer to exit.

There are more charts on the breakdown of growth EIS in the market data section on page 68.

Of course the details will vary between each individual opportunity, but these funds typically invest between £500,000 and £2 million in five to ten investee companies over each client tranche. Their selection of investee companies will be based upon criteria such as:

- Growth prospects must be above average relative to the company's sector
- Significant market potential with clear need and market growth
- Valuations must be fair and attractive relative to market sector
- Business fundamentals must be judged to be sound
- High-margin, capital-efficient business model
- Passionate, energetic and experienced management team, must be stable and of high quality
- Opportunities must exist to boost the investee company's' values by improving financial operations
- An exit must be visible and anticipated to take place within four to five years of investment
- Exit strategy aligns interests of management with shareholders
- Target IRR must be a minimum of 15% (excluding any tax reliefs)

There are examples of investee companies in the sponsor editorial on page 47.

These funds usually source their opportunities from their existing networks of specialist intermediaries. A good growth EIS will have a healthy long list of opportunities and should be able to evidence a thorough due diligence process that identifies a handful of investees that fit their criteria and make it onto the shortlist. Dealflow is a crucial and the manager must have a pipeline of good quality opportunities that matches their fundraising efforts. There is often some wording in the brochure that gives them room to 'pivot' and deploy money into investments that do not meet the original criteria stated in the investment memorandum, so dealflow is an important area to explore when conducting due diligence.

Managers of growth EIS funds will often take a seat on the board of their investee companies as a non-executive director. This enables the manager to offer advice and mentoring, use their network to help the investee company open doors and break into new markets and, of course to look out for their investors' interests and ensure the management remain focused on growing the business without doing anything to compromise EIS qualifying status until it is time to exit.

One might expect growth EIS funds to charge higher fees in comparison to their peers to reflect the time and effort that goes into sourcing opportunities and the hands-on, ongoing management. But, these issues are actually common to all EIS funds and in reality there is very little difference in the fee structures. However, among the growth focused EIS funds we've been looking at, all but two of them had an exit performance fee. The hurdle for exit performance fees ranged from 100% to 150%. As always, the devil is in the detail and advisers need to examine the fee structures carefully.

One aspect of growth EIS funds where advisers can feel totally comfortable is they can be certain that these EIS funds are seeking to invest in companies that are operating well within the letter and the spirit of the EIS qualifying rules and are therefore very unlikely to ever be challenged by HMRC at outset. However, as we have said above, whilst this is the case, it is imperative that the EIS managers ensure the company remains within the qualifying rules during the EIS investment term to maintain its EIS status.

INVESTMENT OPPORTUNITIES

We can broaden that data set out. If we also include opportunities structured as a single company this rises to 33, and if we include investments that have an objective of either 'Growth and Income' or 'Capital Preservation and Growth' the number rises to 67. This is out of a total of 71 offers that were open or Evergreen in 2015. However, for the purposes of this section we will focus on our original, more narrowly defined data set.

SUITABILITY

As EIS are not mainstream collective investments, and are not eligible for the FSCS, arguably any advice and recommendation should be more thorough than for a mainstream investment. There is no prescribed way of doing this, but at our EIS masterclass events this process was proposed by Keith Robertson of Armstrong Financial:

- A generic report explaining EIS and EIS investments
- A highly personalised suitability report
- A highly researched investment-specific due diligence report

GENERIC EIS REPORT

This will describe and explain the EIS landscape and, once written, should require only marginal amendment from year to year, if the rules change. It should include as a minimum:

- History of EIS
- Types of EIS
- Range of risks
- Qualifying criteria for investees
- Fees and charges
- Exit routes and time frames
- Liquidity
- Tax reliefs
- Portfolio strategies and serial investing
- Comparisons of funds and providers
- Third party sources of analysis
- Suitability

Having all this in a stand-alone document will avoid cluttering a personalised suitability report with generic information, and can be provided to potential clients well ahead of the EIS season.

> *"If it looks too good to be true, it probably is. EIS is about taking risk and getting a fair return for it"*
>
> **Nigel Ashfield, TIME Investments**

HIGHLY PERSONALISED SUITABILITY REPORT

The basic structure of your suitability report (COBS 9.4) must cover:

- The client's demands and needs
- Why the EIS is suitable for this client
- Possible disadvantages and risks

Above all else, this must place the advice in context, explaining what has led to this point and the client's 'needs' – which could be almost anything: a desire to recover some tax, a wish for diversification, interest in the riskier end of investing but with some protection from tax reliefs, social impact investing, IHT planning, BPR, etc.

Within that context, an EIS can be recommended as a suitable investment vehicle, but the client must be alerted to any alternative products which could also work: SEIS, VCT, SITR, pension, ISA, etc.

The report should include all of the costs and charges, including the cost of specific advice and investment management, and how these costs compare with possible alternatives. Declare any conflicts of interest. Disadvantages and generic risks should also be documented, and here the report can refer back to the client's feeling about investment risk.

It may be worth explaining that the EIS will not fit into any asset allocation models based on risk profiling technology as mainstream investments do: for example rebalancing EIS holdings is impossible.

INVESTMENT SPECIFIC DUE DILIGENCE REPORT

Advisers cannot rely on a provider's marketing "bumf" as constituting sufficient due diligence. In the final analysis, advisers have to provide their own due diligence. Both the Regulator [SYSC 3.2.4] and the courts [Seymour v Ockwell & Co. and Zurich, 2005] make clear that the test of what advisers are expected to do by way of due diligence is set very high. This is still the leading case and precedent and means that advisers owe a non-delegable duty of care to their clients.

Always consider what could possibly go wrong with an investment offering, or what would have to happen in order to get a worse return than expected.

What to include in the specific due diligence report:

BASIC INFORMATION:

- Investment's name
- Structure
- Pre-authorised by HMRC?
- Regulator
- Management House / Promoter / Asset manager / Custodian
- Asset class
- Risk of loss

At a glance a client can see the basic information that they may have to trawl through a prospectus or factsheet to find otherwise.

DESCRIPTION, STRUCTURE & PROCESS:

This should be a plain English narrative, explaining how the EIS originated, how long it has been trading, etc. Explain the structure – maybe ordinary shares paid-up and issued, or a more complex structure with loans and mezzanine structured finance, all of which must be explained along with where the investor stands in priority if the investment goes bad. If the investment is an EIS portfolio service or fund structure, that should be explained clearly, along with why this is better than an alternative structure.

For a very thorough document, it may be wise (where possible) to explain each underlying EIS company and rank them in order of portfolio weighting and risk. The report can explain what the business is and why it will qualify as an EIS trade, go into detail about the experience of the company executives, the trading outlook for the company and how investors' capital will be deployed in order to meet the EIS qualification rules.

ASSETS

The report should provide a broad description of the range of assets held, and whether complementary or competitive businesses are involved. It should explain why the fund/

"Managers with clear specialism in growth capital investing and with strong deal flow will be key considerations for advisers and investors seeking the wise deployment of their capital"

Ian Battersby, Seneca Partners

portfolio manager has the necessary skills to manage a portfolio of small-scale companies and if the manager sits on the boards of the component companies.

BUSINESS RISKS

Here the report should consider broad risks that could affect the business(es) involved. This might be straight competition, interest-rate hikes, dependence on a third party agent, regulatory difficulties (in a regulated sector), loss of EIS qualification, etc. Will the qualifying trade be at risk from an economic downturn under any circumstances and, if so, to what extent? Is the expected return commensurate with these perceived business risks?

DUE DILIGENCE REPORT

ANTICIPATED RETURNS

This should carefully and fully describe how the return will be generated, how much, and when – will there be a lead time before break-even is reached, for example, or will profitable trade be expected immediately. Will dividends be payable throughout the life of the EIS, or does 'total return' depend on a successful sale at the end of the qualifying period? What will be the expected return without the EIS tax reliefs? What will it be with the tax reliefs? Broadly speaking, some favoured trades have a fairly well-known range of gross returns. Does the advertised expected return of the EIS suggest that the promoters and/or others may be creaming off more than might be expected given the relatively low perceived risk involved?

LIQUIDITY

Generally, EIS investments should be considered totally illiquid for the life of each company, there being no secondary market. The report should explain what the exit strategy is and when; and what risks there are which might delay or prevent it. When can investors reasonably expect to get back their original investment and gains?

REASONS WHY

Any number of reasons why could be included here, from the tax relief to IHT exemption to diversification benefits to the potential for very strong returns, among others.

SPECIAL RISKS

These major ones should be included, but it is not an exhaustive list:

- EIS investments should be considered high-risk and illiquid.
- The underlying costs and charges levied by various levels of management can be opaque.
- Valuation of shares at any time prior to the sale of the company, is likely to be problematic, and will probably be a valuer's subjective opinion.
- It is entirely possible to suffer total loss of investment in a small unquoted company, and even the several tax reliefs, including loss relief, available to EIS will not cover all loss in the event of an insolvent liquidation.
- While every effort has been made to conduct due diligence on this investment, it is impossible to identify all future risks, not excluding fraud, which might result in a worse outcome than is currently hoped for by adviser and investor alike.

SOME ADDITIONAL THOUGHTS

Advisers should be careful not to sell to a relatively new client until it is clear that an EIS or similar will have a place in their overall portfolio and that they can be comfortable with such investments. One-off sales look bad.

The advisory process works for advisers here, with a clear timeline from initial discussion through a range of documents and then a further conversation about how comfortable they are prior to investing. KYC is the rule.

EIS are likely to be for only a small proportion of clients who have the wealth and ongoing income tax liabilities to make this a useful additional strategy.

Advisers will probably need to explain the whole universe of tax-incentivised investments and where EIS sits.

When conducting due diligence, advisers should try to discover the true costs and charges being levied by all the managers in the food chain.

Who is custodian of the assets, including cash?

Small companies can often have hidden governance issues; how is the EIS investment manager going to deal with those?

There is a great deal of work involved in doing this stuff well. Advisers might legitimately be worth an additional due diligence fee, as well as any fund-related fee.

PROVIDER DIRECTORY

BLACKFINCH

www.blackfinch.com
0168 457 1255
enquiries@blackfinch.com

Blackfinch Media EIS Portfolios

PARKWALK ADVISORS

www.parkwalkadvisors.com
0207 759 2285
enquiries@parkwalkadvisors.com

Parkwalk Opportunities EIS Fund

DEEPBRIDGE CAPITAL

www.deepbridgecapital.com
0124 474 6000
enquiries@deepbridgecapital.com

Deepbridge Technology Growth EIS
Deepbridge Life Science SEIS

ROCKPOOL INVESTMENTS

www.rockpool.uk.com
0207 015 2150
team@rockpool.uk.com

EIS Portfolio Service

FORESIGHT GROUP

www.foresightgroup.eu
020 3667 8199
info@foresightgroup.eu

Foresight Energy Infrastructure EIS Fund

SENECA PARTNERS

www.senecapartners.co.uk
020 3195 7100 / 01942 271746
sales@lgbrcapital.com / eis@senecapartners.co.uk

Seneca EIS Portfolio Service

OCTOPUS

www.octopusinvestments.com
0800 316 2298
salessupport@octopusinvestments.com

Eureka EIS
Octopus EIS

TIME INVESTMENTS

www.time-investments.com
020 7391 4747
questions@time-investments.com

TIME:EIS

OXFORD CAPITAL

www.oxcp.com
0186 586 0760
investment@oxcp.com

Oxford Capital Growth EIS
Oxford Capital Infrastructure EIS

We invited EIS investment providers to include their details within this directory.

This is not a comprehensive list of all the providers but does capture a section of the market. Providers contributed to the production and distribution of the report in exchange for including their details.

The following ten pages are investee company case studies provided by our report sponsors. These pages do not qualify for CPD.

BLACKFINCH

The Blackfinch Media EIS Portfolios allow investors to access the attractive tax benefits of EIS by investing into qualifying media companies. Our portfolio companies target capital preservation through their predictable income streams underpinned by intellectual property or high levels of contracted revenue. Targeting returns of £1.05p - £1.20p for each £1.00p invested, the companies are focused on two main areas, Television Distribution and Music Publishing.

BLACKFINCH	
	2016
	Television Distribution
	International
	25
www.blackfinch.com	

Back Catalogue Distribution sells the broadcast rights for television programmes on behalf of producers. The companies acquire the distribution rights for those television programmes by advancing money to the television producer which is then recovered in first position, along with sales commission and expenses, from sales of the programme to international broadcasters which license those rights.

RATIONALE FOR INVESTMENT: The global demand for television programmes has grown by 5% in the last 5 years, and increasingly discerning consumers are demanding higher quality television productions which are achieving higher prices supported by additional advertising or subscription revenues for broadcasters.

GROWTH IN REVENUE AND EMPLOYMENT: Since launch, Back Catalogue Distribution has secured distribution rights for six projects through early advances totalling approximately £280,000. These projects have estimated gross valuations of approximately £776,000 which should be achieved through future sales to international territories. These early projects have involvement from actors such as Stephen Fry, with primary broadcasters such as Channel 4, BBC One and Channel 5. Sales have already started to produce capital inflows on these early projects.

VALUE ADDED BY EIS MANAGER: Back Catalogue Distribution Limited (BCD) is a TV distribution company that will acquire the distribution rights for a portfolio of approximately 25 different television projects.

Blackfinch work with BCD's director, Terry Back who, as a Partner of Grant Thornton from 1997 to 2014, led their media team and advised a number of TV distribution companies. His experience in the market and his knowledge of TV producers and broadcasters makes him well placed to help select TV projects for BCD and also identify suitable broadcasters.

AMOUNT INVESTED AND CO-INVESTORS: Blackfinch clients are the only investors and will target a raise of c£5m.

BLACKFINCH	
	2016
	Music Publishing
	International
	25
www.blackfinch.com	

Our music publishing companies are responsible for creating, protecting, administering and monetising rights in musical compositions on behalf of musicians, songwriters and composers. Music publishing royalties are the revenues due to the owner of that underlying intellectual property and are generated from a number of sources.

RATIONALE FOR INVESTMENT: Within the wider industry, the worldwide music publishing industry has grown by 5.3% over the last 4 years, supported by new methods of monetising music publishing royalties from online broadcasts and streaming in addition to the traditional sources of revenue – for example, from TV broadcasts and record sales.

GROWTH IN REVENUE AND EMPLOYMENT: Since its recent launch, First Score Music Limited has secured the music copyright for twelve projects through early advances totalling approximately £750,000. The underlying music scores are underpinned by projected gross revenues which should provide returns of approximately 8-12% per annum. The projects have involvement from actors such as Johnny Depp, Keanu Reeves, Gemma Arterton, Sam Worthington and Nicholas Cage. Each project will be sold to international territories and will feature approximately 40 minutes of music which will have been produced, and will be owned, by First Score Music Limited.

VALUE ADDED BY EIS MANAGER: Blackfinch work with Rupert Christie, director of First Score Music Ltd (FSM), which will create and own a catalogue of at least 40 scores and soundtracks for different films and television programmes. Those scores are expected to be created within the first year of investing into the company and will be generating revenues from year 2. FSM will effectively create and provide the music score to a film or television producer in return for the publishing royalties derived from that score.

Rupert is an experienced composer and music supervisor who was responsible for writing the score for a number of films including Mamma Mia and a number of television programmes, including Band of Brothers.

AMOUNT INVESTED AND CO-INVESTORS: Blackfinch clients are the only investors and will target a raise of £5m.

www.blackfinch.com 0168 457 1255 enquiries@blackfinch.com

Deepbridge

Deepbridge works closely with financial advisers and investors to design innovative products, ranging from investment in technology growth companies to asset-backed renewable energy projects. Partnering with innovative and committed management teams to help UK based companies realise their potential, Deepbridge operates across four principle divisions: disruptive technology, sustainable technologies, life sciences and renewable energy. The following two companies are supported via the Deepbridge Technology Growth EIS.

Resonant Software	
	2012
	Technology - B2B Software
	USA and UK
www.resonant-software.com	

Within the financial services industry, many critical business processes are still performed manually. Resonant's Adaptive Process™ software technology transforms the management of business processes that are complex, inefficient, resource-intensive and human-centric in an automated, adaptive and thus time and cost-saving way. The result for users is significant immediate value gain, averaging 30% productivity improvement, 90% reduction in time to enact change and significantly greater compliance to regulatory reporting requirements (which historically has been extremely unusual in the underwriting market). Resonant software accelerates each task, lowers hand-off delays and minimises errors. Resonant's initial core target market is the general insurance market.

RATIONALE FOR INVESTMENT: Resonant was introduced to Deepbridge by one of Deepbridge's non-exec partners, who has considerable experience of identifying and developing disruptive technologies.

Resonant ticked the following boxes of Deepbridge's stringent investment criteria:

- Created a new market by solving a solution to a market problem
- Multiple markets
- A clear path to commercialisation
- Robust intellectual property
- A committed and engaged founding team

GROWTH IN REVENUE AND EMPLOYMENT: Pre investment gross revenue in 2011: $560,000
Gross revenue in 2015: $2,100,000

VALUE ADDED BY EIS MANAGER: Deepbridge instigated a fundamental initial change to the business by recommending and implementing a change from a licensing model to a 'pay per click' model, thus enabling greater profitability per order and control over software distribution. Deepbridge also led Resonant to develop a two-pronged sales strategy and has instigated numerous introductions which have led to sales and commercial agreements.

AMOUNT INVESTED AND CO-INVESTORS: Deepbridge has to date raised $2.7 million for Resonant and advised on additional fundraising and potential exit opportunities.

SKY MEDICAL TECHNOLOGY	
	2013
	Medical Technology
	Buckinghamshire & Cheshire
	>30
www.skymedtech.com	

Sky Medical Technology Limited has developed the OnPulse™ technology platform, a technology which, at its core, has been proven to dramatically improve blood flow (both volume and velocity) and elevates oxygen levels in the blood. The platform can be used across a variety of indications, displacing both pharmaceutical and device solutions on the market today. The initial target markets that Sky is pursuing are Deep Vein Thrombosis ("DVT"), wound care and urinary incontinence with Sports Injury/Recovery for elite athletes, with additional markets. The OnPulse technology has been proven through clinical studies, has received regulatory approval for sales in the UK, EU, Canada and USA, and is in the midst of device approvals process in various other markets, including China.

RATIONALE FOR INVESTMENT: Sky was introduced to the Deepbridge team by a trusted contact. Sky ticked all of the boxes of Deepbridge's stringent investment criteria:

- Highly disruptive to existing growing markets
- The ability to create new markets
- A clear path to commercialisation
- Robust intellectual property
- A committed and engaged founding team

GROWTH IN REVENUE AND EMPLOYMENT:
Employment: from 2 to >30 staff
Revenue: from £100,000 to £1.1 million

VALUE ADDED BY EIS MANAGER: Deepbridge has assisted Sky with sourcing fundraising from additional sources, has assisted with international licensing advice and is currently advising the business on potential stock market listing in the UK and/or US.

AMOUNT INVESTED AND CO-INVESTORS: £1.5 million raised by Deepbridge. Additional sums raised by parties sourced by Deepbridge, including Juno Capital and Spark Ventures.

www.deepbridgecapital.com 0124 474 6000 enquiries@deepbridgecapital.com

Foresight group

Foresight Group LLP (Foresight) is a leading independent infrastructure and private equity investment manager which has been managing investment funds on behalf of institutions and private investors for more than 30 years.

In that time, Foresight has grown to establish itself as one of the UK's leading VCT and EIS managers as the firm has broadened its focus beyond Private Equity for UK SMEs to become a leader in renewable energy and environmental infrastructure. Since 2011, Foresight has raised more than £280 million for its Solar EIS Funds and AD EIS Fund. Foresight has over £1.8 billion of assets under management across twenty-two funds including Business Property Relief (BPR), Enterprise Investment Schemes (EISs) and Venture Capital Trusts (VCTs).

Foresight Solar EIS

Foresight Solar EIS	2012
	Renewable Energy
	South of England
	N/A

www.foresightgroup.eu

Foresight Solar EIS Fund invested in 14 EIS Qualifying investee companies, which acquired four solar power plants in Kent and Somerset with a total aggregate generating capacity of 16MW, alongside funds from Foresight Solar VCT.

RATIONALE FOR INVESTMENT: To acquire operational utility scale solar power plants in areas of high irradiation in the south of England, to deliver capital growth for investors upon exit with a target return of 130p.

GROWTH IN REVENUE AND EMPLOYMENT: The four solar plants have performed well since acquisition generating stable revenues both from the generation of clean electricity, which is sold to the National Grid and from the government's index-linked Feed-in Tariff (FiT) subsidy scheme, which was in place when the original investments were made.

VALUE ADDED BY EIS MANAGER: Foresight's experience in solar infrastructure and its in-house team of portfolio managers and technical directors ensure optimal operational efficiencies at each site. In May 2013, Foresight refinanced the assets owned by Foresight Solar EIS Fund and Foresight Solar VCT Fund through the listing of a £60 million solar bond on the London Stock Exchange, at that time the largest solar bond, which was fully subscribed at launch by two leading financial institutions. This refinancing generated an immediate 20% uplift in NAV for the EIS, enabling investors in Foresight Solar EIS to exit the fund at a tax-free return of £1.33 from a net cash investment of 70p after tax relief, exceeding the original target return and delivering a tax-free uplift to investors of c.90% in year four, representing an annual return of 21%.

AMOUNT INVESTED AND CO-INVESTORS: Foresight Solar EIS Fund invested £24.9 million alongside co investor Foresight Solar VCT, which invested £25 million.

Foresight Energy Infrastructure EIS

Foresight Energy Infrastructure EIS	2015
	Energy Infrastructure
	UK wide
	N/A

www.foresightgroup.eu

Foresight has developed an innovative funding solution that has enabled the installation of more than 40,000 smart meters at Industrial and Commercial customers. Long term agreements exist with the relevant Energy Supply Companies, including the "top six", for the provision of the meters and their data.

HOW THE REGULATION CHANGE WAS CONFRONTED AND THE NEW SECTOR WAS IDENTIFIED:

Regulatory change has had no impact on this trade. Foresight has been involved in Smart Data Equipment for over 3 years and has recently applied for and received advance assurance from HMRC to deploy EIS qualifying money alongside the other funds already deployed. The sector was identified in-house as one which would experience significant growth over the coming years and one in which there are attractive risk/return characteristics.

RATIONALE FOR INVESTMENT: The roll-out of smart meters is driven by UK Government and regulatory legislation leading to high, largely predetermined levels of demand. In the UK, the market opportunity is for 50 million "dumb" meters to be replaced by 2020, at an estimated cost of £6 billion. Although the responsibility for this roll-out falls to the energy suppliers, these suppliers are reluctant to own the meters due to the competitive nature of the supply market encouraging customers to find the best deals and switch suppliers. As a result they are interested in private funding solutions of the kind provided by Foresight Energy Infrastructure EIS Fund and Foresight ITS. Smart meters use simple technology, fully tested and proven in the market together with manufacturer warranties which offer significant benefits to consumers and distributors. Investors find the predictable rates of return and the low risk profile from dealing with blue chip asset providers compelling.

OCTOPUS INVESTMENTS

Octopus is a fund management business with positions in several specialist sectors including healthcare, energy and smaller company investing. Founded in 2000, Octopus manages over £5.5 billion of funds on behalf of 50,000 investors.

