Social Investment Tax Relief Explained

SITR

Social Investment Tax Relief (SITR) was introduced by the UK Government in April 2014 to encourage investment into social enterprises.

The following overview of the rules is as they currently stand, but we expect various changes to the scheme when the government's 2017 Finance Bill comes into force. This is a simplified summary and doesn't go into all the detail.

Background to SITR

SITR is the most recent addition to the existing Venture Capital Schemes (EIS, SEIS and VCT). SITR was introduced in the 2014 Finance Act to encourage new investment by individuals into Social Enterprises. It is designed to help such organisations raise investment to develop or expand their social mission or to help them find new ways of tackling societal or environmental issues.

SITR presents many similarities with EIS, but a noticeable difference between the two schemes is that for SITR the investment can be made in the form of equity or debt. This is key, as many social enterprises are structured without share capital and have no means of issuing equity in exchange for investment.

How does SITR work for investors?

UK-taxpaying individual investors can invest up to £1 million in multiple charities and social enterprises per tax year and benefit from up to 30% income tax relief on the amount invested in the tax year of the investment or, since 2014/15, the previous tax year.

The maximum investment into an individual organisation is approximately £300,000 over a rolling three year period.

Investors may gain income tax relief (as mentioned above) plus certain capital gains and other tax reliefs.

The investor or their 'connected person':

- must not be an employee, director or trustee
- cannot have more than 30% interest in the investee, nor a 51% subsidiary of it.

Equally, the investor:

- cannot claim SITR if that investment has already attracted EIS or SEIS [you cannot get more than one relief for the same investment]
- must hold the investment for at least three years for the relief to be retained.

Qualifying debt or equity interests must:

- be in a community interest company, a registered charity, a non-charity community benefit company, or certain types of special purpose vehicles largely relating to social impact bonds.
- be new securities, and new money invested.
- be invested directly into a social enterprise or through a nominee

but must not:

- have pre-established terms for buyback repayment or release of value within three years from investment,
- enjoy preferential rights to capital on a winding up, interest or dividend when compared to any other class in issue.

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How does SITR work for social enterprises?

Social enterprises can issue unsecured debt finance or equity. The maximum that can be raised by an organisation is approximately £300,000 over three years (technically €344,827 under European state aid rules). The amount of tax relief is further restricted if the investee company has received State Aid in other forms.

Organisations must be less than 7 years old and have fewer than 500 employees and gross assets of no more than £15 million.

SITR cannot support certain excluded activities, including property development or money lending, amongst other things, and money raised cannot be used to pay off existing loans.

The main benefits to a social enterprise receiving SITR qualifying investment are:

- the investment must be unsecured; and
- it is patient capital – there can be no capital repayments for three years, giving time to implement the business plans and start generating income to repay the investment.

Expected changes coming soon:

The second Finance Bill of 2017, delayed by the 2017 general election, includes various changes to SITR which will, from the date on which the Bill actually comes in to force, apply retrospectively from 6th April 2017.

In summary:

- the total investment a social enterprise can raise through SITR during a 3 year period increases to £1.5 million, provided the social enterprise is less than 7 years old

- specific activities will no longer be SITR qualifying, these include trades such as on-lending to other social enterprises and asset leasing

- investments in to nursing homes and residential care homes will be excluded, though the Government may introduce an accreditation system to allow such investments to qualify for SITR

- a financial health requirement will apply to a social enterprise raising funds under SITR which will be that it is “not in difficulty...for the purposes of the Community Guidelines on State Aid for Rescuing and Restructuring Firms in Difficulty (2004/C 244/02)”

- the limitation on the number of full-time equivalent employees of the social enterprise concerned will be reduced to 250 from 500.