Deferring capital gains from a sale of shares by investing via an EIS portfolio

Throughout life there are various actions that can trigger a capital gains tax (CGT) event. The most common events are triggered when selling valuable assets such as property, shares, or business interests.

In this scenario, we explore how Enterprise Investment Schemes (EIS) can offer various tax relief benefits including the deferral of a CGT liability.

Benefits of tax-efficient investments are subject to change and personal circumstances.

Don't invest unless you're prepared to lose all the money you invest. This is a high-risk investment and you are unlikely to be protected if something goes wrong.

Take 2 minutes to learn more on page 4

Meet the client

David is a 57 year old client who recently sold shares in a company he invested in 20 years ago. When David sold the shares, the profit he made after his annual CGT allowance was £30,000, causing a potential CGT liability of £7,200. David contacts his financial adviser to find out what options might be available to him to help him manage this tax bill.

Guidance given by the adviser:

David's adviser starts by talking to him about his ability to absorb any losses if an investment was to fall in value. David's adviser explains that by investing into an EIS, you are effectively able to transfer the CGT liability to the EIS portfolio, provided the investment occurs within 3 years of the CGT liability occurring. This is called CGT Deferral Relief. Not only this, but EIS portfolios can offer other tax relief benefits.

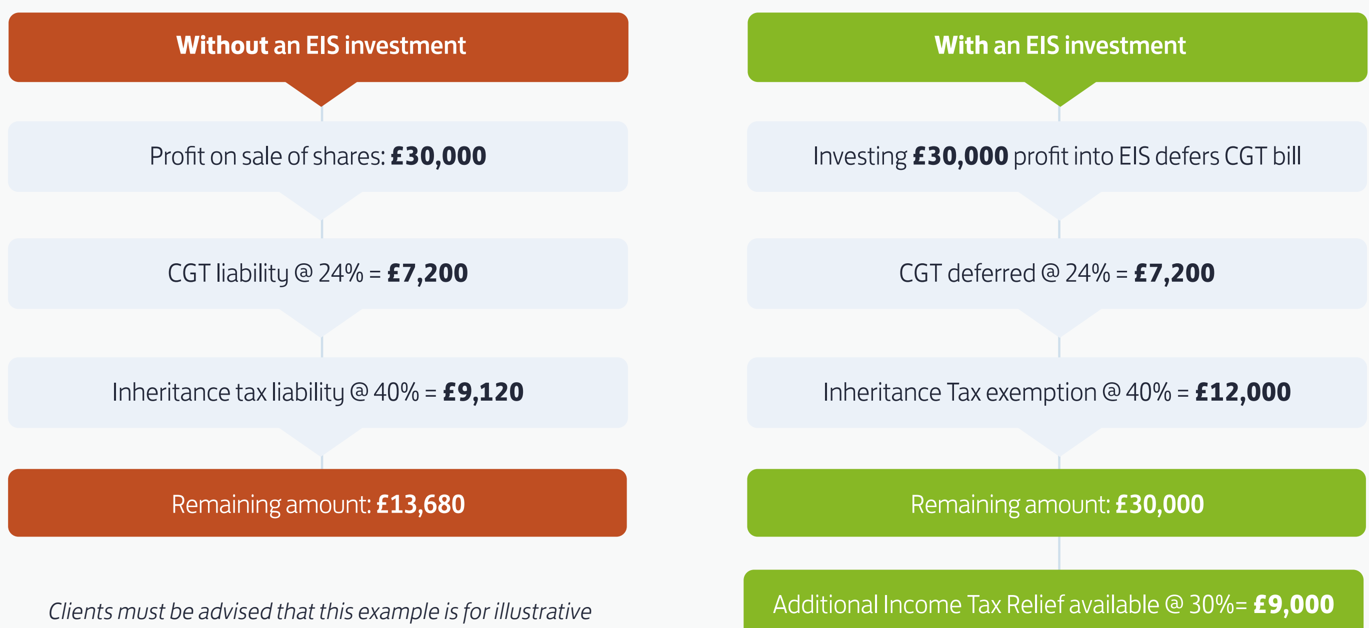
Whilst not guaranteed, David's EIS investment would aim to be invested across 10 different companies which are likely to be sold in different years. Only when the EIS qualifying companies in his EIS portfolio were sold, would the CGT bill become payable again. This means that each tax year, David can use his annual CGT allowance against the deferred gains from the shares sold.
Potentially, if in the year that the EIS company is sold David is a basic rate tax payer, it would result in a lower rate of CGT being applied to the deferred gain.