Octopus works with financial advisers to create investment solutions that combine its expertise in smaller company investing with government approved tax reliefs. The core product range currently includes VCTs, EIS and IHT solutions using Business Property Relief.

The following two companies were supported by Octopus' Titan VCT and Eureka EIS.

Zynstra

zynstra	2013
	Technology / IT
	Bath
	45

www.zynstra.com

Zynstra delivers cloud managed IT infrastructure for Small-Medium Enterprises on a subscription based model, available with the installation of minimal hardware. By leveraging hybrid cloud technologies, Zynstra offers the services of a corporate-grade IT infrastructure at an affordable cost. Zynstra works with Managed Service Providers and IT retailers who re-brand the service and resell it through their distribution channels.

RATIONALE FOR INVESTMENT: Octopus was extremely impressed by the calibre of the management team and their experience given that they are serial entrepreneurs within the enterprise software space. The Zynstra team founded and grew Cramer Systems that they sold for more than $400m to Amdocs in 2006. In addition, the Zynstra technical platform solves a real pain point for SMEs who do not have the in-house expertise to manage complex IT systems.

VALUE ADDED BY EIS MANAGER: As an investor, Octopus aims to offer much more than just money, adding value by providing experience at board level and access to its network of portfolio companies. One of its Venture Partners, Ian Perry, has provided Zynstra with concrete advice and active support as the company builds out a global B2B SaaS sales team.

In addition, we've been able to leverage Octopus's network in the technology space on several occasions. This has enabled it to connect more easily to senior people in relevant organisations, including large global corporates, with positive results.

CO-INVESTORS: Octopus Ventures and high profile angel investors.

Swoon Editions

SWOON EDITIONS	May 13, May 14, June 15
	Retail
	London
	56

www.swooneditions.com

Swoon Editions sells high quality furniture at insider prices. Sourcing direct from factories in India, China and Vietnam, the company buys in container quantities and sells direct to consumers. Cutting out the middlemen, shops and warehouses allows Swoon to sell beautifully handcrafted furniture at fair prices.

RATIONALE FOR INVESTMENT: Swoon operates in a large and attractive market and is pioneering a new and disruptive business model for e-commerce. Octopus was extremely impressed by the calibre of the management team, the vision of the company and the innovative business model.

GROWTH IN REVENUE AND EMPLOYMENT: Swoon has grown its headcount from 15 employees in May 2014 to 56 in October 2015. Revenue has grown 200% per year every year since investment.

VALUE ADDED BY EIS MANAGER: Octopus is an active participant on the board at Swoon Editions. It has facilitated numerous introductions; has set up numerous press and media opportunities and advised on debt negotiations.

OXFORD CAPITAL

Oxford Capital aims to make tax-efficient investments accessible and easy to understand for investors and their financial advisers. They currently offer two distinct EIS investment opportunities.

The Oxford Capital Infrastructure EIS invests in companies which own and operate infrastructure assets, typically capable of generating stable revenues through long-term contracts.

Through the Oxford Capital Growth EIS, clients can invest in a portfolio of small companies seeking to solve scientific, technological or commercial problems. The current portfolio spans sectors including games development, marketing software, sustainable agriculture and healthcare.

OXITEC

Date	1st investment, April 2004
Sector	Healthcare / Disease Control
Location	Oxford
Employees	50

www.oxitec.com

Oxitec has developed novel methods to suppress insects that spread disease to people, crops or livestock. The company produces genetically-modified insects that can be rendered sterile in the wild. Oxitec releases modified males into local populations of insects. The modified insects mate with females, producing offspring that do not survive to reproductive age. As such, continued releases of Oxitec's insects cause iterative reductions in the population of pests. Oxitec's technology can be used both for agricultural purposes, and for controlling the spread of disease amongst urban populations.

Oxitec, valued at £5 million at the time of Oxford Capital's original investment in the company, was sold to Intrexon Inc. in 2015, in a deal which valued the business at more than £100 million.

RATIONALE FOR INVESTMENT: Governments have historically tried to control harmful insect-borne diseases using chemical pesticide 'fogging' in urban areas. This is ineffective in eradicating the target pest and introduces harmful chemicals into the foodchain. Oxitec's solution can almost totally eradicate disease carrying insects without the use of chemicals.

GROWTH IN REVENUE AND EMPLOYMENT: Revenues were negligible during the investment holding period, as the business was focused on R&D and taking its first steps towards commercialisation. Before being acquired by Intrexon in 2015, Oxitec obtained its first regulatory approvals for commercial use of its technology insects and secured its first sales in Brazil.

Employee numbers increased from 25 in 2004 to 50 in 2015.

VALUE ADDED BY EIS MANAGER: Oxford Capital was one of the earliest investors in Oxitec. Since then, it has been instrumental in leading subsequent funding rounds, through which it introduced Oxitec to important additional strategic investors. Oxford Capital also shaped the board of Oxitec, helping to bring in directors with the right mix of commercial, strategic and scientific expertise.

Outplay entertainment

Date	May 2014
Sector	Mobile Phone Games
Location	Dundee
Employees	84

www.outplay.com

Outplay Entertainment is a games development studio founded by Doug and Richard Hare, industry veterans with 15 years' experience gained on the west coast of the USA. Outplay's games have been downloaded more than 30 million times. The company produces high quality free-to-play games for mobile devices for the 'casual' sector (fun, easy games usually played for short periods) and 'mid-core' sector (more difficult games for keener gamers). The games generate revenues through targeted on-screen advertising banners and by encouraging users to spend money on extra lives and other features. Outplay publishes its titles on the major platforms - Apple, Android, Amazon and Samsung.

RATIONALE FOR INVESTMENT: The market for mobile games is growing more than 25% a year, and there are a number of big companies in the sector that are active acquirers of smaller development studios. Outplay's strategy is to develop and release new games at regular intervals, rather than relying on revenues from a single title.

GROWTH IN REVENUE AND EMPLOYMENT: Revenues in 2015 are expected to exceed £5 million, compared with £1.8 million in 2014. Founded in 2011, the company's staff has grown quickly to 84 employees – 20 have been recruited since Oxford Capital's investment in the company.

VALUE ADDED BY EIS MANAGER: Oxford Capital has worked closely with Outplay to improve the quality of its data analytics, allowing the company to make quicker and better-informed decisions about future developments in order to maximise revenues.

Oxford Capital has also introduced Outplay to a number of advisers and key contacts within the industry, making the business more visible to potential acquirers.

AMOUNT INVESTED AND CO-INVESTORS:
Oxford Capital EIS Funds - £1.6 million
Oxford Capital Co-Investors Circle - £0.2 million
Co-investors: Pentech - £3.2m; Scottish Enterprise - £2.9 million

www.oxcp.com 0186 586 0760 investment@oxcp.com

ROCKPOOL INVESTMENTS

Rockpool helps to build wealth through investment in private companies, with the reassurance of thorough analysis by our experienced team and the benefit of approved tax reliefs.

We contribute to the success of those companies by giving them access to flexible capital and an insightful contact network. We provide investors and advisers with exceptional transparency and a personal service. Our senior partners have been investing in private companies for over 20 years.

Our EIS Portfolio Service offers unusual flexibility, as advisers can set portfolio diversity and investment strategy to suit the client's risk profile. Most investors get fully deployed in 3-4 months, helping to ensure tax relief can be claimed earlier than with a traditional EIS fund.

Kirkleatham Memorial

Date	March 2013
Sector	Crematorium
Location	Yearby, North Yorkshire
Employees	4

www.kirkleathammemorial.co.uk

Kirkleatham Memorial Park and Crematorium was opened in 2014 and offers cremation, traditional burial and natural burial on a greenfield site near Redcar in Cleveland.

The Company has a mission to provide exceptional standards of service and surroundings for the bereaved families that use its crematoria and gardens of remembrance.

RATIONALE FOR INVESTMENT: Rockpool investors subscribed for £3,500,000 of EIS qualifying shares in 2013.

The investment provided the capital for acquisition of the company's freehold site, and the construction and working capital for the crematorium. Rockpool backed the management team to open and develop a profitable business with predictable cash flows and asset backing.

GROWTH IN REVENUE AND EMPLOYMENT: Revenues have grown from zero to £0.5m since the date of investment, consistently performing ahead of budget on revenues and EBITDA. For the year to 31st December 2014, the Company delivered revenue of £542,180 and EBITDA of £88,247, ahead of the budget of £485,590 and £62,771 respectively.

The Company employs 4 people directly and provided employment for 10 others under the construction contract.

VALUE ADDED BY EIS MANAGER: Rockpool worked with the management team to structure the investment to deliver a fixed dividend to investors, reflecting the cash generative nature of the business.

AMOUNT INVESTED AND CO-INVESTORS: EIS qualifying share subscriptions of £3,500,000 by Rockpool investors. No co-investors.

AIREDALE GROUP

Date	February 2013
Sector	Commercial Catering Equipment
Location	Bradford
Employees	225

www.airedale-group.co.uk

Airedale designs, installs and services catering facilities in commercial premises, such as schools, pubs, hotels, restaurants and hospitals. It is one of the largest players in a relatively fragmented UK market.

The Group operates from 4 different regional office locations which allows for a truly nationwide offering.

There are currently four in-house divisions: Airedale Catering Equipment, SCC/Airedale Building Services, and Airedale Fabrication (Caterform). These divisions provide everything from design and installation, fabrication of bespoke stainless steel units, turnkey building works and ongoing equipment maintenance.

RATIONALE FOR INVESTMENT: The rationale for investment was to support the new management team's vision of expanding the business to a nationwide footprint by providing working capital and expertise to scale the business towards an exit in 3-4 years.

GROWTH IN REVENUE AND EMPLOYMENT: Airedale has grown much faster than the market. This has been achieved by widening its geographic reach and professionalising its tendering processes.

In the year to 31st December 2014, sales increased by 53% to £29.4m and EBITDA doubled to £2.36m. At the time of investment revenues were £18.2m.

The Group employment grew from 80 to 225 people from the time of investment to 2015.

VALUE ADDED BY EIS MANAGER: Rockpool assisted with the search for a Chairman and identified and introduced Andrew Bristow, a Rockpool investor, who took up the role in 2014. Andrew has led 80 acquisitions of private businesses and helped Airedale complete its first acquisition in 2014.

www.rockpool.uk.com 0207 015 2150 team@rockpool.uk.com

Seneca Partners was formed in 2010 bringing together a first class team of finance professionals with over 300 years of combined investment experience, extensive contact networks and exceptional deal flow. We have a dedicated team who specialize in private company equity investments targeting companies who can demonstrate sound underlying business fundamentals and strong growth potential. Our focus is on helping companies to grow. With a presence in Manchester, Liverpool, Leeds and Birmingham, we are well represented in the UK's SME heartlands. The established, trusted and high quality contact network of the Seneca Partners team, which includes fellow professionals, funders, investors and SMEs themselves, is critical to our ability to source the most interesting and compelling investment opportunities. The combination of our network and our location ensures that our EIS investment deal flow remains buoyant. We expect to complete 15-20 EIS Investment deals per year in the normal course of our business.

HAM BAKER GROUP	
	January 2014
	Manufacturing
	UK wide
	C. 200

www.industrialvalve.co.uk, www.hambaker.co.uk, www.kempsteruk.com

FJ Holdings is an independent specialist manufacturer and global distributor of flow control products. The group was formed following a MBO of Industrial Valves and the subsequent formation of Industrial Penstocks and Industrial Pipeline Solutions. Kempster Valves and Engineering and Dowell and Maskell were acquired in 2008 to expand the product range. IVL Flow Control was launched in 2012 and Ham Baker was acquired in August 2012.

RATIONALE FOR INVESTMENT: With operational synergies and opportunities existing to consolidate sites and activities and strong support from its senior debt provider and bankers, funding was required to support the re-organisation and working capital of the new combined business, with the Ham Baker brand enabling the new group to build upon and accelerate its international growth strategy and providing prospects for growth through future acquisitions.

GROWTH IN REVENUE AND EMPLOYMENT: To date, the investment has helped to fund the creation of a the joint venture installations business employing an additional 30 members of staff, the acquisition of a process engineering business, which now has 15 additional staff and the creation of a joint venture GRP plastic manufacturing business, which has added 25 staff into the group.

All of the above have supported the group's ability to provide full service, turn key solutions in engineered solutions to flow and process control applications in the water, waste water and process industries, fueling a c.20% increase in turnover.

VALUE ADDED BY EIS MANAGER: Active board presence providing corporate advisory and strategic direction, including identifying acquisition targets, providing advice on funding and financing, strategic corporate finance advice on the market place, potentially interested parties for the future exit.

AMOUNT INVESTED AND CO-INVESTORS: Sub £1m invested from Seneca's EIS fund and £100,000 of non EIS funds.

Rothband Your Partner in Medical Imaging	
	March 2015
	Medical Manufacturer
	Haslingden, Rossendale, Lancashire
	10

www.rothband.com

WSR Medical Solutions Limited ("Rothband") is a specialist manufacturer of lead aprons and related products for use in radiology environments.

With over 100 years of manufacturing radiation protective equipment for clients across the UK and Ireland, Europe and the Middle East. Rothband supplies lead aprons and associated x-ray shielding equipment directly from its headquarters in Haslingden, Lancashire.

RATIONALE FOR INVESTMENT:

- Rothband had developed a position as a leading supplier of lead protection products required for the modern x-ray department – sold into NHS hospitals
- A Managing Director with vast experience in medical and healthcare industries
- Significant market share
- The business was ready for a fresh management approach
- Profitable business with decades of steady performance and a strong platform for further growth

GROWTH IN REVENUE AND EMPLOYMENT: Since investment:

- c.30% growth in revenue
- Employment of lead sales manager to expand and drive buyer network

VALUE ADDED BY EIS MANAGER:

- Active board presence providing corporate advisory
- Working with company to develop new product launch strategies

AMOUNT INVESTED AND CO-INVESTORS: Sub £1m investment with additional debt provided by FW Capital and Rosebud Finance with invoice discounting finance by Ultimate Finance.

TIME Investments works in partnership with financial advisers, wealth managers and family offices to create and deliver innovative investment solutions for their clients. Throughout their investment solutions they focus on providing consistent, stable returns delivered through a defensive and transparent investment strategy.

TIME are dedicated to supporting financial planners and that's why they don't accept direct business.

TIME were recently awarded Best BPR Investment Manager at our inaugural Growth Investor Awards.

	2014/2015
	Renewable Energy
	North West Scotland
	54

www.time-investments.com

TIME's hydro EIS opportunity invested in three EIS qualifying investee companies which each acquired a separate hydro-electric power project in Inverness-shire, Scotland with a total aggregate generating capacity of 1.5MW. Two of the projects have been constructed by the EIS investee companies, whilst one project was acquired fully operational.

TIME sought to raise EIS funds for three projects that had been identified from the outset rather than raise further EIS funds blind, with no certainty of commitment of capital within the required timeframe. The manager's calling card is to never be in a position where it has raised capital with uncertainty over dealflow sufficient to commit capital. This way, it is never in the position where there is pressure to do a deal simply because the EIS tax clock is ticking.

RATIONALE FOR INVESTMENT: To acquire and develop hydro-electric installations in areas of high rainfall in Scotland, with the benefit of Government renewable energy subsidies, to deliver capital growth for investors upon exit with a target return of 110p.

GROWTH IN REVENUE AND EMPLOYMENT: All construction works to the two development projects were undertaken by a Scottish build contractor, which employed local labour. The hydro-electric turbines were purchased from Gilbert Gilkes & Gordon, a Kendal based turbine manufacturer which was founded over 160 years ago. All three hydro-electric installations are now operational and are generating revenues both from the generation of clean electricity, which is sold to the National Grid and from the Government's index-linked Feed-in Tariff (FiT) subsidy scheme.

VALUE ADDED BY EIS MANAGER: Having identified the projects in a market with little dealflow prior to fundraising, and invested the EIS capital, TIME managed the extensive construction programme to ensure that all activities were completed within the original programme and within budget. With the projects now operational, asset management activities are being conducted to maximise revenues, improve operational efficiencies and minimise running costs.

	2015 / 2016
	Dry Bulk Shipping
	UK vessels operating globally
	54

www.time-investments.com

TIME has received Advanced Assurance from HMRC to raise up to £20 million of EIS capital for four new shipping companies which will each seek to acquire a secondhand dry bulk vessel of the Supramax or Handymax class without the use of bank debt. The vessels will be chartered to customers to enable the transportation of dry bulk cargo, such as grain, fertiliser or coal between seaports for a period of 3-5 years before being sold and the capital returned to investors.

HOW THE REGULATION CHANGE WAS CONFRONTED AND THE NEW SECTOR WAS IDENTIFIED: In the run up to the demise of renewable energy investments as EIS qualifying, we reviewed a number of potential EIS trades. The investment team at TIME has monitored the shipping sector for over 15 years and in light of a recent downturn in the market to a 35 year low point, it is our opinion that now is the opportune time to launch a dry bulk shipping EIS. The trade of operating a dry bulk vessel was not affected by the recent changes in regulation and remains an uncontentious EIS trade. Most importantly, it has a real investment rationale for investing now, rather than being a trade that is reliant on the EIS tax benefits.

RATIONALE FOR INVESTMENT: The acquisition and operation of a dry bulk vessel provides investors with the opportunity to access an asset backed EIS investment, with a significant element of downside protection (the current scrap value of a vessel is around 40% of the current acquisition cost). Following the introduction of the new EIS & VCT rules, such opportunities are now limited. Furthermore, recent significant falls in both charter rates and vessel values provide investors with an opportunity to access the sector at a historic low point, without the requirement for leverage. Investors will therefore be well placed to benefit from a market recovery with significant upside potential not historically available through asset backed EIS opportunities. The EIS tax reliefs are a secondary benefit to the investment proposition.

EIS COMPARISON

		AUM (NOV 15)	CHARGES & FEES*	MIN. SUBSCRIPTION TOP UP	INVESTMENT STRATEGY	FUND MANAGER
BLACKFINCH	BLACKFINCH MEDIA EIS PORTFOLIOS	£3.5m	2.00% Initial Charge 2.00% AMC 25% Performance fee over the hurdle of £1.05p returned to investor	£25,000	The Blackfinch Media EIS Portfolio service will focus on the media sector and invest in music publishing and television distribution. The portfolio companies target capital preservation by investing in companies underpinned by intellectual property and which have predictable income streams and/or high levels of contracted revenue.	Blackfinch Investments Ltd
Deepbridge	DEEPBRIDGE TECHNOLOGY GROWTH EIS	£7m	No charges to the investor Charges to investee companies: 2% Initial Charge 0.35% Initial Deal Fee 2% AMC	£10,000	The Deepbridge Technology Growth EIS is an opportunity to participate in a portfolio of actively-managed high-growth technology companies, taking advantage of the potential tax benefits available under the Enterprise Investment Scheme. A diversified portfolio of actively managed high-growth companies seeking commercialisation funding, the Deepbridge EIS invests in technology growth companies that have a proven technology, clear intellectual property and are operating in a high growth/high value market sector.	Deepbridge Capital
	DEEPBRIDGE LIFE SCIENCES SEIS	£0.4m	No charges to the investor Charges to investee companies: 2% Initial Charge 0.35% Initial Deal Fee 2% AMC	£10,000	The Deepbridge Life Sciences SEIS is an opportunity to secure potentially attractive returns by investing in a diversified portfolio of early-stage life science companies, whilst taking advantage of the considerable income tax, capital gains tax, and inheritance tax benefits available under the Seed Enterprise Investment Scheme.	Deepbridge Capital
Foresight group	FORESIGHT ENERGY INFRASTRUCTURE EIS FUND	£310m	2.5% Initial Charge 1.5% AMC	£10,000 minimum. Multiples of £1,000 thereafter	Investing in a portfolio of EIS Qualifying Investee Companies which will own and operate energy infrastructure assets including smart data and international solar, that generate a regular and sustainable income, and to refinance and/or sell the assets within 4 years to generate capital gains for investors.	Foresight Group LLP
OCTOPUS INVESTMENTS	EIS	£400m	Advised Clients: Initial 2.5%, Ongoing AMC (deferred) 2% + VAT per annum	£25,000	Capital preservation strategy for investors who aim to preserve the value of their investment rather than achieve high returns.	Octopus Investments
	EUREKA EIS	£86.3m	Advised Clients: Initial 2.5%, AMC 1.5% + VAT, 20% Performance fee subject to conditions outlined in the brochure	£50,000 minimum £5,000 increments	Eureka invests in a combination of AIM quoted and unquoted companies. The investment team look for investments with the potential to deliver higher investment returns over the long term (5+ years) compared to FTSE 100 companies.	Octopus Investments
OXFORD CAPITAL	OXFORD CAPITAL GROWTH EIS	£50m	2.5% Initial fee AMC 2% 20% of profits Performance fee	£25,000	Companies from a range of industries, seeking to solve commercial, technological or scientific problems in innovative ways.	Tom Bradley, Oxford Capital
	OXFORD CAPITAL INFRASTRUCTURE EIS	£200m	2.5% Initial fee AMC 1.5% 20% of profits Performance fee	£25,000	Companies that own and operate assets capable of generating long-term contracted revenues.	Oliver Hughes, Oxford Capital
ROCKPOOL INVESTMENTS	EIS PORTFOLIO SERVICE	£125m	No charges to the investor Charges to investee companies: Arrangement fee (7%) at completion of the investment & Monitoring fee quarterly thereafter (1.5% p/a)	£10,000 minimum £250 increments	Choice of growth and asset-rich.	Andrew Green, Rockpool Investments
SENECA PARTNERS	SENECA EIS PORTFOLIO SERVICE	£20m	Initial Charge: 2% + VAT Custodian Fee: 0.35% + £350 Admin fee AMC: 2% + VAT. *(This is capped and can only be charged for 4 years max and is deferred until an investor has received their original £1 investment back)* Exit Fee: N/A Performance Fee: 20% above £1.096	£25,000 minimum £5,000 Increments	To provide investors with a portfolio spread of 4-6 qualifying investments into companies whose business fundamentals are strong enough to support a growth in value within a 4 year investment term. The Service targets a return of £1.60- £1.80 per £1 invested irrespective of tax reliefs and where there is exit capability and visibility for investors by the end of the 4th year. Seneca are SME specialists with a senior and highly experienced Investment team maintaining a strong regional presence in the Midlands and North of the UK with strong deal flow in the SME heartland areas.	Seneca Partners
TIME INVESTMENTS	TIME:EIS	£160m	3% Initial Fee No AMC Stepped Performance fee	£10,000	TIME:EIS invests in the dry bulk shipping sector where TIME believes significant market downturn has created an exciting investment opportunity. Each EIS portfolio company will purchase a vessel without the use of debt. The asset backed nature of the investment creates considerable downside mitigation through scrappage, which, at today's levels should deliver a 'worst case' return of 40% of purchase cost. Base case target return for EIS investors of £1.27 on 70p net investment.	TIME Investments specialist team of 16; industry expertise provided by independent third party industry experts

