

RESEARCH AND DEVELOPMENT (R&D) TAX CREDITS SCHEME



The UK's R&D tax credit regime is one of the most attractive in the world. Since its inception in 2000, the R&D tax relief scheme has had a significant impact on businesses engaging in innovative projects. The government's ongoing drive to encourage businesses to invest in R&D has resulted in increased rates of tax relief available to UK companies, with the repayable credit under the SME scheme now standing at 14.5%.

The scheme gives higher rates of corporation tax relief on allowable R&D costs. SME companies can deduct an additional 130% of qualifying costs from their taxable profits, giving a reduction in their corporation tax liability. Loss-making companies can surrender their R&D losses for a 14.5% repayable credit which can offer a lifeline to early-stage businesses.

For example, a profitable company investing £100,000 in qualifying R&D activities can obtain a £230,000 tax deduction, resulting in a reduction in the corporation tax liability of £24,700. If instead the company is loss-making, it can surrender the R&D losses for the tax credit available. This would generate a repayment of £33,350 which is an effective 33.35% subsidy on their R&D qualifying spend.

For accounting periods beginning on or after 1 April 2020, a **cap of 300% of the company's total PAYE and NIC costs** is expected to apply to the amount of repayable credit that can be claimed. This will predominantly affect companies who subcontract their R&D, as they do not have permanent employees.

From 1 July 2016, companies claiming more than €500,000 of relief per annum under the SME scheme have their details published on the European Commission website.

Large company relief

Relief for 'large' companies is by way of a 12% above-the-line taxable repayable R&D expenditure credit (RDEC).

The RDEC regime replaced the previous superdeduction alternative.

Rather than providing a deduction from taxable profits only, the RDEC is applied in the company's profit and loss account, i.e. 'above' the profit line, reducing the cost of qualifying expenditure. An RDEC is available at a rate of 12%. This is, however, subject to corporation tax at the main rate (19% since 1 April 2017), giving a net credit of 9.72%.

For example, a large company investing £100,000 in R&D qualifying expenditure can claim a taxable above-the-line credit of £12,000 (£9,720 net of corporation tax at 19%). This will give the company a net credit of 9.72% and tax relief of £9.72 for every £100 spent on qualifying R&D.

The main rate of corporation tax is due to fall to 17% from 1 April 2020 which will increase the net credit to 9.96%.

Deduction rate on qualifying expenditure

The current rates of relief for qualifying R&D expenditure are set out below:

SME Scheme
Post 1/4/15
230%

SME scheme repayable tax credit

SME Scheme
Post 1/4/15
14.5%

RDEC (gross credit)

Large Scheme	
1/4/15 - 31-12/17	Post 1/1/18
11%	12%

How projects qualify as R&D

To qualify as R&D, your project must meet four specific criteria set out by HMRC, as summarised below.

1. What was the scientific or technological advance?

It is not enough that a product is commercially innovative; the creation of the product or process must involve steps or techniques that are not readily known and deducible by an expert in the field. The advance needs to extend the overall knowledge or capability in a field or science and not just an advance in the company's own knowledge or capability.

Projects to develop innovative business products or services that do not incorporate any advance in science or technology are not eligible.

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2. What were the scientific or technological uncertainties involved in the project?

As part of achieving the scientific or technological advance, there will be scientific or technological uncertainties that exist. Such an uncertainty exists when knowledge of whether something is scientifically possible or technologically feasible, or how to achieve it in practice, is not readily available or deducible by a competent professional working in the field. Uncertainties that can be resolved through relatively brief discussions with peers are **routine uncertainties rather than technological uncertainties**.

Technical problems that have been overcome in previous projects on similar systems are not likely to be technological uncertainties.

3. How and when were the uncertainties actually overcome?

The project should involve overcoming the uncertainties identified. In making a claim to HMRC, you will need to be able to explain the methods adopted to overcome the uncertainties as well as the investigation and analysis undertaken.

In some cases, the uncertainties may not be overcome. This does not preclude the project from qualifying as claims can be made in respect of projects that fail.

4. Why was the knowledge being sought not readily deducible by a competent professional?

It might be publicly known that others have attempted to resolve the uncertainties and failed, or perhaps that others have resolved the uncertainties, but precisely how it was done is not in the public domain. In either case, a valid scientific or technological uncertainty can still exist.

Alternatively, if the project is one where there is little public information available, you will need to show that the team leading the R&D project are themselves competent professionals working in the relevant field and why they consider the uncertainties as scientific or technological uncertainties rather than routine uncertainties.

Advance assurance

HMRC has introduced an advance assurance process for use by certain companies seeking to claim R&D tax relief for the first time.

It is aimed at small start-up companies who want reassurance in advance that their activities fit within the rules. This saves them unnecessarily analysing expenditure and incurring professional fees in preparing claims.

Applying for advance assurance is optional and gives a company comfort that their R&D claim for the first three periods will be processed without further enquiry, provided the claims are in accordance with details provided in the original application.

The advance assurance is only available to companies meeting all of the following criteria:

- First time claiming R&D tax relief
- Annual turnover of £2million or less, and
- Fewer than 50 employees.

How we can help you

Dealing with HMRC is key. A well-presented and properly supported claim is far more likely to succeed than merely meeting the minimum legal requirements.

In making an R&D claim, HMRC requires you to satisfy criteria in three main categories:

- Project qualification
- Supporting documentation, and
- Clear effective methodology.

We know HMRC's requirements inside out, and have a wealth of knowledge and experience across numerous sectors. We can assess which of your business activities qualify for R&D tax relief and then help you maximise your claim.

Qualifying expenditure

The R&D tax relief is limited to costs incurred on the following types of qualifying expenditure:

- Staffing costs
- Externally provided workers (amount capped at 65% if unconnected to the claimant company)
- Subcontracted R&D expenditure (amount capped at 65% if unconnected to the claimant company)
- Consumable items (materials and utilities)
- Software

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Moore Kingston Smith has been helping clients build their business for more than 90 years. As chartered accountants and business advisers, we work with clients to understand their potential and ambitions, and provide all the information and support they need to achieve them.

Most of our commercial client businesses are managed by the people who own them. We have over 60 partners and more than 500 professional staff focused in and around London and the South East, where our commitment to the more entrepreneurial types of business has created long-lasting successes.

Outside the UK, our membership of Moore Global Network offers our clients the strength and experience of 609 offices in 112 countries throughout the world to support their international reach. That combination of geographic knowledge, commercial expertise and client empathy has given us a great track record in helping clients open and grow their business in the UK.

CONTACT US

To find out more, please contact your client partner or our R&D team for a no-obligation chat.

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