In the event that multiple companies exit in the same year, and the deferred gain at that point exceeds his CGT tax-free allowance, David could reinvest some of the proceeds of the sales into another EIS-qualifying investment. This would further defer the gain, a process that can be repeated until there was no CGT bill left.
If David were to die whilst still owning the EIS investment, any deferred CGT would die with him.

David's adviser also explains that all growth in his EIS investment would be completely tax free, subject to holding his EIS shares for at least three years and if Income Tax relief has been claimed. Up to 30% Income Tax Relief can be claimed.

The investment would also qualify for up to 100% Inheritance Tax (IHT) relief after it had been held for two years and provided it was still held at the time of his death. Please note, rules relating to Business Relief are changing. Please see our Guide to Business Relief for more information.

Let's take a look at how David's portfolio could change, using two different investment strategies. Both examples assume the client has exhausted all other applicable reliefs and that an income tax bill of at least £9,000 has been paid in this or last year. For the purposes of IHT it assumes the client does not have other investments that would take their total Business Relief qualifying investments over £1m.



Clients must be advised that this example is for illustrative purposes only and ignores initial and annual charges. Please refer to our product literature for further details.

Background

Since its introduction almost 30 years ago, the EIS has become a valuable tax-planning tool. The UK Government launched it in 1994 to encourage investment in start-ups and early stage companies.

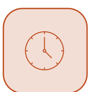
Tax Reliefs

The EIS offers a range of valuable tax reliefs to encourage investment and reduce the risks involved. Investors must have a sufficient income tax liability to benefit from the tax reliefs available.

Supporting the UK Economy

Investing in EIS-qualifying businesses positively contributes to the UK's economic growth, enhances innovation reputation, actively supports entrepreneurial ventures, fostering job creation and economic productivity.

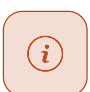
EIS Tax Benefits



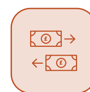
Up to 30% Income Tax relief
in the current or previous tax year, providing investments are held for a minimum of three years.

Up to 100% (IHT) Exemption
on qualifying investments in as little as two years (and if held at time of death).

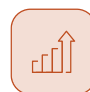
CGT deferral relief
The EIS shares you subscribe for must be issued to you in the period beginning one year before, and ending three years after, the date of the disposal for which you wish to claim relief.



New Business Relief rates will apply from April 2026. Please refer to the Guide to Business Relief for further information.



Offsetting of capital losses up to 45%
Dependent on marginal rate of Income Tax at time of loss. Capital losses of one portfolio company can be claimed irrespective of the performance of other companies in the portfolio.



Growth free of CGT
if Income Tax relief has been claimed.

Carry back to previous tax year
(for Income Tax relief).

Risks

Due to the potential for losses, the Financial Conduct Authority (FCA) considers this investment to be high risk.

What are the FCA key risks?

1 - You could lose all the money you invest
If the business you invest in fails, you are likely to lose 100% of the money you invested. Most start-up businesses fail.

2 - You are unlikely to be protected if something goes wrong
Protection from the Financial Services Compensation Scheme (FSCS), in relation to claims against failed regulated firms, does not cover poor investment performance. Try the FSCS investment protection checker. (https://www.fscs.org.uk/check/investment-protection-checker)

Protection from the Financial Ombudsman Service (FOS) does not cover poor investment performance. If you have a complaint against an FCA-regulated firm, FOS may be able to consider it. Learn more about FOS protection. (https://www.financial-ombudsman.org.uk/consumers)

3 - You won't get your money back quickly
Even if the business you invest in is successful, it may take several years to get your money back. You are unlikely to be able to sell your investment early.

The most likely way to get your money back is if the business is bought by another business or lists its shares on an exchange such as the London Stock Exchange. These events are not common.

If you are investing in a start-up business, you should not expect to get your money back through dividends. Start-up businesses rarely pay these. (https://www.financial-ombudsman.org.uk/consumers)

4 - Don't put all your eggs in one basket
Putting all your money into a single business or type of investment for example, is risky. Spreading your money across different investments makes you less dependent on any one to do well.

A good rule of thumb is not to invest more than 10% of your money in high-risk investments. (https://www.fca.org.uk/investsmart/5-questions-ask-you-invest)

5 - The value of your investment can be reduced
The percentage of the business that you own will decrease if the business issues more shares. This could mean that the value of your investment reduces, depending on how much the business grows. Most start-up businesses issue multiple rounds of shares.

These new shares could have additional rights that your shares don't have, such as the right to receive a fixed dividend, which could further reduce your chances of getting a return on your investment.

If you are interested in learning more about how to protect yourself, visit the FCA's website. (https://www.fca.org.uk/investsmart)

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