*May not include service fees

INVESTOR CASE STUDIES

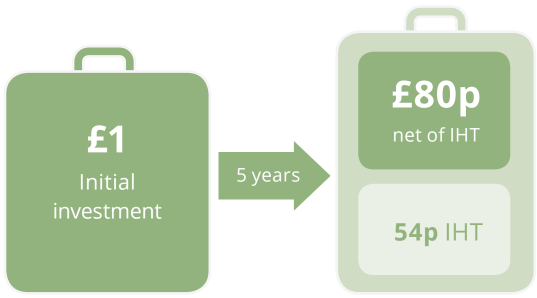
It's worth considering a couple of examples of how EIS can be used in tax planning. These are just hypothetical suggestions, but hopefully they will provide readers with some ideas for their own planning scenarios. We're grateful to Matt Taylor of Rockpool Investments for these examples of tax planning scenarios:

PROFESSIONAL COUPLE

A typical couple in their 50s, both high earners with over ten years to go until retirement and mature ISA and pension portfolios - and adult children. They have just sold a property they had bought some years ago for one of their children to live in at university as they don't want the hassle of being absentee landlords. This means they:

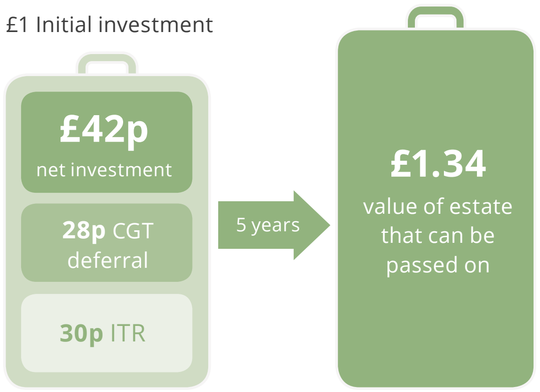
- Have made a gain on the sale of a second home
- Have large Capital Gains tax liability to pay (this example assumes they have used their CGT allowance elsewhere)
- Inheritance tax is a consideration (they want to pass on their wealth to the kids, but they are concerned about giving up control of their wealth at this point)

TAX EFFECT ON MAINSTREAM INVESTMENT



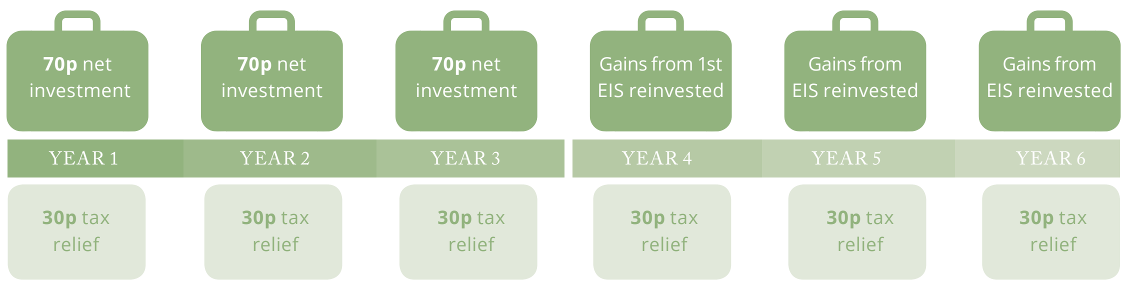
If they were to invest the capital gain in a typical mainstream investment and get 5-6% growth for five years, then £1 invested becomes £1.34, but after IHT, that will only be worth 80p. (The example assumes IHT at 40%, and that the IHT allowance has been used up elsewhere)

RELIEF EFFECT ON EIS INVESTMENT



However, if it was invested in an EIS, the ITR, CGT deferral and IHT relief transform the profile of that £1 invested. The net cost of investment is only 42p, and the entire portfolio value of £1.34 (assuming some growth) can be passed on to beneficiaries as part of the estate. In fact the value of the three reliefs (Income Tax, CGT deferral and IHT relief) adds up to more than the initial £1 investment.

SELF FINANCING TAX-EFFICIENT PORTFOLIO



Invest an equivalent gross sum into each year for 3 to 4 years, after which it could recycle and self fund itself

HIGHER EARNERS

A high earner who is at or beyond the lifetime allowance for their pension and wants to save Income Tax.

A typical high earner may be:

- High Income
- Pension capped
- Well established existing portfolio and conventional planning needs already met (Protection, Insurance, Pension, Cash Savings)
- Perhaps has wealth abroad
- Planning to re-invest the capital plus any gains made from successful EIS investments into new EIS opportunities.

If after a few years of making initial EIS investments they successfully exit, the proceeds can be reinvested in new EIS investments, recycling the money and attracting another round of Income Tax relief. It would be possible to build a portfolio that required no new net investment, and eliminated the investor's Income Tax liability.

By recycling the original investment plus any gains that have been made, this investor can (after a period of time) create a portfolio that requires no new net investment, where the capital is continually recycled for another round of Income Tax relief. Obviously the assumption here is that there will be a sufficient number of exits to do this every year - in practice this would be difficult, but not impossible to achieve. However, the principle of having a self-financing tax-efficient portfolio that can be used to offset income tax still stands.

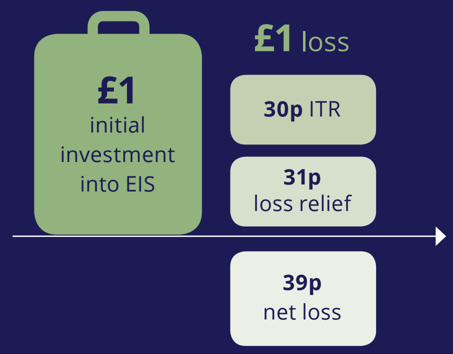
"As well as providing attractive tax reliefs for investors, such as income tax and deferral of Capital Gains Tax, EIS can also be attractive for those investors with potential IHT liabilities to mitigate" **Richard Simmonds, Blackfinch Investments**

HIGH RISK GROWTH INVESTOR

A wealthy and sophisticated client who wants to be an angel investor in high growth businesses. These are risky investments, so some losses are to be expected. Typical investors may be:

- Successful entrepreneurs
- Young wealth builders
- Engaged investors
- Willing to take on risk
- Understanding that they will incur losses and that the winners can offset the losers

RELIEF EFFECT ON LOSSES



The reliefs mean that even a total loss only results in a new loss of 39p per £1 invested. The relief is granted against the net cost of investment, not the gross cost, so it is 45% x 70p = 31p relief (assuming this is an additional rate taxpayer).

Consider the portfolio effect of this. A portfolio of ten investments could have five total losses, four that only returned 1 times capital and just one stellar performer, and still make a return of 86%.

PORTFOLIO EFFECT

EIS	INITIAL INVESTMENT	FINAL VALUE BEFORE RELIEFS ARE CONSIDERED	INCOME TAX RELIEF	LOSS RELIEF	FINAL VALUE
A	£1.00	£0.00	£0.30	£0.32	£0.62
B	£1.00	£0.00	£0.30	£0.32	£0.62
C	£1.00	£0.00	£0.30	£0.32	£0.62
D	£1.00	£0.00	£0.30	£0.32	£0.62
E	£1.00	£0.00	£0.30	£0.32	£0.62
F	£1.00	£1.00	£0.30		£1.30
G	£1.00	£1.00	£0.30		£1.30
H	£1.00	£1.00	£0.30		£1.30
I	£1.00	£1.00	£0.30		£1.30
J	£1.00	£10.00	£0.30		£10.30
TOTAL	£10.00		£3.00	£1.58	£18.58
RETURN					85.75%

Of course, all of these examples assume that the hypothetical clients are suitable for EIS and understand the risks, lack of liquidity and minimum terms to claim the reliefs (three for the Income Tax and two for the IHT). We should also consider that this new EIS portfolio could help to diversify the couple's existing portfolio away from mainstream investments.

DECUMULATION STRATEGIES

EIS investments can also be used in a more sophisticated way to provide tax-efficient decumulation. In the example below, a £180,000 pension pot can be withdrawn over a four year period, and the tax can be offset by investing some of the money into an EIS portfolio - leaving the investor with £90,000 in cash and £90,000 in EIS, hopefully still growing and sheltered from IHT.

	YEAR 1	YEAR 2	YEAR 3	YEAR 4	TOTAL
WITHDRAWAL FROM PENSION	45,000	45,000	45,000	45,000	180,000
TAX-FREE	(45,000)	-	-	-	
TAXABLE INCOME	-	45,000	45,000	45,000	
INCOME TAX WITHOUT EIS	-	9,000	9,000	9,000	
EFFECTIVE TAX RATE ON WITHDRAWAL	-	20%	20%	20%	
EIS INVESTMENT TO OFFSET ALL TAX	-	30,000	30,000	30,000	90,000
CHANGE IN CASH	45,000	15,000	15,000	15,000	
CASH BALANCE	45,000	60,000	75,000	90,000	90,000

"The new pension freedoms that came in from April 2015 give people much more flexibility when it comes to taking their pension at retirement, and for many EIS investments could play a role without purchasing an annuity, and to ensure tax-efficient decumulation"

THE RENEWABLES STORY

Of course one of the big themes in EIS has been the renewables story. The combination of contracted revenues from Feed-in-Tariffs or Renewable Obligation Certificates and the tax relief available via an EIS helped to draw many new investors into the EIS market. The sector grew from £41.2 million in 2011 to £383.5 million in 2014. 2013 was still the biggest sector for EIS investment, and the huge increase in the share of funds raised by the Energy and Water Supply sector can be seen in the chart to the right.

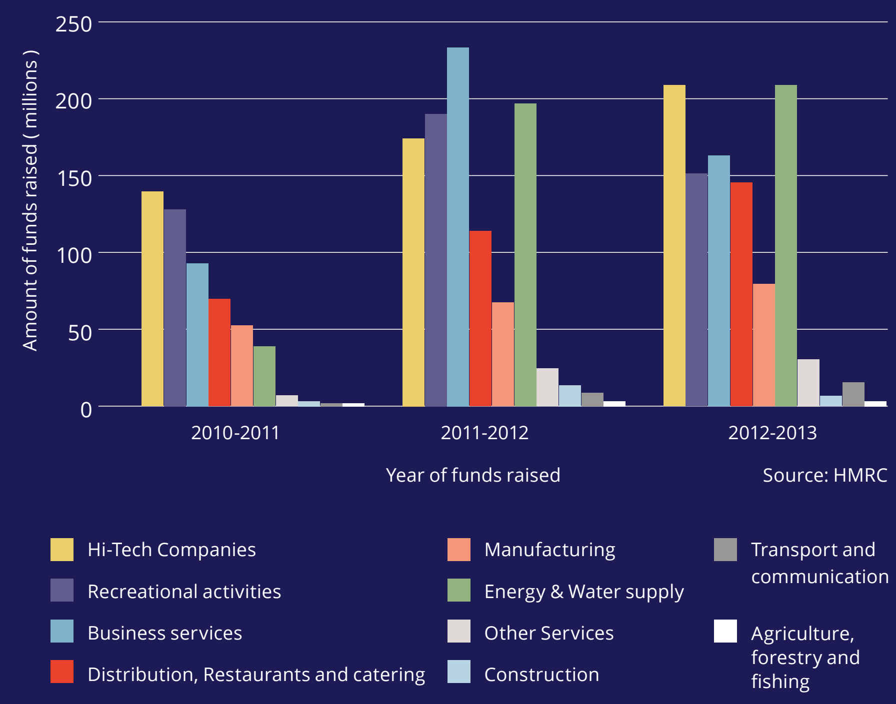
However, the story has now come to an end. The government has now disqualified any business that benefits from Feed-in-Tariffs from the EIS (including FiTs, ROCs and CFDs), and the whole regime of subsidies has been amended. These measures include more esoteric renewable energy sources such as anaerobic digestion, smaller scale production such as Community Energy Schemes and Reserve Power - which for a while looked like it would be a replacement for established renewables such as solar and wind. It's worth taking time to examine this story and bring it up to date, and consider what might happen once these projects start exiting and the money that was invested has to find a new home.

RENEWABLE ENERGY SUBSIDIES

There have been two major programmes of subsidy designed to help develop the renewable energy industry in the UK. They are:

Feed-in-Tariffs (FiTs): were launched in April 2010 to replace UK government grants and encourage the use of renewable electricity-generating technologies. FiTs work by giving a set rate for each kilowatt hour (kWh) of electricity generated – called a generation tariff. Rates vary depending on the size of the system, technology installed and period in which the system was installed.

FUNDS RAISED BY INDUSTRY (2010-2013)



RENEWABLE ENERGY SOURCES

SOLAR

The conversion of sunlight into electricity using photovoltaic cells, or concentrated solar power. Direct sunlight isn't needed for the cells to work and will still produce electricity on a cloudy day

WIND

Wind energy is obtained from air flows using wind turbines to generate electricity. The stronger the wind the more electricity generated

HYDRO

Uses running water to generate electricity from small streams and large rivers. Hydro power systems convert the potential energy of water flowing downstream into kinetic energy in a turbine to drive a generator that produces electricity

ANAEROBIC DIGESTION

Consists of breaking down organic material by micro-organisms in the absence of oxygen. Anaerobic digestion produces biogas and methane-rich gas that are used as fuel

"EIS has been subject to numerous legislative changes over the years as the Government seeks to ensure it continues to fulfil its policy objectives and remain a successful government-approved initiative. In recent years this has included making changes to prevent certain energy generation activities qualifying for EIS funding as the UK renewable energy industry matures. The announcement to exclude all energy generation activities from qualifying is the next logical step" **John Thorpe, Octopus Investments**

MARKET ANALYSIS

"Renewable energy has been a popular for EIS investment. Solar and Anaerobic Digestion, for example, have been able to deliver predictable returns to investors within the tax efficient wrapper" **Nick Morgan, Foresight Group**

Renewable Obligation Certificates (ROC): This is the main mechanism to support renewable electricity projects in the UK. ROCs are "green" certificates issued to accredited operators of renewable energy stations - used by suppliers to demonstrate they have met their obligations. Companies have the obligation of presenting a number of ROCs or otherwise pay an equivalent amount into a buy-out fund. Contracts for Difference (CFDs) will be brought in as a new support mechanism for low-carbon electricity generation from 16 October 2016, replacing the ROC.

Obviously there are different risks involved with each of these, but in general solar and, to a slightly lesser extent, wind power are actually very reliable. The technology is well understood, the installation process should not be overly demanding and ongoing care and maintenance is minimal. Of course they do rely upon the prevailing weather to produce electricity, but believe it or not the weather in the UK is actually highly predictable over longer time-frames: we know how much sun, wind or rain we should expect every year. So the developments themselves were low risk, the projects would reliably produce energy each year and the government would contractually guarantee the price for the energy. Once the EIS reliefs were added on top, it is easy to understand why this sector became so popular.

Perhaps unsurprisingly, the government decided that the EIS relief was no longer needed to incentivise investment into renewables, and has withdrawn the relief over the last few years, starting with FiTs in 2011 and finishing with reserve power in October 2015 (as part of the 2015 Finance Act).

RESERVE POWER

Reserve power plants provide electricity to the National Grid when demand is high or when supply unexpectedly shrinks. These plants usually receive a number of payments from the National Grid on top of the revenues they earn from selling the energy they generate.

Reserve Power was an interesting case. It is absolutely not a source of renewable energy - quite the opposite in fact as reserve power installations usually burn fossil fuels - but did have similar investment characteristics: contractually secured revenues, paid for by customers with a predictable need and installations that are relatively simple to install and manage. For these reasons it was seen as the "new solar" - a low risk, project based investment. And probably for the same reasons, the government decided to exclude reserve power from EIS in the autumn of 2015, upsetting the plans of a number of EIS providers who had launched products based on investing in this area. As we understand it, HMRC wanted to move quickly and disqualify reserve power after receiving a large number of advanced assurance requests.

WHAT NEXT

The big question now is where the money invested into renewables will go once it starts to exit those projects over the next few years. The recent changes the government has made to the rules means that there aren't the same sort of opportunities available in the EIS market.

One possibility is that some of the money will be invested in the providers' BPR schemes. Investments into assets that are BPR qualifying provide 100% exemption from Inheritance Tax after two years. The rules that govern BPR are less strict than those that govern EIS, and renewable energy projects would qualify. Perhaps some renewable investors would be tempted to switch their EIS portfolio into BPR investments. For more detail on the BPR market, please download our 2015 BPR Industry Report from *intelligent-partnership.com.*

The other possibility is that now that this cohort of investors have had a positive experience of EIS via renewables, they will carry on investing in EIS, even if that means making investments that require them to take on more risk. Certainly there is a lot to be said for keeping the money within EIS investments - it is possible to get to a point where an EIS portfolio is self-financing. See our planning idea on page 59.

It's also important to note that, despite the changes to the rules and despite the focus on growth, there are still many lower risk EIS investments out there that have investment objectives based around capital preservation. The providers of these EIS can still identify project based opportunities, often in infrastructure, that can meet these criteria.

TIMETABLE FOR THE END OF RENEWABLE IN EIS

TYPE OF RENEWABLE ENERGY	PROPOSED TO BE DISQUALIFIED FOR EIS	IMPLEMENTATION OF DISQUALIFICATION FOR EIS
Companies whose trade was based fully on FiTs	2011	2012
Subsidised Solar	2011	2012
Wind	2011	2012
Hydropower	2014	April 2015
Anaerobic Digestion	2014	April 2015
Community Power	October 2015	30th Nov 2015
Reserve Power	2015	30th Nov 2015

OVERALL ANALYSIS

The next section takes a look at the current state of the EIS market based on the data we have been able to collect and include in our EIS investment register. The register includes data on 321 investments across EIS companies and portfolios, dating back as far as 1998.

Last year, our aim was to build a picture of how the market has developed over time and understand the historical context for EIS investments. With that in mind, this year's report will focus more on EIS investments currently open for investment and providing a timely update on the market.

The continued goal of the investment register and this analysis is to help improve the EIS scheme and develop a more mature, open and transparent market that advisers can have more confidence in.

The information included in this register has been analysed to identify emerging trends within the market. It does not single out individual products for praise or criticism. The objective is to simply provide an overall picture of the EIS market to enable investors and advisers to make their own appraisal.

OBJECTIVES

Our aim in compiling the investment register and carrying out the subsequent analysis is to help readers acquire whole-of-market awareness of the EIS sector. There are many different investment products available through EIS, covering a range of investment objectives, structures, manager styles and risk and return profiles. Gathering as much of the available information as we can, in one place, will help advisers develop their understanding of the opportunity and decide if EIS investments are right for their clients. The register and analysis aim to:

- Provide a snapshot of the EIS market at a point in time as of Q1 2016
- Highlight the different investment opportunities, risks and returns available in the market
- Provide comparisons and highlight trends across the different sectors, structure and investment strategies

The information included in this register forms the basis of unique analysis on the EIS market. To the best of our knowledge, data of this kind is not available elsewhere.

As this is our second report much of this analysis is a follow up to our first. Since last year, we have been able to access more data and learn more about the market. As a result, we have updated our analysis and commentary on the EIS market and we feel what have produced is more accurate.

While we do collect information on single company opportunities, these opportunities are not as widely marketed as managed portfolios or funds. With the increasing popularity of crowdfunding as a way to access single EIS qualifying companies and the data HMRC provides, we have excluded these from the main analysis (except where noted) and have given these opportunities their own section that still allows readers to make a comparison across the two structures.

DATA COLLECTION

Another innovation and improvement for this year's report; we have largely relied on data gathered by MICAP from their Fund Finder, where the most recent open EIS and other tax efficient investment products can be viewed and compared alongside each other. This has allowed us to provide the most up-to-date and accurate information on the current market. For historical information, we scraped product provider websites and online marketing materials for data.

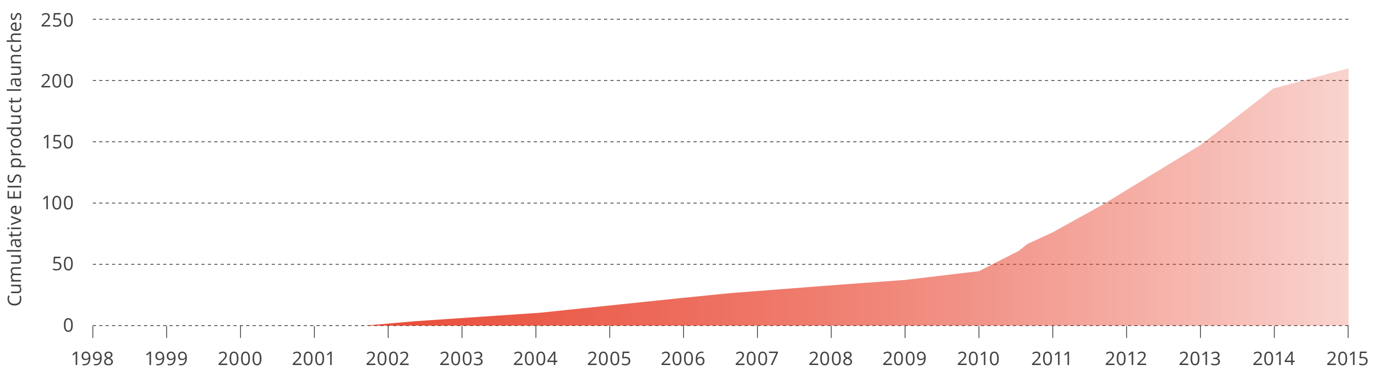
MICAP is part of the same group of companies as Intelligent Partnership.

The data can be broken down and analysed in a number of different ways, slicing and dicing with a number of different criteria. The following sections of this report provide an overall analysis of the EIS portfolio market, looking at how it has grown in recent years, and examining the current opportunities available in the EIS market. Our 2014 report featured a great deal of historical analysis to give context for the growth of the EIS market as a whole. With that in mind, this report focusses more on providing an update over the past year.

The following analysis is broken down:

- Sector
- Objective
- Fundraising Targets
- Returns
- Fees

CUMULATIVE EIS PORFOLIO PRODUCT LAUNCHED (1998-2015)



"2015 saw 45 new product launches, compared with 46 in 2014"

As we discussed in 2014, the market has grown tremendously since its inception; over 22,900 companies have received investment through the scheme, amounting to over £12.3 billion, according to HMRC data. Growth in EIS investments has been particularly strong since 2011. Increased awareness and understanding, a desire to earn higher returns, a need to diversify away from mainstream investments to hedge risk, limits on pension contributions and the recent pension freedoms have all attracted investors to the sector in recent years.

The number of new investments increased significantly in 2011 for a multitude of reasons - the increase in Income Tax relief from 20% to 30% attracted new investment into EIS and the introduction of Feed-in-Tariffs (FiTs) by the Department of Energy and Climate Change (DECC) brought a vast amount of new investment into the renewable energy sector which grew to become the largest sector. Since then, the market has continued to flourish as a result of various legislation changes. Along with historically low interest rates and the introduction of the 50% tax rate for high earners in 2010 to 45% today, there has been a greater demand for EIS.

2015 UPDATE

2015 saw a total of 45 product launches which isn't far off from the 46 of 2014.

While we might have thought that the new regulations could have made sourcing deals more challenging for managers (and that the end of the renewables story in particular could have led to a reduction in fundraising), 2015 saw a total of 45 new product launches, only one less than the total of 46 new products that launched in 2014.

