



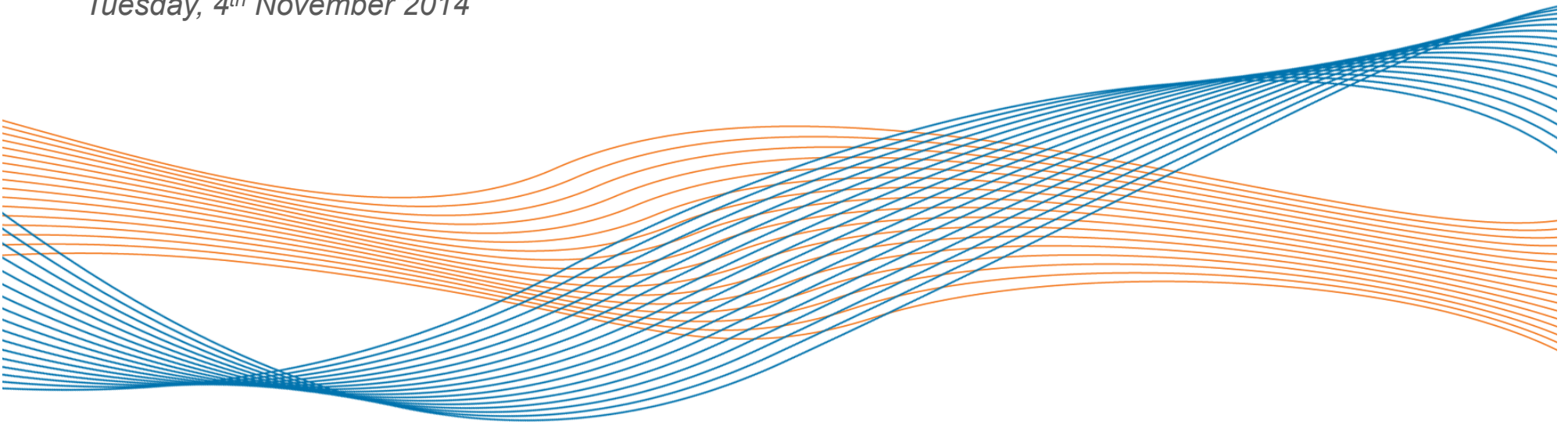
Innovation. Investment. Impact.

E3M: Finance for Social Enterprise Growth Social Investment Tax Relief

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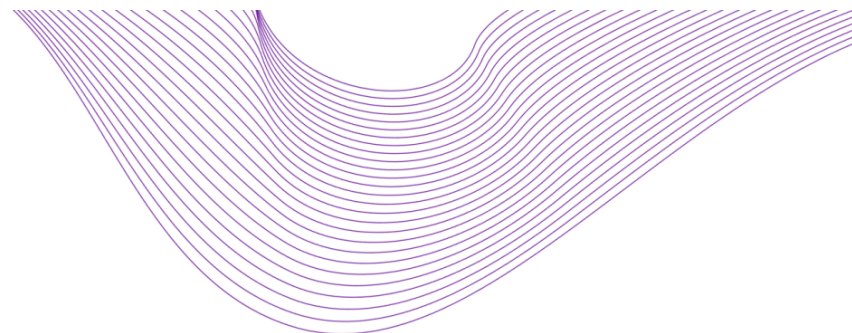
ClearlySo

Tuesday, 4th November 2014



Determining eligibility

A direct investment needs to satisfy eight tests



| | | |
|------------|--------------|---|
| Investee | Test | The investee organisation is eligible if it: |
| | Legal Status | Is a registered charity, Community Benefit Society or CIC; AND |
| | Size | Has less than 500 FTE equivalent AND Less than £15m assets AND |
| | Activities | Not undertake excluded activities, being: electricity generation, property development solely or primarily to make capital gains, personal lending (20% threshold for certain activities) |
| Investment | Test | The investment is eligible if: |
| | Type | It is either of: <ul style="list-style-type: none">- Shares OR- Debt that is:<ul style="list-style-type: none">o Not secured by any assets ANDo Does not repay the principal in first 3 years ANDo Is not preferred to any other investment instruments on wind-up AND |
| | Size | The tax relieved amount is no more than £290,000 (approximate calculation) AND |
| | Other relief | It has not received tax relief already (through EIS or VCT) on the same |
| Investor | Test | The investor is eligible if: |
| | Investor | It is an individual paying tax in the UK AND |
| | Structure | The investor invests either: <ul style="list-style-type: none">- Directly OR- Through a nominee fund |

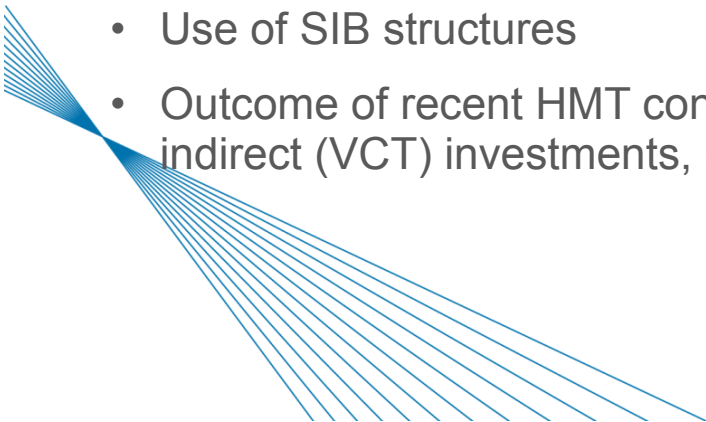
A slow start – but encouraging progress

Early obstacles included

- Limited state aid allowance for investee organisation due to ICRF and other grants
- Interpretation of what constitutes an excluded activity e.g. property development
- Limit on 500 FTEs excludes many 'people businesses' in the social sector e.g. domiciliary care
- Lack of clarity over HMRC interpretation

However, advance assurance processes starting to give greater clarity over eligible transactions

- Advance assurance proposals working through HMRC following Royal Assent
- Standard form of investment documentation emerging
- Use of SIB structures
- Outcome of recent HMT consultation on scheme might help further (broader SIB definition, indirect (VCT) investments, expanding scheme)



Case study – Structuring a SITR deal

Background

ClearlySo raised £1.25m debt into a leading social enterprise from leading social impact funds earlier this year to fund expansion via new sites.

Several HNWLs were keen to explore an investment in the investee alongside the impact funds.

Eligibility analysis

The social enterprise and the deal was thought likely to satisfy the criteria.

Illustrative economics

£100k unsecured loan @ 5.00%, 5 year bullet term = £25k total interest

Total return to investor (including 30% SITR) = £55k

Annualised undiscounted returns = 9.16%

Challenges

Pre-dated Royal Assent and advance assurance process

HNWLs investing through trusts already benefit from tax relief

Cannot hold more than 30% of capital / take paid board positions

Counter-intuitive to take a lower return as junior lenders despite tax relief

| | | |
|----------------|--|---|
| The Investee | 1. Legal status = Charity | ✓ |
| | 2. 400 employees and circa £4m assets | ✓ |
| | 3. No excluded activities | ✓ |
| The Investment | 4. Unsecured subordinated debt + Principle repaid after 5.25 years and No preference in wind-up | ✓ |
| | 5. Tax relief < £290,000 Circa £90k State-Aid received (£200k - £115k) / (28% + 30%) = £122k available for relief | ✓ |
| The Investors | 6. No relief received on same investment | ✓ |
| | 7. Individual paying tax in UK | ✓ |
| | 8. Investing directly | ✓ |