EIS and renewable energy

Julie Butler explains how renewable energy projects can assist tax efficient investing.

The opportunity

The trades of farming and property development do not qualify for Enterprise Investment Schemes (EIS) relief but where the trade is working with renewable energy, EIS qualification can be achieved.

The Budget of 23 March 2011 extended the scope of EIS and improved the capital allowances position on the equipment used in a renewable energy commercial project.

What are examples of the renewable technologies?

- Wind – individual or multiple turbines
- Solar photovoltaic – solar panels
- Hydro – small scale hydro schemes, e.g. rainwater harvesting
- Anaerobic digestion – the breakdown in organic waste materials to create biogas

In April 2010 the nationwide Feed-in Tariff (FIT) was introduced that offers a guaranteed price for electricity generated from renewable sources. On 10 March 2011, the Renewable Heat Incentive (RHI) was announced to offer incentives for the generation and use of energy from

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renewable sources by communities, the public sector, not-for-profit organisations, business and industry.

EIS can help tax planning around FITs and RHIs.

Action for landowners

The action plan for landowners is simple: understand the opportunities offered by RHI, see how this can add value to the farming enterprise and look at the most tax efficient route in the short, medium and long-term for the farming operation. All taxes must be considered – income tax, corporation tax, VAT, stamp duty, inheritance tax (IHT) and capital gains tax (CGT).

The use of EIS could be very useful where there is a need for an outside investor, i.e. outside funds will be required to see the project through.

The stages for consideration are:

- Landowner has suitable site for a renewables enterprise
- New company (Newco) is set up to own and operate the enterprise, (Newco cannot be a subsidiary of another company).
- Individual subscribes 30% (or less) share in Newco (see below).
- EIS claim is made by the investors.
- Landowner shares in profits of the renewables operation and achieves EIS tax relief.
- Landowner could receive rent for site, i.e. ownership of land retained therefore IHT protection via Balfour (RCC v Brander (as Executor of the Will of the late fourth Earl of Balfour) 2010 UK UT 300 TCC).

Tax relief from EIS

With EIS there are four separate reliefs:

- Income tax relief on subscription.
- CGT deferral relief on subscription.
- CGT exemption on disposal.
- Extended loss relief on disposal.

As farmers/landowners have not been used to EIS opportunities, as farming activities do not qualify, there will have to be education as to the structure. There are advantages in that an EIS company could bring expertise into the trading vehicle to help the commerciality.

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Subject to state aid approval, FA 2011 will introduce legislation to increase the income tax relief given under the Enterprise Investment Scheme from 20% to 30% of the amount subscribed for shares from 6 April 2011. In addition, with effect from 6 April 2012, FA 2012 will increase the following restrictions for the EIS company:

- The employee limit to fewer than 250 employees for both EIS and venture capital trusts;
- The size threshold to gross assets of no more than £15 million before investment for both schemes;
- The maximum annual amount that can be invested in an individual company to £10 million; and
- The annual amount that an individual can invest under EIS to £1 million.

FA 2012 will also introduce legislation providing that companies whose trade consists wholly or substantially of feed-in tariffs or similar subsidies will only be able to benefit from the schemes for shares issued from 23 March 2011 where commercial electricity generation commences before 6 April 2012.

HMRC guidance

The HMRC Business Income Manual at paras BIMs 40510, 40520 and 40530 provides advice on domestic microgeneration and renewable obligation certificates. No income tax or capital gains tax will arise on renewable obligation certificates where the microgeneration system is located at or near the taxpayer's home. Business income arising from such systems will be taxable.

Capital allowances

It was also announced in the March 2011 Budget that the Government is proposing to introduce legislation to clarify capital allowances treatment of equipment that is installed under the FIT and renewable heat incentive scheme. A consultation paper on this issue was released on 31 May 2011.

Tax Planning

For landowners, tax planning will range from looking at using the Annual Investment Allowance (AIA) to 5 April 2012 on plant associated with the installation of the regeneration system to hiving off the income from renewables in an EIS company. Farming does not qualify for EIS but a renewable energy incentive company does qualify. Inheritance Tax (IHT) must be considered in relation to the Balfour case.

For Business Property Relief (BPR) purposes active involvement by the landowner is more beneficial than rent, and consideration whether Balfour is robust enough must be considered.

The types of renewable technology such as wind, solar photovoltaic, harvesting rainfall, anaerobic digestion will be prolific in the months and years ahead and the tax planning should be in place from the start of the project.

Expenditure on non-domestic wind turbines or other alternative energy generators will attract capital allowances relief, including a proportion of the associated costs such as professional fees and site preliminaries. Typically for small discreet projects, these 'on costs' are included with the design and build price from the builder/ installer. On larger projects these costs are usually part of a more significant capital project and so would be subject to a pro-rata apportionment against the full contract expenditure.

Whatever reservations landowners might have about the whole concept of renewable energy technology; now is the time to embrace the opportunity and the exciting tax planning advantages.

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