CURRENT OPPORTUNITIES

As of February 2016 there are 53 open EIS or EIS/SEIS investment opportunities listed on MICAP. 14 of these are single company offerings, and the remainder are discretionary portfolio services.

Investment launches often occur in the final quarter of the year and see a large amount of activity ramping up towards the end of the tax year, in anticipation of investors and advisers putting their tax affairs in order in April. It is also worth noting that several investments launched in 2014 and 2015 and closed in early 2015.

MINIMUM INVESTMENT LEVELS

Investment levels are a good indication of how accessible a market is for investors; a low minimum subscription level makes it fairly easy for investors to enter the market.

Based on our data, the level of investment required for open EIS investment portfolios at the time of writing, ranges from £10,000 to £50,000, illustrating the wide range of initial investment subscriptions. A quarter of funds require minimum investment levels of £10,000, and about half between £10,000 and £25,000.

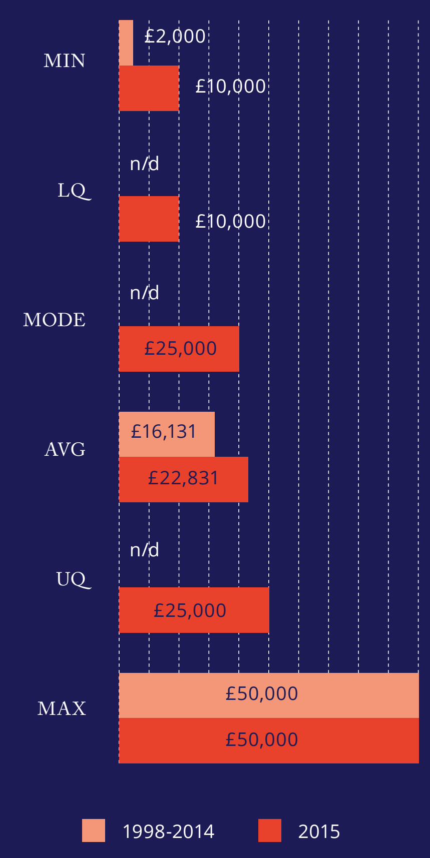
The average minimum subscription has increased from just over £16,000 to just under £23,000. The average has been pushed up from the bottom - the highest minimum subscription level remains £50,000.

Note that this data reflects EIS funds - much lower minimum investment levels will be found in single company EIS opportunities (think of somebody raising a couple of hundred grand for a film for example).

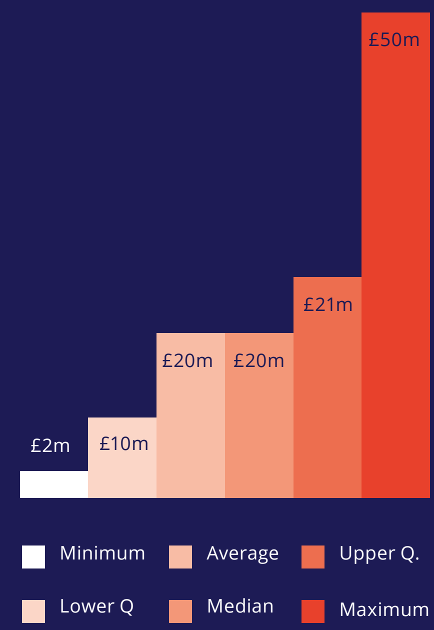
The entry level of investment is closely linked to the fundraising level. For portfolio services the range of fundraising targets varies from £2 million up to £50 million. However, the majority of fundraises target under £21 million. Historically, the average fundraising target is £12.84 million - and the low is lower and high is higher, so today we have a tighter range of targets.

Note that there are also a number of evergreen funds, which don't specifically have an upper limit or target level to their fundraising.*

MIN. INVESTMENT (1998-2015)



FUNDRAISING LEVELS (Q1 2016)



*A more detailed analysis of fundraising targets will be explored in the fundraising section.

SECTOR ANALYSIS

HMRC divides the EIS market into ten different sectors, and different providers use different ways of breaking down the market. For our analysis, we have followed the sectors used by MICAP for ease of comparison. MICAP divides the EIS market into nine principal industry sectors which can then be broken down into a number of specific sub-sectors. However, at the time of researching this report, three specialist sectors (Sport & Leisure, Transport and Pharmaceuticals/ Biotechnology) were represented by single company EIS, so they have been excluded from the following analysis. The analysis is broken down a follows:

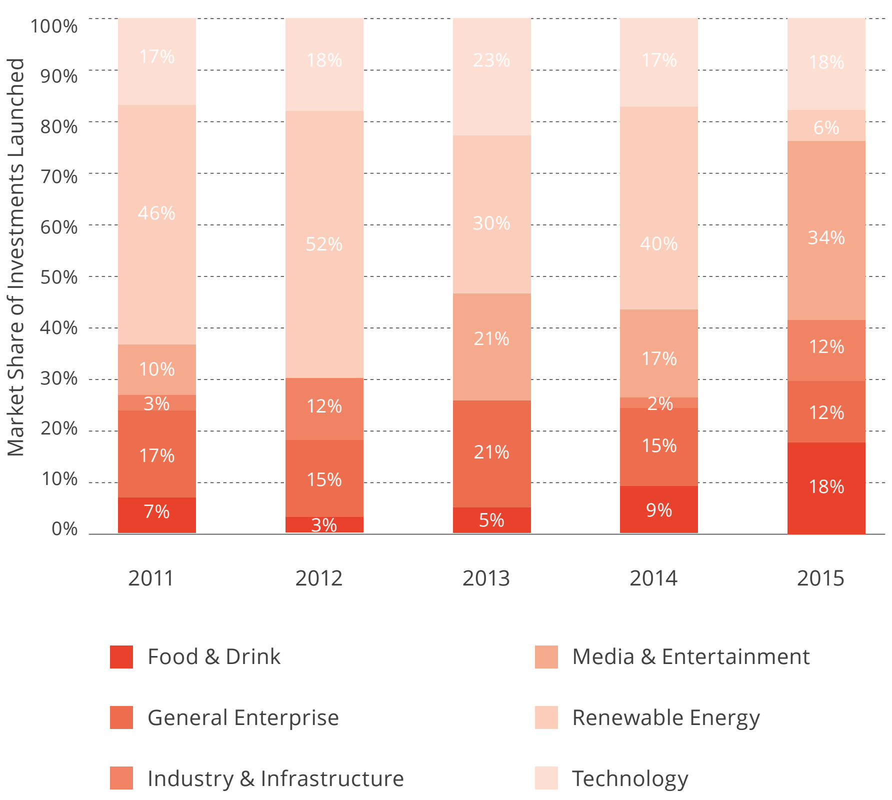
- Food & Drink
- General Enterprise
- Industry & Infrastructure
- Media & Entertainment
- Renewable Energy
- Technology

Since 2010, the EIS market has grown and the landscape has changed dramatically. Media & Entertainment and Food & Drink have seen a rise in their market share (based upon the number of investment opportunities available), whereas Renewable Energy has shrunk. Sectors such as General Enterprise and Technology have maintained a fairly consistent proportion of the market in the past few years.

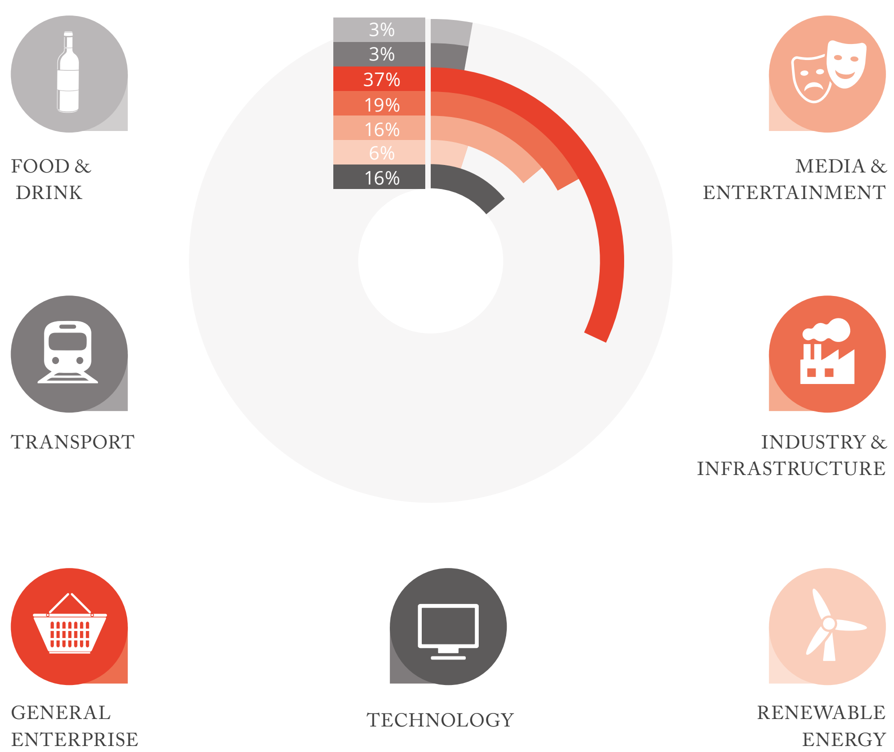
RENEWABLE ENERGY

The renewable energy industry emerged in the EIS market in 2008. The introduction of Feed-in-Tariffs (FiTs) in April 2010 had particular success in encouraging new investment until 2012, when most trades attracting FiTs or overseas equivalents were excluded from benefiting from EIS. However, some exemptions such as Hydro and Anerobic Digestion still existed. The 2014 Finance Act removed these exemptions and the government continued to monitor renewable energy projects. As of April 2015 "all companies substantially benefiting from the generation of renewable energy have been excluded from the EIS".

MARKET SHARE BY SECTOR BY LAUNCH YEAR (2011-2015)



OPPORTUNITIES BY SECTOR (OPEN PORTFOLIOS) (Q1 2016)



"Infrastructure continues to offer the kind of predictable and uncorrelated returns that investors find appealing given continuing market volatility and low interest rates" **Ben Thompson, Foresight Group**

The result of this has been a huge reduction in the number of EIS projects in the Renewable Energy industry; a mere 6% of investments launched in 2015 were in the Renewable Energy sector as compared to 40% the previous year.

MEDIA & ENTERTAINMENT

In recent years, media & entertainment has become a significant sector in the EIS market. The number of new media investment opportunities has been increasing, both within portfolios as well as via single company investments (see page 72). Media & Entertainment has certainly grown in terms of market share, accounting for 34% of investment opportunities in 2015 versus 10% in 2011.

Film and TV production lends itself well to EIS financing because potential earnings streams are often visible and secured against strong counterparties. Investee companies finance either the whole or part of production, recouping earnings in a variety of ways. Additionally, many of the companies benefit from a UK Government rebate, up to 25%, for UK qualifying film production with a budget of £20m or less or up to 20% for films with higher budgets.

TECHNOLOGY

Following the collapse of the dot-com bubble; technology lost a great deal of market share. However, since then, the sector has grown steadily and significantly, consistently capturing close to 20% of the available opportunities.

Technology is predominantly a growth-focused sector and is therefore well suited to the EIS. The targeted returns within this sector tend to be high and it is easy to see why this sector is attractive to investors.

FOOD & DRINK

Food & Drink companies such as pubs and restaurants have been popular EIS investments since the beginning of EIS. Such businesses can prove attractive to investors in part due to the asset-backed nature of the businesses.

The sector has undergone various changes in recent years, particularly in response to the smoking ban introduced in 2007. Nevertheless, the sector has maintained a steady EIS presence. In recent years, many managers have reorganised their business models around perceived changes in consumer preferences. One example of how entrepreneurial managers have used EIS funding is investment into the 'gastro-pub' market to capitalise on changing consumer habits.

We may see the popularity of these investments fall in years to come, as new regulation prevents EIS funds being used to acquire existing businesses. Pubs and restaurants EIS opportunities look to buy existing proven locations and this will no longer be an option.

INDUSTRY & INFRASTRUCTURE

Industry & Infrastructure EIS qualifying companies operate in a range of areas, such as manufacturing, cars, heavy equipment, aerospace, roads and business services. These tend to be heavily asset-backed, commonly targeting a capital preservation objective. Previous to 2014, there were fewer EIS portfolios focused in this sector, but in 2015 they accounted for 12% of new product launches.

Some managers that had previously focused on renewable energy have moved into this sector after the legislation changes. This has been a very logical move for them, as many have chosen to focus on energy infrastructure companies which still qualify for EIS reliefs.

Other sectors in the market range from precision engineering, construction and storage.

"The Enterprise Investment Schemes market has historically seen considerable sums invested into asset-backed and subsidised industries, such as renewable energy. By removing such sectors from EIS qualification, the UK Government is seeking to ensure that EIS is utilised for its original purpose of creating jobs or innovation. The Government wants investors to be taking appropriate risk in order to be rewarded with the potentially generous tax reliefs on offer. As there are fewer 'lower risk' opportunities available, EIS providers have to be much clearer in showing how they manage risk and increasingly transparent about what companies they are investing in"

Ian Warwick, Deepbridge Capital

ANALYSIS BY OBJECTIVE

The following section looks at the market broken down by the fund's stated investment objective.

Providers may use a variety of terms to classify their investment strategies and risk profiles, but for the purpose of this report we have used the investment objectives that are used for MICAP's Risk Matrix. This provides a guideline to gauge inherent investment risks of EIS investments (a full overview of the MICAP Risk Rating Matrix can be found at *www.micap.com*). These categories are:

- Capital Preservation
- Capital Preservation & Growth
- Growth
- Super Growth

The investment objective is important in determining the risk to an investor. Capital preservation aims to achieve returns at least in line with inflation. Capital preservation & growth aims to do slightly better, while still following a conservative strategy. Growth and super growth portfolios take on more risk and aim for higher returns. However, as we will point out on page 70, there is sometimes some crossover between growth and capital preservation strategies when we examine the level of return they target.

Looking at the overall current market we can see that the majority of open investments (41%) have a growth objective. This is unsurprising, considering the aim of EIS is to stimulate investment into small companies in order to fund their growth. Only a further 13% of EIS investments have an objective of super growth, which is likely to be to be characterised by small, start-up companies seeking very high, early growth. Seed EIS (SEIS) is also likely to capture this end of the market where investee companies may be at very early seed funding stages.

Capital preservation accounts for 12% of the opportunities and capital preservation & growth accounts for 31%. Capital preservation investments are often backed by contractual income streams, tend to be asset-backed and are perceived to have a high-creditworthiness and low investment risk. Capital preservation & growth investments contain asset-backed investments and fall into a slightly higher risk category because the ongoing earnings stream, though resilient, may be less predictable than companies whose revenue streams are guaranteed. However, if they were to fail, the assets could be sold, offering a degree of capital protection.

Splitting the market across sectors allows us to see trends and where some of the lower risk investment objectives can be found.

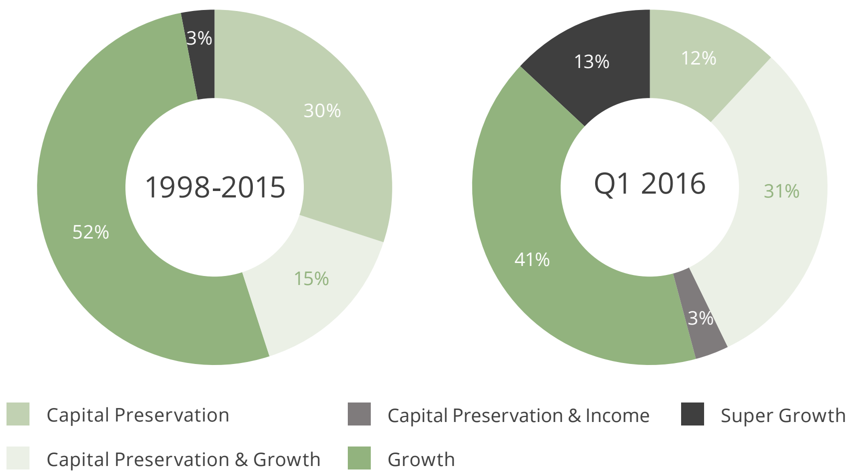
Traditionally, capital preservation investments have had a larger presence in the renewable energy and infrastructure sector. However, the removal of EIS relief in the renewable energy industry in 2014 has resulted in a reduction in capital preservation opportunities within the renewable energy sector.

Media & Entertainment can be another industry that lends itself to a less risky investment strategy, where projects can be completed and sold quickly, returning the investment back to cash in a relatively short timeframe.

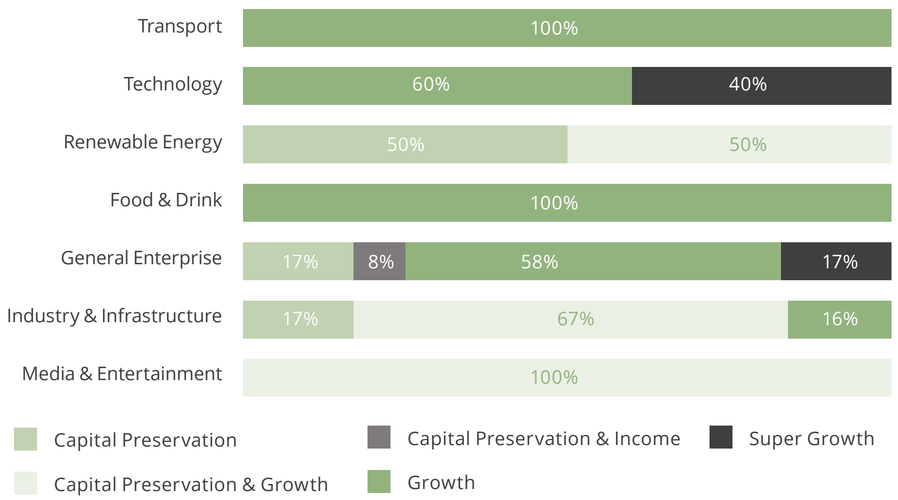
Technology, on the other hand is 100% either growth or super growth, which reflects the high risk / high return nature of this sector where there are many opportunities to fund early stage companies.

The remaining sectors consist of a mix of strategies and, as expected, there is an emphasis on growth.

INVESTMENT OBJECTIVE* (1998-2016)



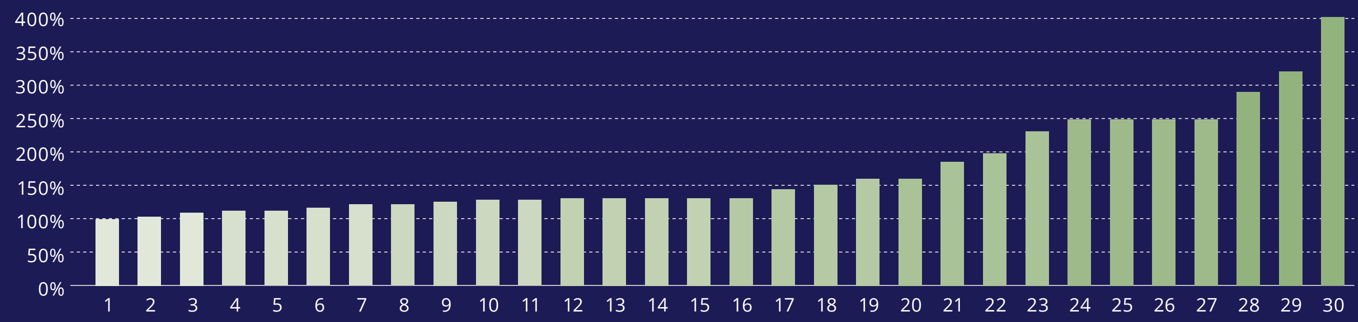
SECTOR BY OBJECTIVE (Q1 2016)



*Open portfolios

RETURNS ANALYSIS

DISTRIBUTION OF TARGET RETURN (OPEN OPPORTUNITIES) (Q1 2016)



The following section looks at returns available in the current EIS market (based upon the managers' stated target levels of return). It is important to examine the returns of the underlying investment opportunities because often too much emphasis can be placed on the tax benefits of EIS, instead of the investment case of the investee companies. As a result, the returns may appear disproportionately attractive.

Advisers and investors should be careful when evaluating an investment's forecasted returns because it is not always clear if these are calculated before or after tax reliefs and different funds state their returns differently. If forecasted targets are stated after tax reliefs, the stated return will be magnified. The lack of uniformity makes assessing the market tricky since investments with returns stated before tax relief are likely to understate their overall benefits. It is also important to note that the tax benefit is dependent on the marginal tax rate of the investor.

OVERALL RETURNS

All investments in the EIS market offer variable returns, there are no products able to offer a fixed rate of return. Target returns are typically stated as a total return for the investment period, often as a multiple of a return of capital; this can make investments appear extremely attractive. However, it is important to bear in mind the likely investment term and consider how strong the possibility of an exit is.

It is worth noting that not all investments disclose target returns. Almost 20% of the investments we have looked at have not quoted targeted returns in their marketing literature or provided these upon enquiry. Therefore, we can only comment on a sample of our data.

As of February 2016, the average total return targeted is 172%. The minimum is just 100% and the maximum is 400% (excluding single companies).

BY SECTOR

As of February 2016, the General Enterprise sector offered average target returns of 207%, with a minimum of 110% and maximum of 400%.

Industry & Infrastructure was lower on average at 135%, with a minimum of 110% and maximum of 198%.

The biggest sector (by open opportunities), Media & Entertainment, offered 149% total return on average, with a minimum of 104% and maximum of 290%.

Technology offered 198% on average, ranging between 130% and 320%, and the few remaining renewables opportunities offered target returns of 110% on average.

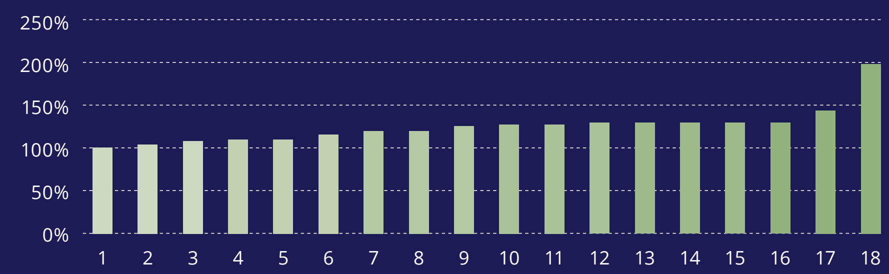
BY INVESTMENT STRATEGY

Portfolios with either a Capital Preservation, Capital Preservation & Growth or Capital Preservation and Income mandate offered a target return of 126% on average, with a minimum return of 100% and a maximum of 198%.

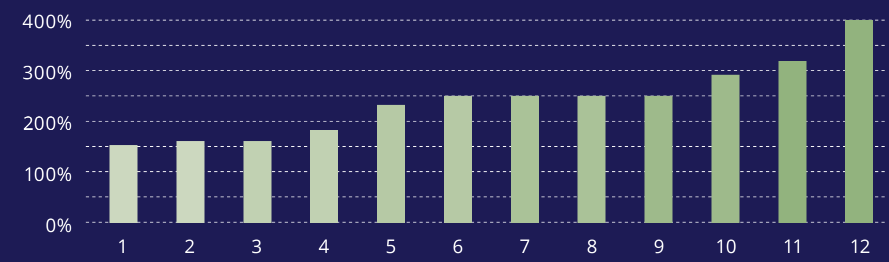
Portfolios with either a Growth or Super Growth mandate offered a target return of 241% on average, but this was dragged up by an outlier targeting 400%.

If the outlier is excluded, than the average target return for Growth and Super Growth portfolios is 227%. The minimum level of return targeted in this segment is 150%.

PORTFOLIOS WITH A CAP. PRESERVATION MANDATE* (Q1 2016)



PORTFOLIOS WITH A GROWTH MANDATE* (Q1 2016)



*Where stated

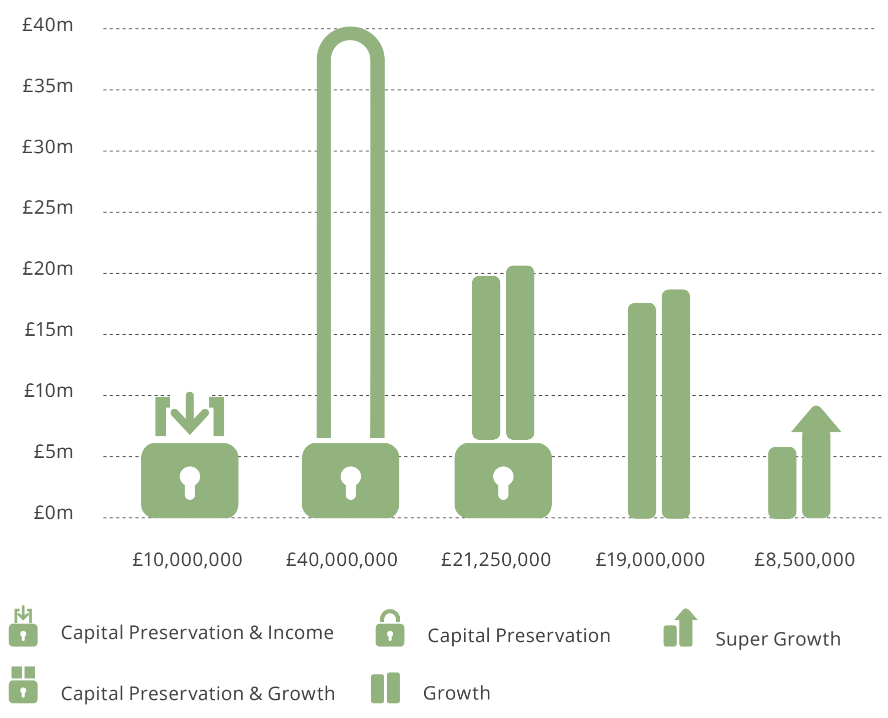
FUNDRAISING ANALYSIS

As stated elsewhere in the report, fundraising within EIS is strong and has been increasing year-on-year.

Even though we have seen some uncertainty brought about by changes in legislation in 2015, and even though the very popular Renewable Energy sector has now been excluded, the EIS scheme still raised a record breaking £1.5 billion in the tax year 2014/15.

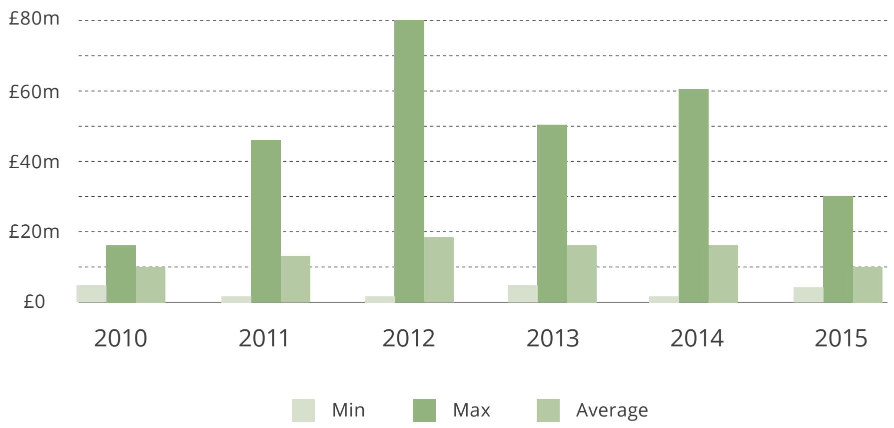
It has previously been estimated that around half of fundraising was attributable to single company EIS opportunities. We would speculate that with the increase in the number of providers in this space and the growing levels of awareness of the market, that the majority of fundraising is now going into portfolios (funds).

AVERAGE TARGET FUNDRAISING BY OBJECTIVE (Q1 2016)



Looking at fundraising targets by objective, we can see that the riskier, more growth-oriented companies have smaller fundraising targets. Super growth has the lowest fundraising targets, on average, and capital preservation has the highest. This may indicate capital preservation funds have a larger potential investment universe than high growth funds which need to identify new, fast growing companies.

TRENDS IN FUNDRAISING (2010-2015)

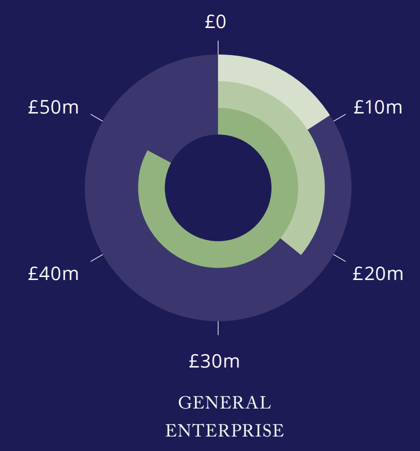


This looks at the historical fundraises from 2010 to 2015. The 2014/2015 report examined trends in fundraising targets from 1998 to 2014. Looking closely at recent years, average fundraising targets have remained fairly consistent, averaging between £10 million and £20 million. However, between 2010 and 2012, maximum portfolio target fundraises increased enormously, coinciding with the legislation increasing the investment limit for EIS companies, and the boom in renewables.

There has been a fall in the maximum fundraising targets over the past year from £60 million to £30 million.

*Where stated

FUNDRAISING TARGET BY SECTOR (Q1 2016)



It is interesting to see the difference in fundraising targets across sectors. Historically, Renewable Energy has been the largest sector by size, due to several factors – high investment costs, investor demand and a large amount of deal flow.

The Industry & Infrastructure, General Enterprise and Technology sectors have the largest fundraising targets, with Media & Entertainment not far behind with an average target of just over £18 million.

Technology has the largest range of fundraising targets.

With few open offers at the time of writing (Feb 2016), there is little to say about the fundraising targets in Renewable Energy or the Food & Drink sectors.

"Although investments benefiting from subsidies have been disqualified, energy infrastructure investments are still EIS eligible and investors can still benefit from managers' extensive experience in the sector"

Mike Currie, Foresight Group

SINGLE COMPANY ANALYSIS

For investors, there are two main ways of accessing the EIS market; either by investing directly into an EIS company, or into a managed portfolio. A managed portfolio/fund will pool together EIS qualifying investments in one fund in accordance to the investment objective the fund managers choose to adopt. While there are a good number of EIS portfolios to choose from, information on funds is relatively easy to access when compared to single company investments.

Single company investments may provide more active investors with more interesting and engaging opportunities, and with the increasing popularity of crowdfunding, accessing these investments has never been easier (we analyse the role of the crowdfunding platform in another section).

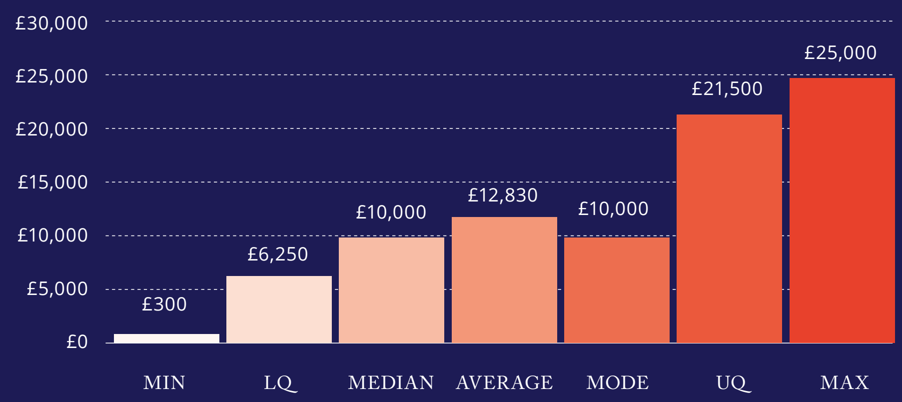
Since the launch of EIS in 1994, over 22,900 companies have received investment through the scheme, with over £12.3 billion funds raised (HMRC).

For this analysis we have relied on the MICAP Fund Finder, but this only represents a small sample of the total number of companies seeking EIS investment in the UK, we just don't have the reach to obtain data on all the single companies out there.

INVESTMENT LEVELS

The range of investment levels required for a single company varies greatly, from as little as £300 to £25,000. The average subscription level, at £12,630, is significantly lower than for portfolios, making them more accessible to investors. This is expected; a portfolio has monies split across a number of underlying companies and therefore a greater amount of capital is required to ensure the portfolio is well managed and sufficiently diversified.

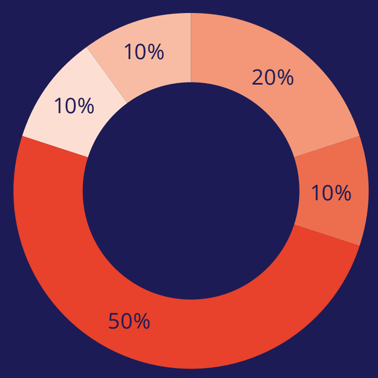
RANGE OF INVESTMENT LEVELS (Open Nov 2015)



OBJECTIVE

Historically, growth has been the largest objective in the EIS market amongst single companies with capital preservation following shortly behind. There also more super growth investments amongst single companies. This is expected since the nature of EIS companies is to encourage growth and enterprise.

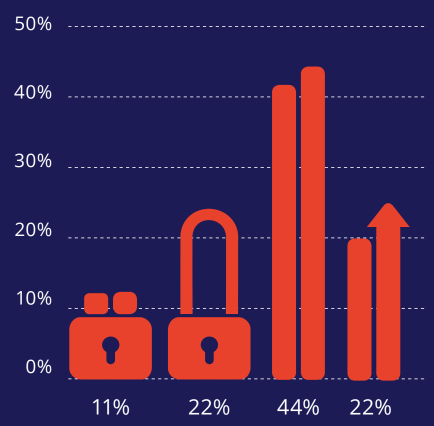
INVESTMENTS BY SECTOR



As with portfolio investments, Media & Entertainment is the largest sector in the EIS market, indicating the number of projects that launch in this dynamic sector. Food & Drink is the next biggest sector. While both sectors are can be widely accessed in portfolios, investors can expose themselves to these opportunities with smaller allocations through a single company investment.

Media & Entertainment
Renewable Energy
Food & Drink
Industry & Infrastructure
Technology

MARKET BY OBJECTIVE

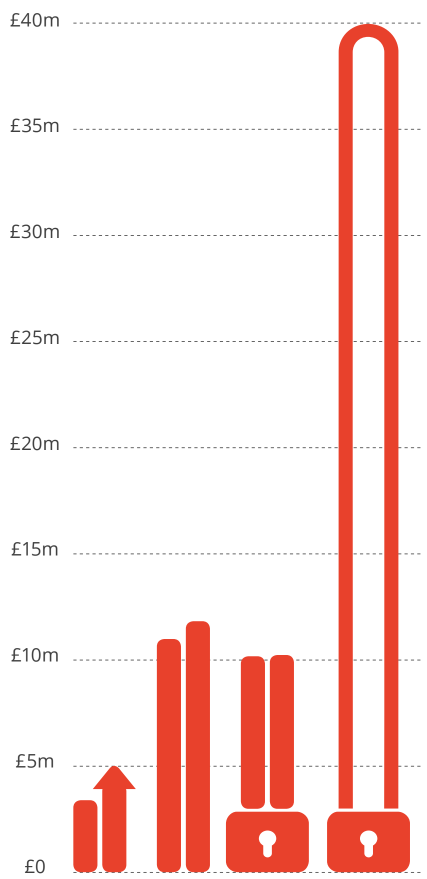


Capital Preservation
Super Growth
Capital Preservation & Growth
Growth

"Single companies as compared to portfolios are likely to be riskier since the risk isn't hedged over multiple investments"

AVG FUNDRAISING TARGET

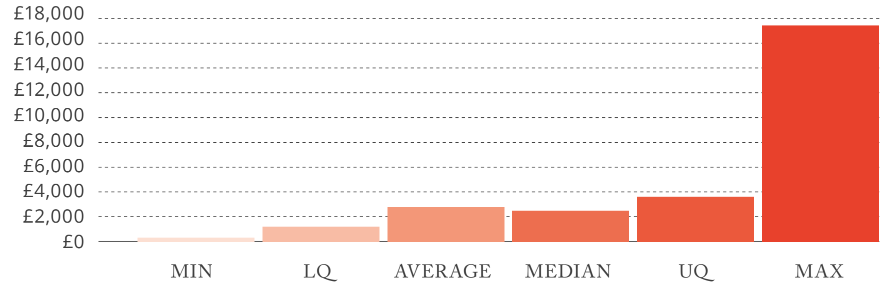
OPEN NOV 2015:



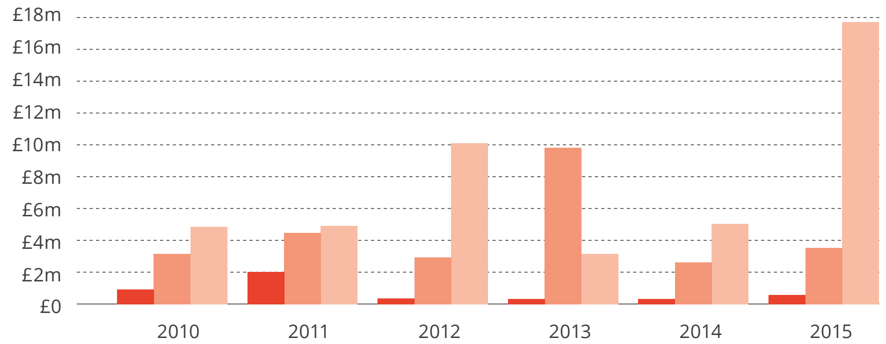
Super Growth
Growth
Capital Preservation & Growth
Capital Preservation

The fundraising target varies greatly depending on the strategy adopted by the company. According to our data, capital preservation oriented companies look for more money on average.

RANGE OF FUNDRAISING TARGETS (Open Nov 2015)

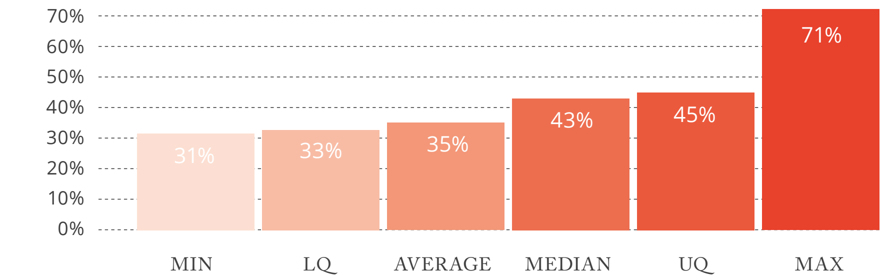


FUNDRAISING TARGETS BY LAUNCH YEAR (2010-2015)



We can see that the range of fundraising targets for single companies is incredibly wide. The maximum recorded target at £17.5 million is 100xs larger than the lowest recorded target at £175,000. This range has increased over the past few years. We can see that not only has the maximum target increased from £4.5 million, but the minimum target has also decreased from £1 million. The discrepancy in size is down to fundraisings (previous to the summer Budget 2015) being used at a variety of stages and reasons.

ANNUALISED TARGETED RETURNS (Open Nov 2015)



On average, the returns targeted by single company EIS investments are exceptionally high compared to mainstream investments. They are even higher than EIS portfolio investments which average at 26%. The maximum return recorded at 71% is not representative of the market and therefore may skew the data to look a little misleading. Nevertheless, excluding this outlier, we still find an average targeted return of 34%.

Single companies are more risky than EIS funds as there is no diversification. Accordingly, the potential returns are higher. It has been estimated that single company EIS account for half of all EIS funds raised, although this is only an estimate and has not been verified. We suspect that while this might have been true once, with more managers entering this space they now comprise the majority of the fundraising. However, we should not underestimate the role crowdfunding is playing in bringing single company EIS investments to a new market. Whether this is a good or bad thing remains to be seen.

FEES ANALYSIS

The following section looks at the charges associated with EIS investment opportunities.

EIS portfolios often use the experience and expertise of a specialist investment manager, which is accompanied with various fees. High charges are one of the main criticisms associated with EIS investments.

As we explained in the 2014/15 report, there are three main charges that are levied on almost every investment in the market; an initial fee, an annual management charge (AMC) and an exit performance fee.

The initial fee is often taken upfront and therefore affects the amount of capital that actually reaches the underlying investments that reliefs can be claimed on. Looking at the market as a whole, the initial fee ranges from 1.00% to as high as 5.00%. The average at 3.7% is extremely high when compared to mainstream fund based investment opportunities, and could have a dramatic impact on returns. Having said that, there are higher costs associated with EIS investments as they are more specialised; sourcing deals, research, due diligence and ongoing monitoring are expensive to maintain.

The annual management costs (AMC) covers the active management involved with EIS funds and portfolios and is commonly taken as a percentage of the investment subscription to the adviser on an annual basis. The lowest AMC found at 0.5% is very competitive, even compared to mainstream funds. The average is 1.66%.

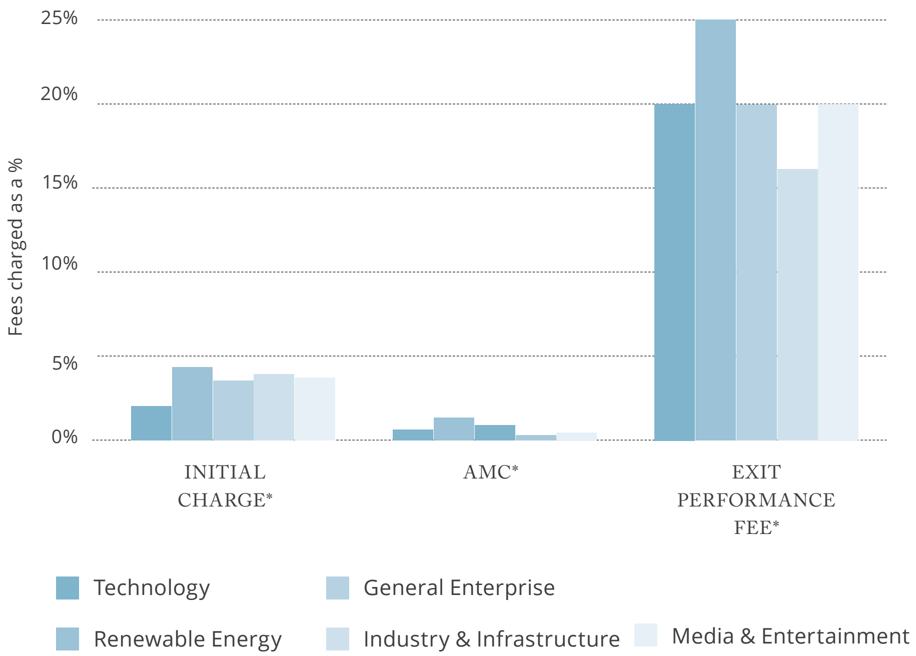
The performance fee is charged on exit when underlying companies are sold and profits are realised. The fee is usually set based on a hurdle rate (most commonly 120%), so a fee of 20% is charged on any profit above 120p for every 100p invested. The performance fee incentivises managers to return a profit as they share in the success. However, it could result in managers taking on more risks in search of this profit, or could potentially mean that they are unfairly rewarded with a high share of profits when they haven't truly earned them.

RANGE OF FEES (Q1 2016)

	Initial Fee (%)		AMC (%)*		Exit Performance Fee (%)	
	Open	1994-2014	Open	1994-2014	Open	1994-2014
MIN	1.00	1.00	0.50	0.50	16.00	10.00
LQ	2.5	N/A	1.50	N/A	20.00	N/A
AVG	3.7	4.30	1.66	1.82	21.70	20.00
MEDIAN	4.25	N/A	1.50	N/A	20.00	N/A
MODE	5.00	N/A	2.00	N/A	20.00	N/A
UQ	5.00	N/A	2.00	N/A	20.00	N/A
MAX	5.00	6.50	2.50	3.00	35.00	25.00

Some providers take the initial fees from the investee company rather than the investor. This leaves the full amount of the investment available to claim tax relief on. Some providers also choose to take their ongoing fees from the investee company, and only take a performance fee from the investor. This makes their proposition fee-free to the investor until the manager has exceeded their performance target.

FEES BY SECTOR (Q1 2016)



*Where charged

"EIS portfolios often use the experience and expertise of a specialist investment manager, which is accompanied with various fees"

We can look at the fees charged by sector. For this we have only conducted analysis on five sectors since there is not sufficient information to undertake meaningful analysis on the others. Again, this is based on where fees are applied - as noted above not all products apply initial and ongoing fees to investors.

There is some variation in the AMC across sectors, with AMCs ranging from 0.5% to 2%. The average AMC for each sector on currently open investments is lower than historically. This could be an attempt by managers to make EIS investments more competitive than it has been historically.

There is more variation in initial charges and performance fees.

The Renewable Energy sector charges the highest average performance fee at 25%. This may reflect the manager's confidence that these projects will deliver returns as expected.

Renewable Energy and Industry & Infrastructure both charge the highest initial fees, on average around 4%.

This could be due to high upfront costs required at the beginning of the investment term. However, the Industry & Infrastructure has the lowest average AMC and performance fees in the market.

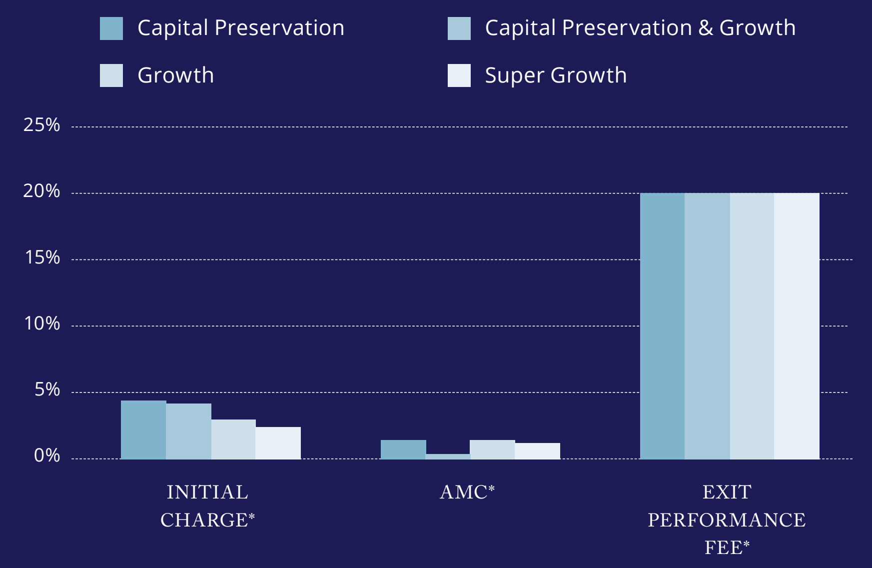
Overall, while there are some differences in fees when we break the market down by sector, they are not that large. We also note that fees do seem to be coming down compared to their historical average.

FEES BY OBJECTIVE

The average performance fee was the same across all investment strategies. However, initial charges (where they are levied) are higher with more conservative strategies.

This could reflect the fact that there is less potential to earn high performance fees.

AVERAGE CHARGES BY OBJECTIVE (Q1 2016)



CONCLUSIONS

- The EIS market has seen incredible growth since 2010
- There are six main sectors for EIS investments. Media & Enterprise has experienced the most significant growth to become one of the largest sectors
- The exclusion of subsidised Renewable Energy investments benefiting from EIS has resulted in a reduction of renewable energy projects in the EIS market. The effect of this is likely to be felt over the coming tax year. Since renewable energy has been a significant part of the EIS market, the reduction may be responsible for slower growth in the EIS market
- Growth is the most common investment objective with 41% of portfolio investments stating growth as their primary objective
- Targeted returns for EIS investments are significantly higher than mainstream investments. Single company investments target higher returns than portfolios. Food & Drink sector targets the highest returns
- The range of fundraising targets for EIS portfolio investments varies. Portfolios with capital preservation strategies, on average, target significantly higher fundraises
- The average AMC is fairly consistent between 0.5% and 2%. There is greater fluctuation in initial fees across investments, averaging around 3.7%. The average exit performance fee is 20% of any return over the hurdle rate
- Not all products apply initial and ongoing fees to investors, so 100% of the investment can be used to claim tax relief.

*Where charged

MARKET RESEARCH

ADVISER SURVEY

The intention of the survey is to gauge how advisers feel about EIS, in what circumstances they use EIS, what criteria advisers use to assess products and what factors make them hesitate to use EIS.

METHOD

The adviser survey was carried out from October to December 2015 in conjunction with the EISA. We gathered a total of 297 responses, making this the largest every study of advisers and their feelings about EIS. The responses were collected both online and on paper and the survey was distributed at PFS events, our own EIS Masterclasses and by our report sponsors. Respondents were given the chance to win one of five tickets to the Chairman's Reception at the House of Lords in February 2016 as an incentive to participate.

ADDITIONAL SURVEYS

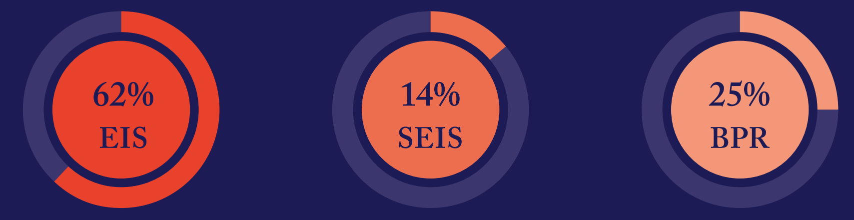
We also surveyed providers, asking them similar questions to advisers so that we can try and identify where there might be gaps between what providers believe advisers want, and what advisers actually want. For the most part, we did find that providers and advisers' perceptions were aligned.

Finally, we surveyed investors. Given the difficulty of accessing investors, this survey was carried out by a 3rd party company and the questions covered VCT and BPR investments in addition to EIS.

Taken together, the intention of the surveys is to give readers a 360 degree view of the sector from the perspective of all of the market participants.

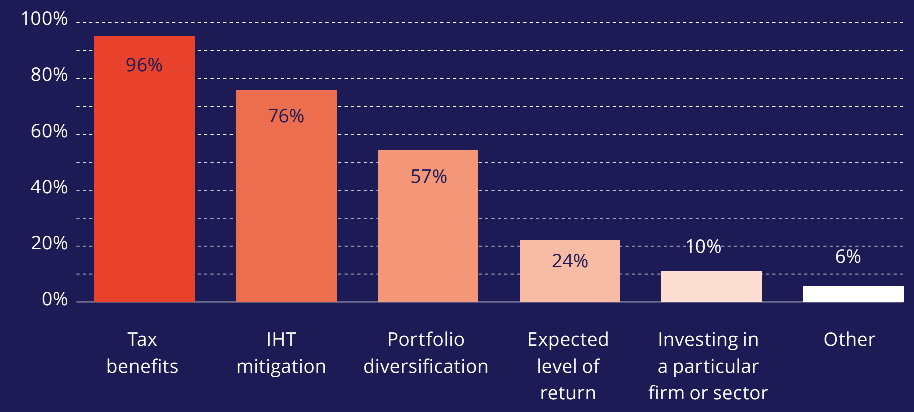
The provider and investors surveys follow on after the adviser survey.

DO YOU RECOMMEND ANY OF THE FOLLOWING INVESTMENTS TO YOUR CLIENTS?



76% of respondents recommended either EIS or SEIS to their clients. Only 25% of advisers did not recommend either. This finding is consistent with our 2014 survey and possibly indicates that there is a rump of advisers who are not engaging with the market. Of course what this result doesn't tell us is how much advisers invest in EIS – we examine this later on in a later question.

WHAT ARE YOUR TOP 3 REASONS FOR RECOMMENDING EIS & SEIS?



Respondents were able to choose up to three answers to this question and unsurprisingly 96% of advisers indicated that the tax benefits are one of their main reasons to recommend EIS or SEIS investments. This compares to 91% of respondents in 2014.

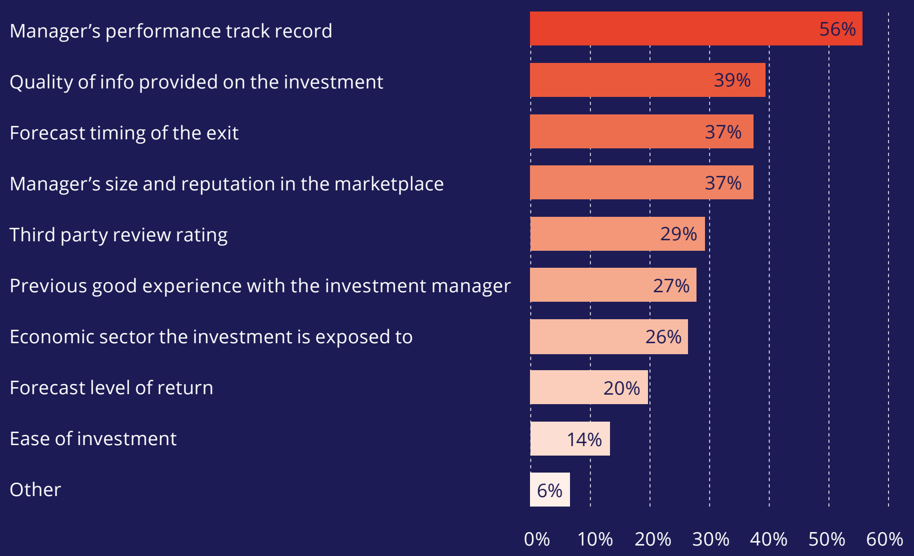
This year we also gave respondents the option of specifically identifying IHT mitigation as a reason for recommending EIS. This was not something we examined in 2014, but based upon our work with advisers we suspected that this might be a key driver. Our suspicions were proved correct, with 76% of our sample indicating that this was one of their top three reasons for recommending EIS. We believe that this is an indication of changing financial planning needs within advisers' client banks as the baby-boomer generation starts to retire (baby-boomers control 80% of private wealth in the UK by some estimates).

57% cited portfolio diversification (compared with 61% in 2014). The targeted level of returns or gaining exposure to a particular firm or sector was seen as less important. Other stated reasons for recommending EIS or SEIS were the reduction in pension limits or as an alternative to pensions – which really links back to the tax benefits in our opinion.

Based on this result, providers may want to consider doing more to highlight IHT mitigation and the diversification benefits (we think that the other tax benefits are already well understood as they have been successfully promoted by the industry), whereas focusing on the expected level of return won't influence the majority of advisers.

"The biggest change since 2014 is the placing of manager's size and reputation in the market place"

WHAT ARE THE MOST IMPORTANT FACTORS WHEN CHOOSING AN EIS OR SEIS INVESTMENT?



Advisers could select up to three responses here.

56% of advisers selected the manager's performance track record as the most important criterion when choosing an EIS or SEIS, making it the most common response; up from the second most common response in 2014 (53% of respondents chose this is 2014).

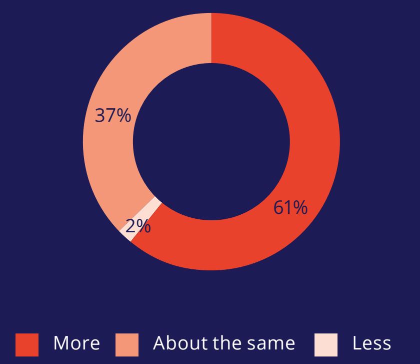
This is an interesting result as providing up to date, meaningful performance information is not always easy for EIS managers – they are reluctant to disclose valuations of companies that they intend to sell in the future, and in any event small company valuations can be very esoteric. We mentioned this in the 2014 report, but is there a case for a concerted industry effort to report standardised performance information?

The biggest change since 2014 is the placing of manager's size and reputation in the market place. This was the most common response in 2014, with 63% of respondents selecting it, but this year it is only in fourth place with 37% of advisers selecting it. This may indicate that as advisers have learned more about the EIS sector they are being more discerning about who they work with and not just relying upon picking the best known brands.

The quality of the information provided on the investment seems to have become more important, and is now the second most important criterion (39%), up from joint fifth in 2014 (32% of respondents chose this is 2014). We can speculate that this is linked to the point above: if advisers are becoming more discerning, than they need high quality information to base their decisions on.

Exit risk came in third place with 37% of respondents indicating it was a key criterion; exactly the same result as 2014. Previous good experience with the manager (27%) and the economic sector the investment is exposed to (26%) were also important criteria.

DO YOU SEE YOUR USE OF EIS OR SEIS IN CLIENT PORTFOLIOS CHANGING OVER THE NEXT 12 MONTHS?



61% of respondents believed that their use of EIS will increase, compared to 53% in 2014, an indication that not only will the market will continue to grow strongly, but that growth could still accelerate. When we quizzed advisers on this point, most of them indicated that they felt changes to the UK pension regime would drive more investment into EIS.

37% of respondents felt that their use of EIS would remain about the same and only 2% of advisers forecast a decrease, compared with 42% and 5% in 2014.

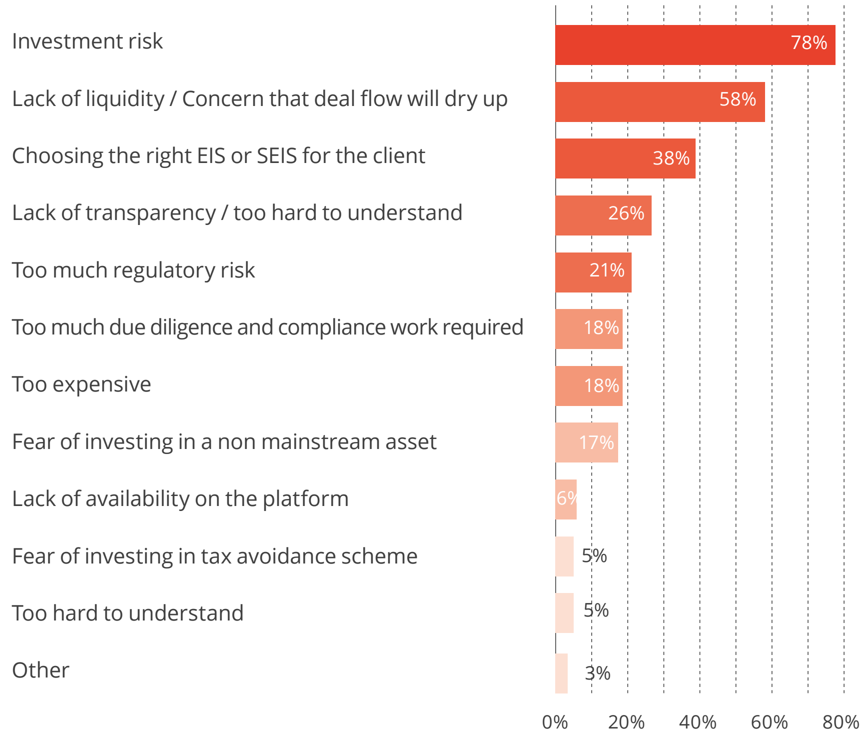
IN YOUR OPINION, WHAT SINGLE CHANGE OR INNOVATION WOULD IMPROVE THE EIS OR SEIS MARKET?

When posed this question, advisers had different opinions on what single change or innovation would improve the EIS or SEIS market. The most common suggestions were increased levels of transparency, availability and ability to compare "similar" EIS and SEIS schemes. Advisers also mentioned a wider understanding in the marketplace, providing better education and access via platforms as changes that would improve the EIS or SEIS market.

"Increasingly, entrepreneurial smaller businesses in the UK are looking to EIS investors to help provide the capital they need to meet their growth potential. Access to finance remains a key issue for these types of businesses with the Octopus High Growth Small Business Report 2015 revealing that one in four of the country's fastest-growing smaller companies are finding it difficult to secure the funding they need. Equally, these figures demonstrate how investors are realising the benefits that EIS offer as part of a well-balanced portfolio, as well as the role they play in supporting the next generation of UK businesses" **John Thorpe, Octopus Investments**

"Offerings where there is little or no investment risk really ought to carry a health warning for investors and are likely to carry increased 'tax risk' in the future, as HMRC's torch will bring them into sharp focus" **Ian Battersby, Seneca Partners**

WHAT ARE YOUR TOP CONCERNS WHEN RECOMMENDING EIS AND SEIS?



We changed tack on this question a little bit this year, making direct year-on-year comparisons difficult.

Previously this question was split into two, as we asked advisers who did recommend EIS what factors would make them hesitate, and we asked advisers who did not recommend EIS what their reasons for not doing so were. This year, to simplify the survey and get more responses, we amalgamated the two questions and simply asked what advisers' biggest concerns were. Again, respondents could tick up to three answers.

Unsurprisingly investment risk scored highest (78% of respondents), followed by lack of liquidity or fears that there would not be sufficient deal flow (58%). These are issues that providers can address to some extent by educating advisers about their processes to try and engender confidence, but ultimately risk and illiquidity will always be a concern with EIS investments: it's one of the reasons qualifying companies can struggle to raise capital and therefore by extension it's one of the reasons why the tax reliefs are in place.

Perhaps more surprisingly is that choosing the right (S)EIS for a client was the third most commonly cited concern. This suggests that advisers struggle to assess the whole of market and select a product with confidence, perhaps because "apples to apples" comparisons can be so difficult. Again, it could indicate that standardised information on performance, charges and other key pieces of information could help advisers here.

CONCLUSIONS

The survey indicates that more advisers are using EIS than last year and that they expect to invest more of their clients' money over the next 12 months; clearly a positive result for the industry that seems to be driven by reductions to the amounts that can be saved into pensions and the threat to higher rate tax relief. Nobody will be surprised to learn that tax is the biggest reason why people invest in EIS.

Digging a little deeper though, it does appear that advisers are becoming more discerning about which products they choose and don't follow the market leaders to the same extent that they used to: they are increasingly citing accessing performance history, receiving good quality information on the investment and being able to make meaningful comparisons between funds as their concerns.

Standardising the way information is presented could be one way that the EIS industry could encourage even higher levels of investment from advisers.

The unexpected finding was that IHT mitigation is seen as one of the top three reasons for investing by so many advisers, perhaps an indication of changing financial planning needs within their client banks. It would be interesting to know how many EIS investments got rolled over into pure BPR investments once they exit.

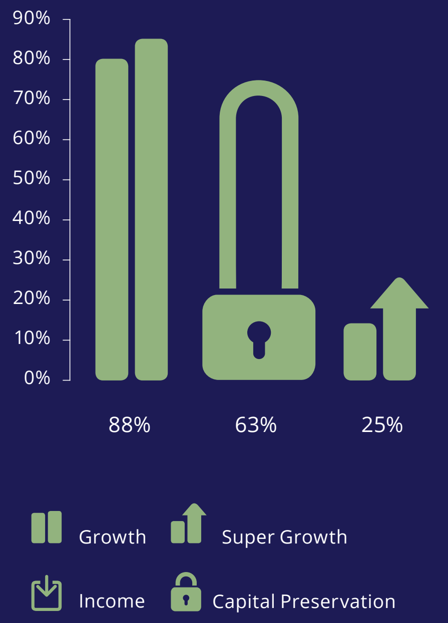
Finally, concerns about investment risk and liquidity are still prevalent. We think that this is a fact of life investing in this universe, but managers shouldn't forget to explain how they mitigate these risks when they are talking to advisers. It might be basic, but it is important.

PROVIDER SURVEY

"The most requested change was a call on HMRC to make the process for claiming tax relief quicker and easier for investors"

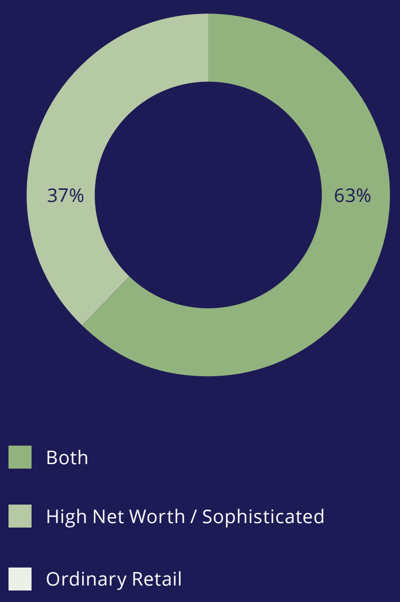
This is the first time we have surveyed EIS providers. Some of the questions asked were similar to those we asked the advisers, so we can make comparisons between the two groups.

WHICH EIS INVESTMENT STRATEGIES DO YOU PROVIDE?



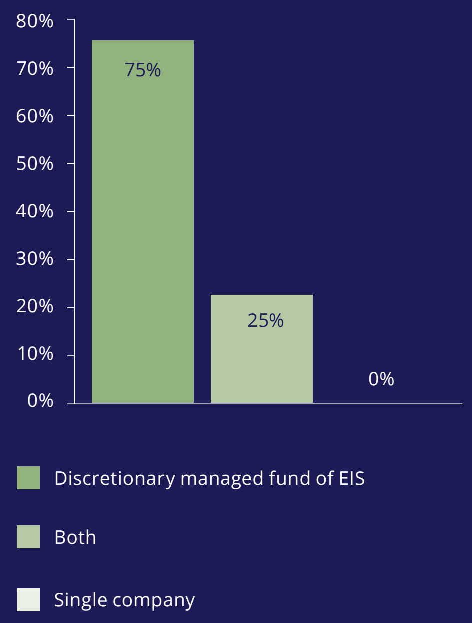
88% of providers have products that target a growth objective and 63% have products targeting capital preservation. 25% have products targeting super growth.

WHAT SEGMENT OF INVESTORS DO YOU FEEL IS SUITABLE FOR EIS?



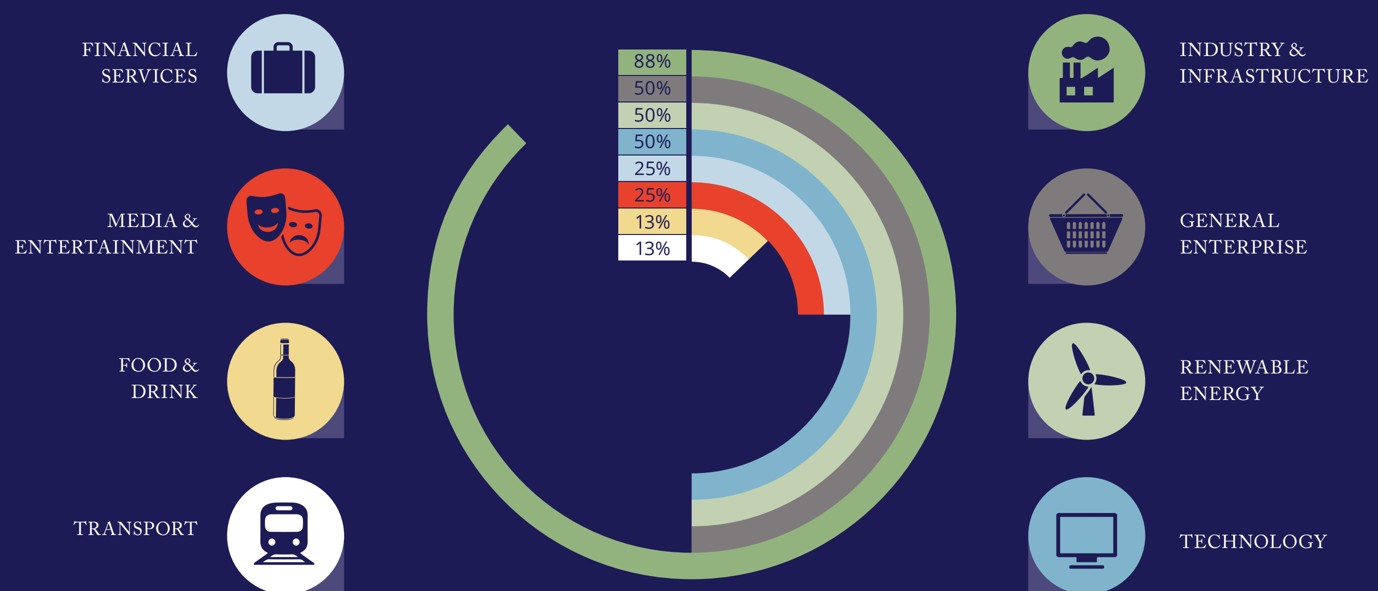
63% of the EIS providers feel EIS can be a suitable investment for both high net worth and ordinary retail investors.

DO YOU PROVIDE:



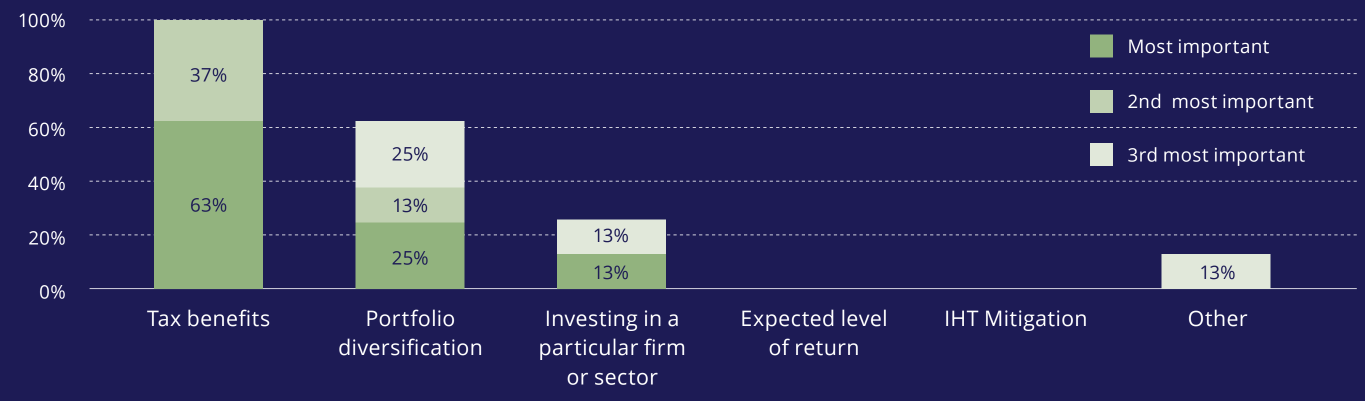
The majority of providers (75%) provide discretionary managed funds and 25% provide both funds and single company opportunities.

WHICH EIS ECONOMIC SECTORS DO YOUR EIS FUNDS MOST COMMONLY TARGET?



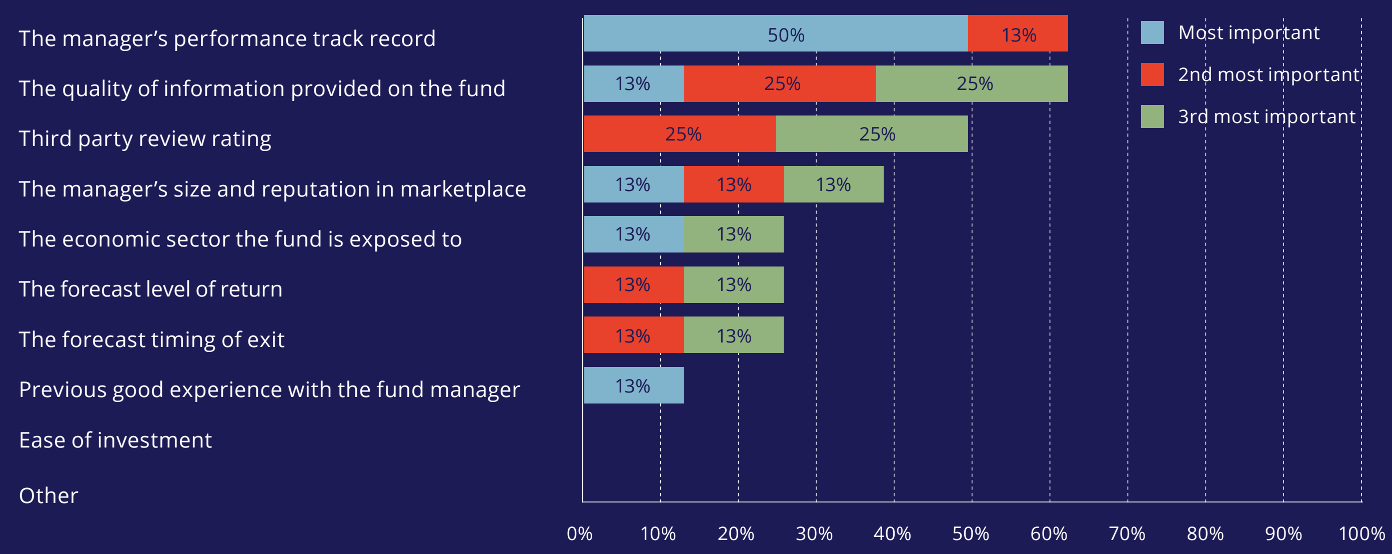
Industry and infrastructure was the most common economic sector for investment. Many providers offer project based opportunities. Other popular sectors are General Enterprise, Renewable Energy and Technology.

WHAT DO YOU BELIEVE ARE THE 3 MOST IMPORTANT FACTORS WHEN CHOOSING AN EIS INVESTMENT?



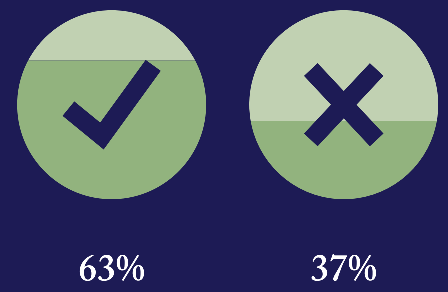
Providers surveyed believe that tax benefits are the number one factor for investors choosing an EIS investment. Portfolio diversification and access to a particular sector were also noted as other important factor by providers. We note that access to a particular sector was not a high priority for advisers.

WHICH 3 FACTORS ARE MOST LIKELY TO MAKE AN INVESTOR/ADVISER HESITATE ABOUT INVESTING IN/ RECOMMENDING EIS?



Track record and quality of information provided are two factors that providers feel are likely to make an investor or an adviser hesitate about investing in an EIS product. This reflects the findings in the adviser survey.

DO YOU FEEL THERE ARE ENOUGH RESOURCES AND INFORMATION AVAILABLE TO ENABLE ADVISERS TO ACHIEVE THE WHOLE OF MARKET KNOWLEDGE OF THE EIS SECTOR?



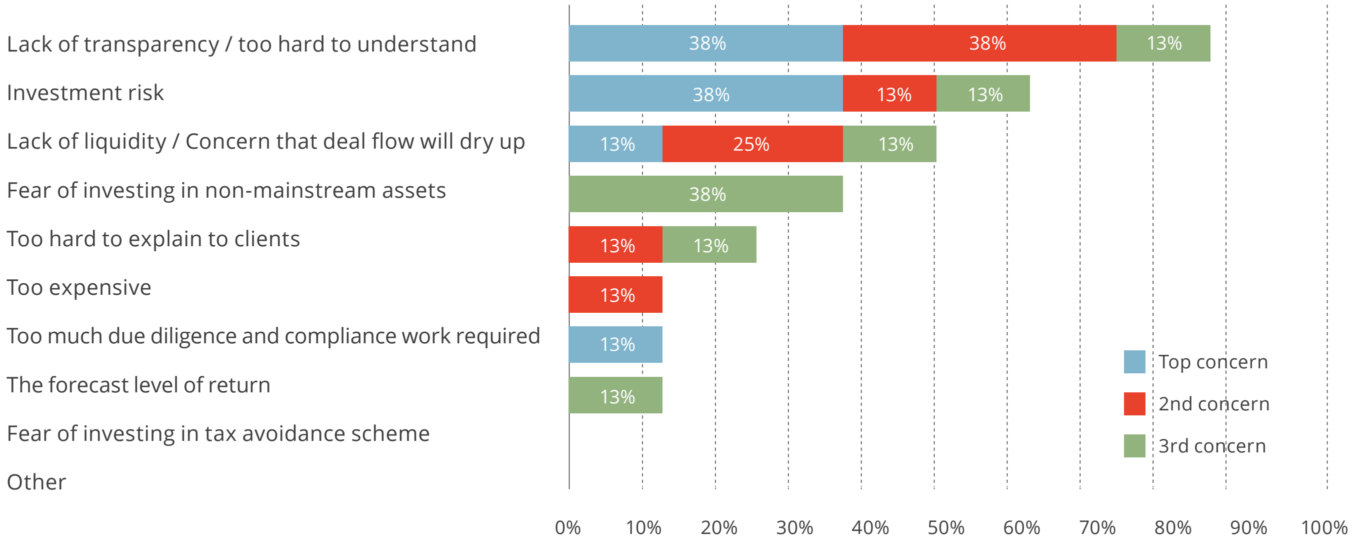
While this question wasn't posed to the adviser community directly, many took the opportunity to say that increased level of transparency and better education in the marketplace would greatly improve the EIS market. However, 63% of providers felt that there are enough resources and information available.

IN YOUR OPINION, WHAT SINGLE CHANGE OR INNOVATION WOULD IMPROVE THE EIS MARKET?

The most requested change was a call on HMRC to make the process for claiming tax relief quicker and easier for investors. Others suggested whole of market education and structured EIS exams.

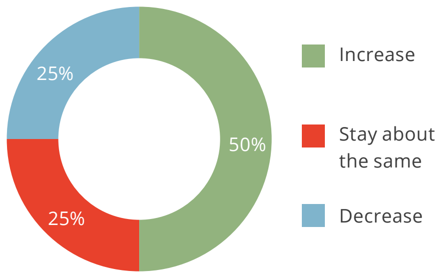
"50% of the providers didn't feel that they would be concerned over deal flow given the new regulations, presumably because their existing strategies already meeting the growth and development test and other new requirements"

WHAT DO YOU BELIEVE ARE THE TOP 3 CONCERNS FOR INVESTORS/ADVISERS WHEN INVESTING/RECOMMENDING EIS?



Providers seem to be spot on again, choosing investment risk and concern over deal flow as some of the most important concerns for advisers and investors. Lack of transparency was also singled out. It is clear that providers do understand what advisers and their clients are concerned about and hopefully they are addressing those concerns. But if they feel lack of transparency is an issue, and yet they also feel that there are enough resources for advisers (see previous question), what is the missing step?

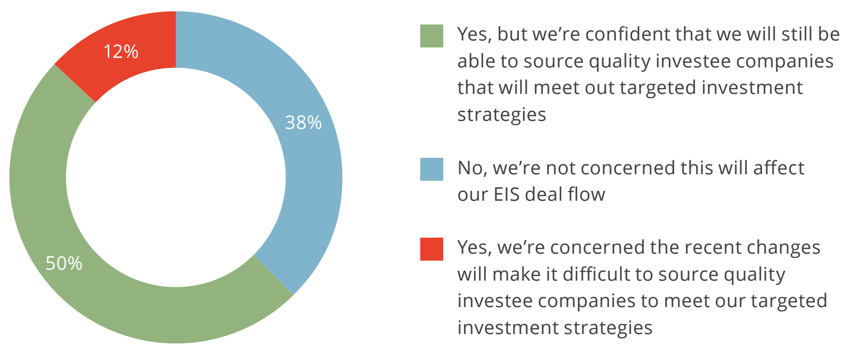
DO YOU EXPECT TO SEE AN INCREASE OR DECREASE IN EIS BUSINESS IN THE NEXT 12 MONTHS?



There is a split feeling in the market over how they view the next 12 months. For those that stated that they expected an increase in business over the next 12 months, pension changes and the growing appetite among advisers to consider EIS as part of a tax planning strategy were cited as reasons why they expected to see an increase.

Those that expected to see a decrease in business felt the new regulations will deter investors from EIS, as opportunities will be higher risk than previously.

DO THE RECENT CHANGES TO VENTURE CAPITAL SCHEME QUALIFYING COMPANY CRITERIA MAKE YOU CONCERNED TO SOURCE EIS DEAL FLOW GOING FORWARD?



50% of the providers didn't feel that they would be concerned over deal flow given the new regulations, presumably because their existing strategies are already meeting the growth and development test and other new requirements. Another 38% of providers were somewhat concerned over the new qualifying criteria going forward, but they were confident they would still be able to source quality investee companies to meet their targeted investment strategies. Only 12% felt that these new rules would make it difficult to deliver their targeted investment strategies.

CONCLUSIONS

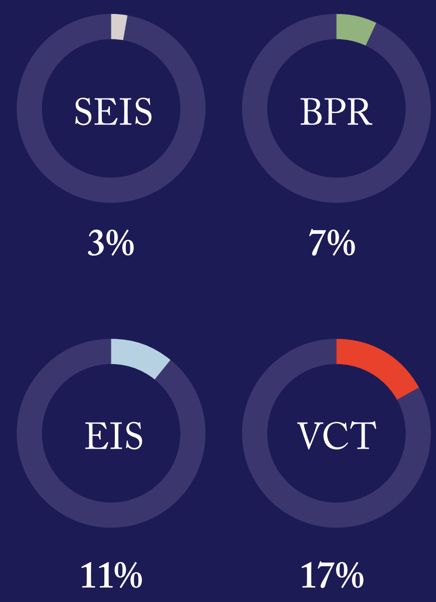
It is clear that the providers are listening to their clients and advisers, and appreciate what their concerns and needs are. It also appears that the new regulations and ensuring they continue to be able to meet their targeted investment strategies are not a major worry for the majority of providers.

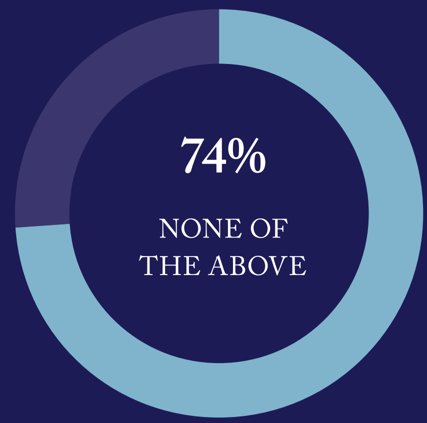
INVESTOR SURVEY

The following survey was carried out on High Net Worth and sophisticated investors, over six days in April 2015. The survey covered all the various tax-efficient investment schemes (EIS, SEIS, BPR and VCTs). The survey was conducted by a third party survey panel of investors and overall we had 92 responses.

While this survey was conducted prior to the 2015 Budget announcements, we expect that their reasons for investing or not investing given at the time would be similar today.

DO YOU CURRENTLY INVEST IN ONE OF THE FOLLOWING TAX-EFFICIENT INVESTMENT?

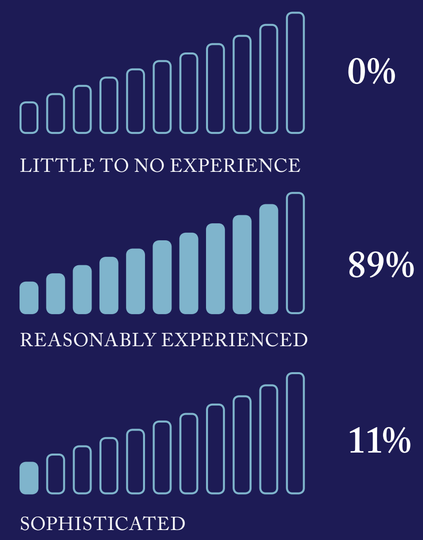




The majority (74%) of our survey respondents do not currently invest in the various tax efficient investment schemes. However, VCTs were the most commonly invested in (17%), with EIS the second (11%), BPR 7% and SEIS 3%.

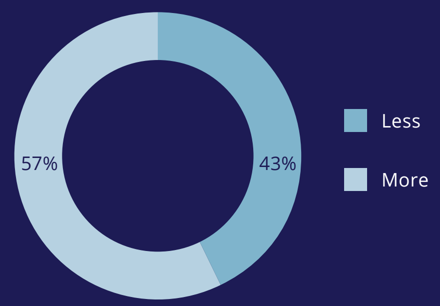
The next few questions will focus on those investing in EIS.

HOW WOULD YOU DESCRIBE YOUR LEVEL OF INVESTMENT EXPERIENCE?



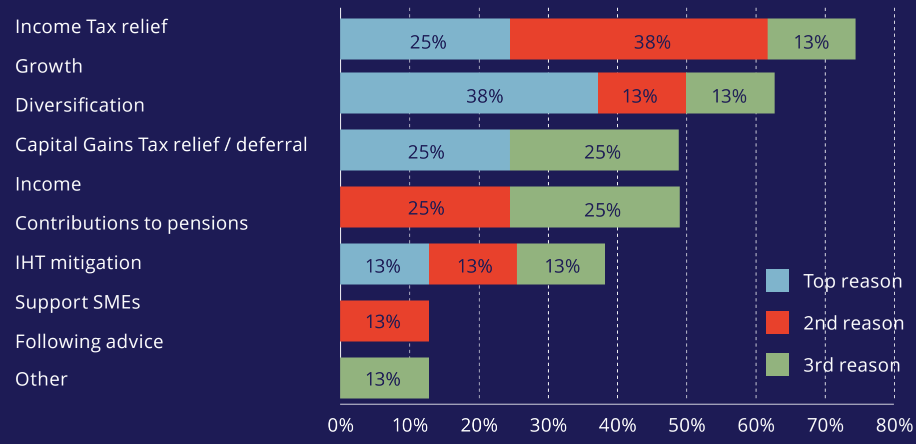
EIS is very close to angel investing, and it takes knowledge and experience to fully understand the investments being made. None of the investors surveyed that are currently investing in EIS would describe themselves as having little or no experience.

DO YOU EXPECT TO INVEST MORE OR LESS IN TAX-EFFICIENT INVESTMENTS OVER THE NEXT FIVE YEARS?



The majority of investors (57%) stated they expected to make more tax-efficient investments over the next five years. This matches with the trends we've seen in the HMRC data and the advisers' and providers' surveys. These are all positive signs that EIS and other tax-efficient investment sectors will continue to experience investment growth in the future.

WHAT ARE YOUR TOP 3 REASONS FOR INVESTING IN TAX-EFFICIENT INVESTMENTS?



The always-obvious answer here is the tax relief, but there are other important reasons to invest that are worth considering. EIS investors noted diversification, growth, and CGT relief as their top reasons for investing in tax-efficient investments.

"Investment risk, fear of a tax avoidance scheme and lack of transparency are all top concerns for EIS investors when choosing a tax-efficient product. Perhaps advisers should be sure to talk through all these things with their clients when choosing a product"

DO YOU HAVE A FINANCIAL ADVISER?

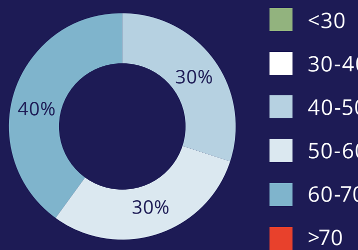
60% of our EIS investors surveyed do have a financial adviser. Crowdfunding technology, discussed earlier, has opened up EIS to smaller self-investment and many investors choose to go without a financial adviser when making decisions on crowdfunding platforms.

IN YOUR OPINION, WHAT SINGLE CHANGE OR INNOVATION WOULD HELP TO ENCOURAGE INVESTMENT IN TAX-EFFICIENT INVESTMENTS SUCH AS EIS, SEIS, VCTS AND BPR?

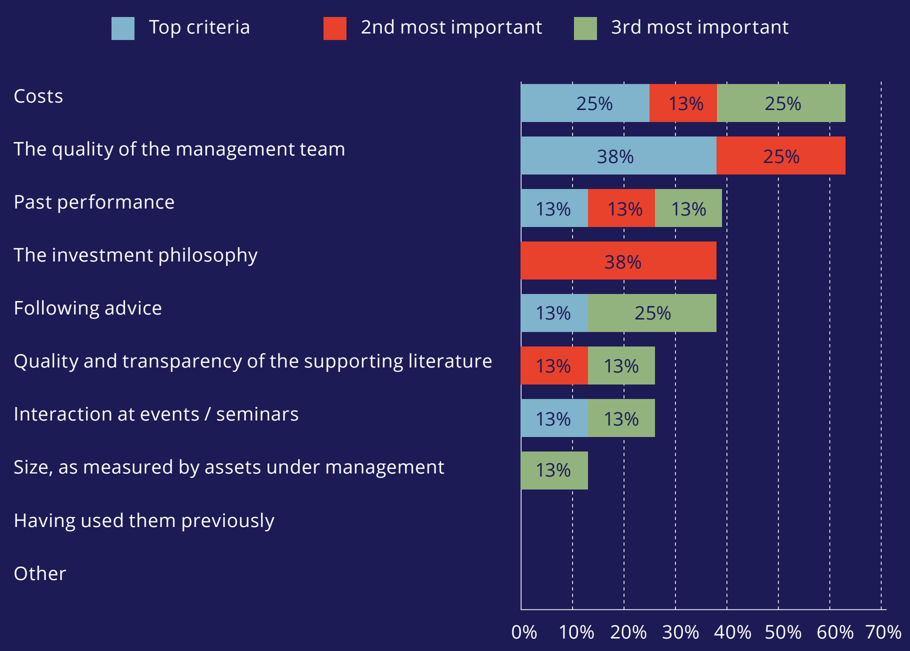
When posed this question, EIS investors stated greater transparency and using plain language rather than financial jargon would improve their experience of the tax-efficient investment universe. Greater tax reliefs and more certainty of the regulatory climate were also noted.

WHAT'S YOUR AGE?

Perhaps unsurprisingly, the survey shows that EIS investors are typically around 40 to 70 years old.

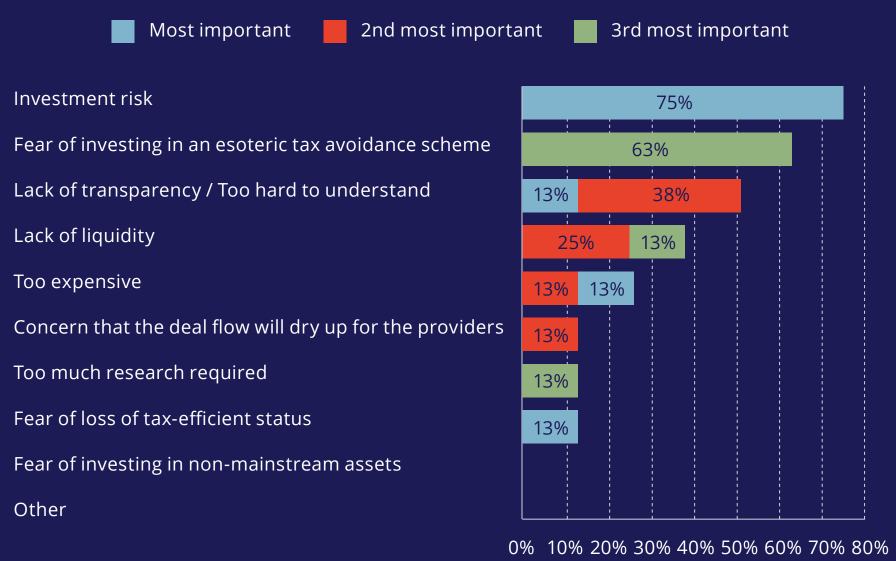


WHAT ARE YOUR TOP 3 CRITERIA WHEN CHOOSING A TAX-EFFICIENT INVESTMENT PRODUCT PROVIDER?



When looking at a provider, the costs, management team, past performance and investment philosophy were among the most important factors for investors.

WHAT ARE YOUR TOP 3 CONCERNS WHEN CHOOSING A TAX-EFFICIENT INVESTMENT PRODUCT?

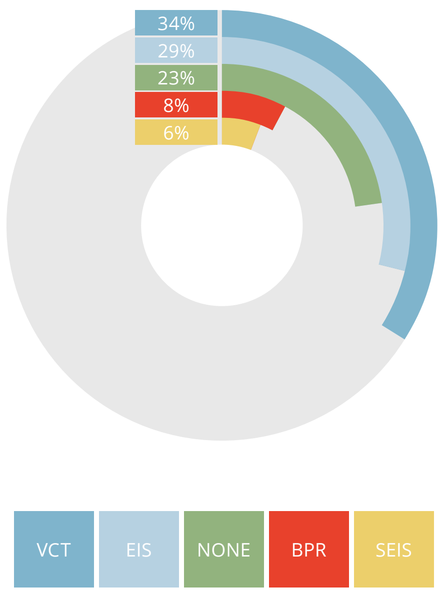


Investment risk, fear of a tax avoidance scheme and lack of transparency are all top concerns for EIS investors when choosing a tax-efficient product. Perhaps advisers should be sure to talk through all these things with their clients when choosing a product. Certainly the statutory nature of the scheme should be emphasised: there is no need for consumers to be concerned that they are investing in some sort of illegal tax evasion when considering EIS.

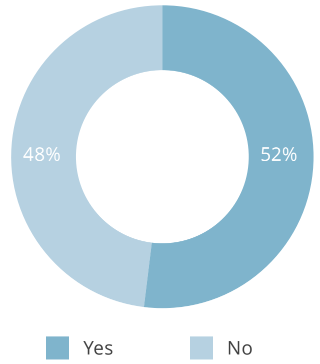
"Investors are calling for the same things – transparency and clarity – that advisers want"

The following questions focus on those investors that are not currently invested in tax-efficient investments.

ARE YOU AWARE OF TAX-EFFICIENT INVESTMENT PRODUCTS?



DO YOU ANTICIPATE THAT YOU WILL INVEST IN TAX-EFFICIENT PRODUCTS IN THE FUTURE?

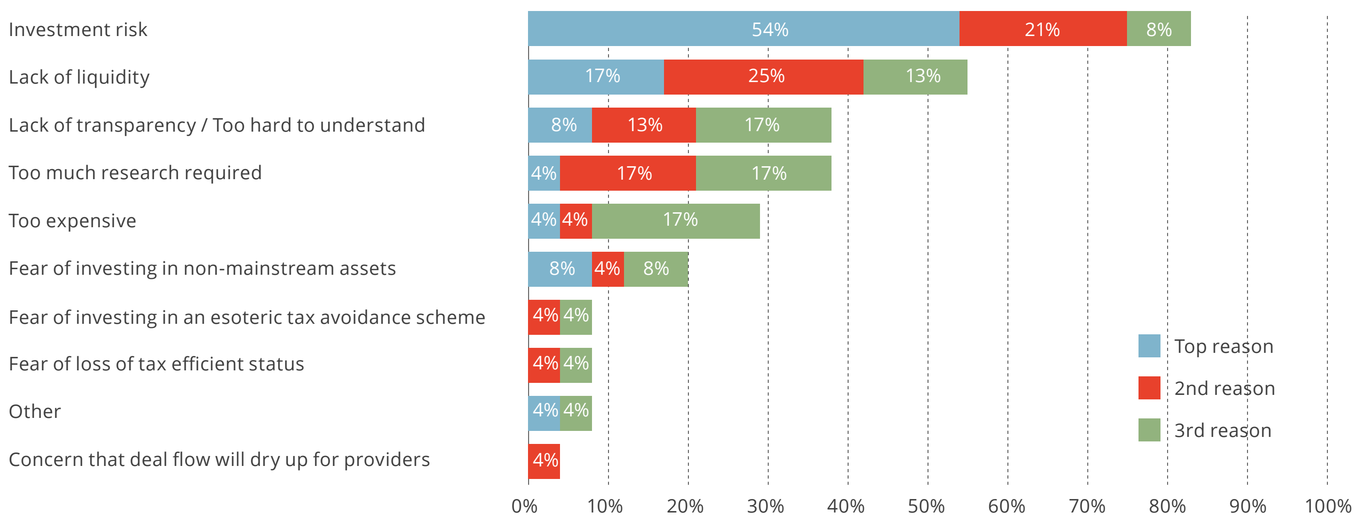


While the majority do not currently invest in any tax-efficient products, the majority (52%) of those who are aware of EIS do anticipate investing in a tax-efficient investment product in the future. We can conclude that this is a signal of future growth in this area.

IN YOUR OPINION, WHAT SINGLE CHANGE OR INNOVATION WOULD HELP TO ENCOURAGE INVESTMENT IN TAX-EFFICIENT INVESTMENTS SUCH AS EIS, SEIS, VCTS AND BPR?

There were the typical calls for even greater tax reliefs, but one notable answer was the ability to source all open products in one place to make for easier comparison. We have definitely seen some innovations and improvements in this space (you can find a list of some of the EIS market's innovations on page 27).

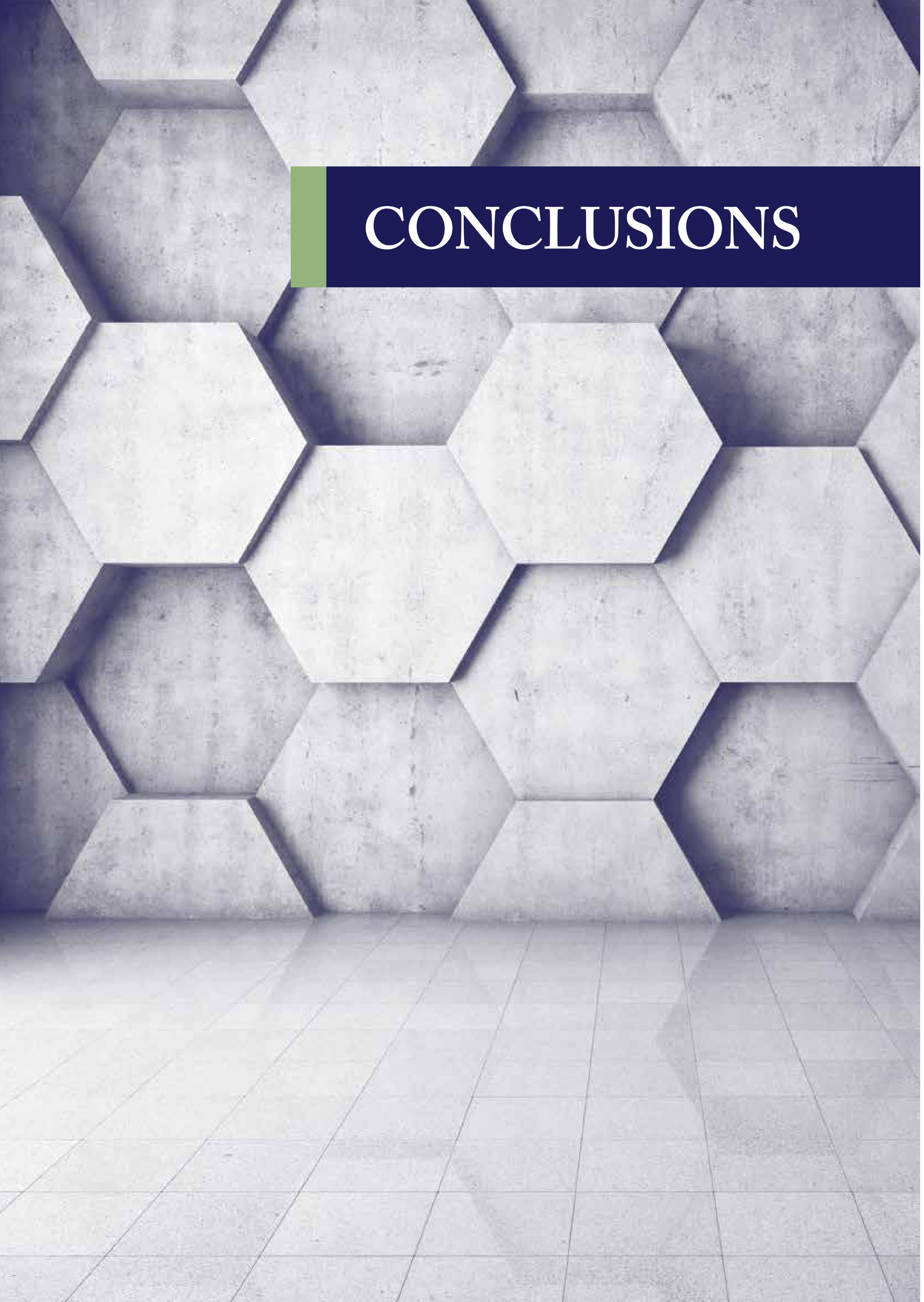
WHAT ARE YOUR TOP 3 REASONS FOR NOT INVESTING IN TAX-EFFICIENT INVESTMENT PRODUCTS?



Investment risk is by far one of the major factors holding investors back from getting involved in this space. This is not something that can really be addressed by the providers or advisers, as EIS investments are by their very nature higher risk than most mainstream options.

CONCLUSIONS

Investors have picked up on the benefits of EIS and the other tax-efficient products and are definitely aware of the important points to be cognisant of when considering one of these investments. They are calling for the same things - transparency and clarity - that advisers want. Advisers and providers need to have a role in improving this for investors by providing information free of any industry jargon.



FINAL CONCLUSIONS

The EIS market has continued to grow, with new products and providers entering the market, and new service providers for IFAs and investors. We think that this growth is being driven by lower pension limits, greater awareness of the scheme and more advisers using tax advantaged investments to implement sophisticated planning strategies. The work that the biggest providers, the EISA and their membership are doing to reach out to advisers seems to be paying off.

However, the biggest driver of growth in new investment over the last few years has now been switched off: subsidised renewable energy investments no longer qualify for the EIS. In November 2015 this was extended to 'peak power' projects, which share similar investment characteristics in as much as they are cheap to install and maintain and have contracted revenues (ironically, they do not share the same green credentials as renewables as they usually burn fossil fuels). This must represent a speed bump for the industry, but we think it is probably no more than that. The other drivers for new investment, such as pension changes and more sophisticated planning mentioned above will kick in, and it may turn out that many of the advisers and investors who were introduced to EIS investments by the mini-boom in renewables will continue to invest in EIS. Certainly, as they begin to exit those investments they may well feel comfortable leaving that money in the EIS sector, and recycling it for further income tax relief (and to maintain the IHT exemption).

Other changes to the legislation governing the EIS scheme have been made to ensure ongoing compliance with EU State Aid. The changes are not ideal and will signal the end of some capital preservation based business models (such as acquiring and renovating pubs) and will make investing in mid-sized companies harder than investing in early stage companies. This is a meaningful change for the industry, but nothing more than that. The EIS has always had a focus on early stage companies and, while there may be a period of adjustment and new administrative burdens for the EIS managers, the industry is more than able to adapt. However, for advisers assessing EIS investments and looking at performance track record, a track record based on investing in renewable energy or a strategy of acquiring businesses is less relevant now.

There is still a dearth of exits (not in the planned exit products, but the growth funds), and the industry will need to demonstrate more successful exits to continue to build confidence in the product and attract those advisers and investors who have been observing from the sidelines and waiting to see more evidence that EIS works as a pure investment and not just as a tax planning exercise.

As more advisers and investors start to consider EIS, platform based solutions and research and due diligence tools such those provided by Kuber Ventures, Mercia Fund Management, Lawson Conner, Seed EIS Platform and MICAP are now viable propositions. They aim to make advisers' lives easier by simplifying and speeding up the advisers' business process. If they are successful, they will become another driver of growth in EIS investment.

We've briefly touched on SEIS, SITR and Crowdfunding in the report. These are all exciting developments in the sector. SEIS has the most generous reliefs, but the small limits on the amounts that can be invested make it hard to cover the fixed costs of sourcing and putting together the deal flow required for a fund. However, in 2016 we should see the first exits from SEIS and we'll be able to start to evidence how the scheme is working. We know anecdotally that successful SEIS businesses can secure subsequent EIS funding, and this would appear to be a route up the 'funding escalator' that managers will be able to construct for investees.

SITR (Social Investment Tax Relief) looks very appealing and we can see how this could provide interesting and engaging investments for clients along with appealing tax reliefs. Crowdfunding has democratised access to the EIS reliefs and we think that as long as the investments are small and made with realistic (i.e. low) expectations this is a good thing. It remains a peripheral issue for the EIS industry at the moment though. An innovation like the CoInvestor platform is perhaps a more realistic way for online retail investors to get involved in building their own portfolio without sacrificing some of the advantages of having a fund manager on your side.

Against this background, we think that fundraising will continue to grow over the next few years and the industry will continue to rise in prominence. As investors successfully exit investments and recycle the money into new opportunities and a further round of reliefs, confidence will rise and more people will be persuaded of the benefits.

"EIS celebrated its 21st birthday in 2015, the latest figures from HMRC show EIS are an established asset class and a critical source of funding for many UK smaller companies. Over the years, investment has been targeted at companies and sectors most in need of finance, including renewable technologies. EIS fundraising is going from strength to strength, with the total amount raised in 2014 up a significant 48% on the previous year" **John Thorpe, Octopus Investments**

POLICY CHANGES TIMELINE

1997-98
From 17 March 1998, farming, market gardening, property management, hotels, guesthouses and care and nursing homes became 'excluded activities'.

1998-99
From 6 April 1998, Capital Gains Tax deferral relief was extended to include shares that did not qualify for Income Tax relief. Previously, deferral relief was only available in respect of such shares. In addition, a company's gross assets limit of £15m before investment and £16m after investment was introduced. Prior to this there was no limit on company size, but a company could only raise up to £1m per tax year through EIS (though certain qualifying shipping activities could raise up to £5m). Also, the maximum amount of investment on which Income Tax relief could be obtained was increased from £100,000 to £150,000.

Capital Gains Tax exemption was introduced from 1 Jan 1999.

2000-01
The period for which shares must be held to retain Income Tax relief was reduced from five years to three.

2001-02
The requirement that all money be employed in qualifying activities within 12 months was changed to 80% (with the remaining 20% to be employed within the next 12 months).

2004-05
The maximum amount of investment on which Income Tax relief could be obtained increased from £150,000 to £200,000.

2006-07
Gross assets limit was reduced to £7m before investment and £8m after investment. Maximum amount of investment on which Income Tax relief could be obtained increased from £200,000 to £400,000.

2012-13
From 6 April 2012, EIS was extended to companies with fewer than 250 full time equivalent employees and gross assets of no more than £15m before investment and £16m after investment. The annual investment limit for companies increased to £5 million; that sum must take account of VCT and SEIS investment, and any other investment received via any measure covered by the European Commission's Guidelines on State Aid to promote Risk Capital Investment in Small and Medium-sized Enterprises. For shares issued on or after 6 April 2012, a company using the funds to acquire shares in another company will not be regarded as using them for a qualifying purpose. The annual investment limit for an individual was increased to £1m, and the £500 minimum investment requirement was removed. Most trades attracting Feed-In Tariffs or overseas equivalents were excluded.

2011-12
The requirement that the trade be carried on wholly or mainly in the UK was removed, and replaced with a requirement that the issuing company have a permanent establishment in the UK. Companies whom it would be reasonable to regard as "enterprises in difficulty" as defined by the European Commission, were excluded. The EIS rate of relief was increased to 30%.

2009-10
The time within which monies raised by the share issue must be employed was extended from 80% within 12 months and the remainder within a further 12 months, to 100% within 2 years.

2008-09
The maximum amount of investment on which Income Tax relief could be obtained increased from £400,000 to £500,000.

2007-08
From 19 July 2007, companies must have raised no more than £2 million under any or all of the tax-based venture capital schemes (Venture Capital Trusts, Enterprise Investment Scheme and, available at the time, Corporate Venturing Scheme).

GLOSSARY

Annual Management Fee (AMC)	The annual fee that the fund company charges to cover the costs of managing the fund.
Business Property Relief (BPR)	Business Property Relief or Business Relief Scheme. Qualifying assets are removed from the estate of the deceased for Inheritance Tax purposes.
Capital Gains Tax (CGT)	This is a tax on the gain or profit made when selling or giving away an asset. It applies to assets that you own, such as shares or property. The individual CGT allowance for 2015/16 is £11,100.
European State Aid	Defined as an advantage of any type conferred by public authorities through state resources to any organisation that could potentially distort competition in the European Union.
Financial Conduct Authority (FCA)	Replaced the FSA on 1st April 2013 and took over the regulation of the financial services industry in the UK. Aim to protect customers, promote competition and enforce standards.
Enterprise Investment Scheme Association (EISA)	The EIS Association is an independent, not-for-profit organisation, which exists to assist in the flow of capital and resource available to British small to medium-sized enterprises through the Enterprise Investment Scheme.
Enterprise Investment Scheme (EIS)	Government supported initiative designed to help smaller higher-risk trading companies raise finance by offering a range of tax reliefs to investors who purchase new shares in those companies.
Feed-in-Tariff (FiT)	FITs are payments energy suppliers pay if you generate electricity of your own.
HM Revenue and Customs (HMRC)	They are the UK's tax authority, responsible for making sure that money is available to fund the UK's public services and for helping families and individuals with financial support. Responsible for Income Tax, Corporation Tax, Capital Gains Tax, Inheritance Tax, Stamp, Land and Petroleum Taxes among others.
Inheritance Tax (IHT)	This is a tax due on the value of your estate at death, including any assets held in trust and gifts made within 7 years of death. The IHT threshold for 2015/16 is £325,000, is frozen until 2019. Tax is payable at 40% on any amount above this nil rate threshold.
Investment Memorandum (IM)	Offering Memorandum (OM) or Private Placement Memorandum (PPM). A legal document stating the objectives, risks and terms of a private investment. It should provide buyers with information on the offering and protect sellers from the liability associated with selling unregistered securities.
Renewable Obligation Certificate (ROC)	This is the main mechanism to support renewable electricity projects in the UK. ROCs are "green" certificates issued to accredited operators of renewable energy stations - used by suppliers to demonstrate they have met their obligations. Companies have the obligation of presenting a number of ROCs or otherwise pay an equivalent amount into a buy-out fund.
Seed EIS (SEIS)	Aims to help small, early-stage companies raise finance by offering tax reliefs to individual investors who purchase new shares in those companies. It complements the EIS and focuses on very early stage companies, offering tax relief at a higher rate than the EIS.
Small and Medium-sized Enterprises (SEM)	Businesses with fewer than 250 employees and less than £15 million in net assets.
Venture Capital Trusts (VCT)	Scheme started on 6 April 1995 and is designed to encourage individuals to invest indirectly in small higher-risk trading companies whose shares are not listed on a recognised stock exchange. VCTs are traded on a regulated market and tax reliefs are available to individuals who invest.

CPD AND FEEDBACK

CONTINUING PROFESSIONAL DEVELOPMENT (CPD)

Intelligent Partnership has achieved accredited status for AiR from the CISI, CII and PFS.

Members of these professional organisations represent the majority of the insurance, investment and financial services industry.

Readers of the industry report can claim one CPD hour towards their CISI, CII or PFS member CPD scheme for each hour spent on the report, the CPD hours claimed should reflect the length of time spent studying the material.

The review process included an assessment of the technical accuracy and quality of the material against CPD Accreditation standards. Achieving the recognised industry standard afforded by these organisations for this report, and our training, demonstrates our commitment to delivering only balanced, informative and high quality content to the financial services and investment community.

In order to obtain CPD and meet accreditation standards, readers must complete a short questionnaire and provide feedback on the report. This includes twelve multiple choice questions to demonstrate learning and a feedback form to assist in the compilation and improvement of future reports.

To claim CPD please visit:

Intelligent-partnership.com/cpd

FEEDBACK

Intelligent Partnership actively welcomes feedback, thoughts and comments to help shape the development of this industry report, with a particular interest in the topics readers would like to be covered in more detail in interim and future annual reports.

This report is produced on an annual basis and is compiled through the conducting of research and surveys with providers, promoters and practitioners within the alternative investment industry. Greater participation, transparency and fuller disclosure from industry participants should help foster best practice and drive out poor practice.

Feedback can be given on the website or via email:

Intelligent-partnership.com/feedback

Reports@intelligent-partnership.com

Participation and feedback are gratefully received.

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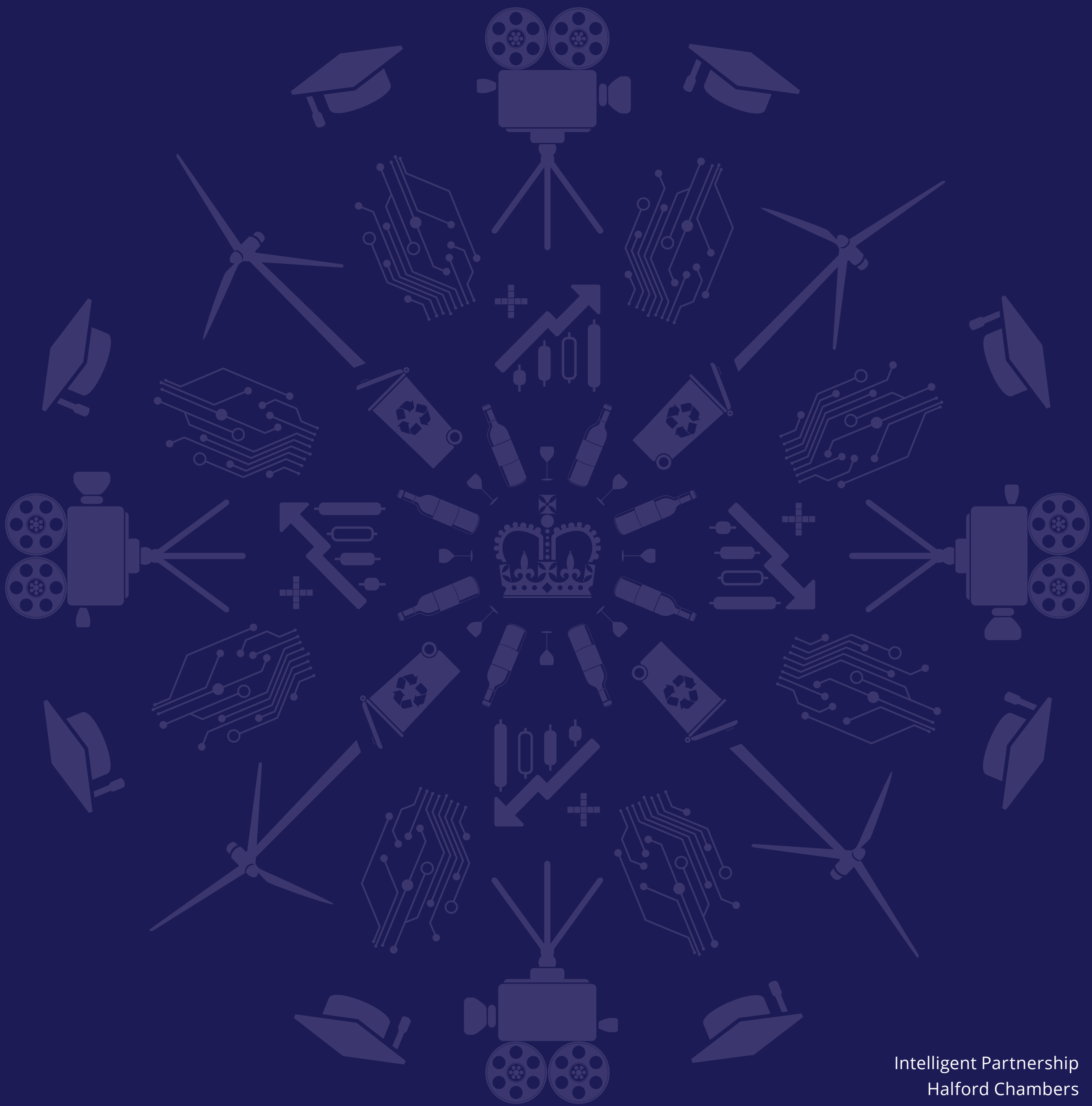
"The EIS market has continued to grow, with new products, providers and services entering the market. This growth is being driven by lower pension limits, greater awareness of the scheme and more advisers using tax advantaged investments to implement sophisticated planning strategies"



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