Research and Development – addressing some of the uncertainty

Large Corporate | Tax voice



20 December 2017

From an R&D tax relief perspective the headline news from the recent Budget was the increase in the rate of R&D Expenditure Credit (RDEC) from 11% to 12%. The increased rate will apply to expenditure incurred on or after 1 January 2018. The proposed amendment to CTA 2009, s104M to effect this change is included in the Finance Bill, published on the 1st December, at Clause 19.

The RDEC was introduced in Finance Act 2013 as the replacement for the superdeduction relief previously available to large companies (at 130%). The rate of

RDEC was initially set at 10% but that was increased to 11% for expenditure incurred on or after 1 April 2015.

RDEC is mainly claimed by large companies, so the increase proposed in the Budget will mainly be of interest to those large companies. It will also be of interest, however, to those SMEs with subsidised expenditure or undertaking R&D subcontracted to them by a large company, as they will claim RDEC on that expenditure.

Although the rate rise was the headline announcement that most people have focused on, buried in the Budget document (at paragraph 4.18) was a brief statement that '*the government will also introduce a new Advanced Clearance Service for R&D expenditure credit claims*'. There is also a reference to this proposal in the Overview of Tax Legislation and Rates (OOTLAR) at paragraph 2.24. This says that ‘the government will pilot a new Advanced Clearance service for Research and Development (R&D) expenditure credit claims, to provide pre-filing agreement for 3 years'.

This looks to be delivering on a promise made in the Spring 2017 Budget to ‘*make administrative changes to the Research and Development Expenditure Credit to increase the certainty and simplicity around claims*’.

Whilst this sounds very promising at first glance, what is lacking at this stage is any real detail. That said, there is a possible precedent for this proposal in the form of the Advance Assurance (AA) scheme available for very small first time claimants of R&D relief. AA was launched in November 2015 and is essentially a scheme for very small first time claimants to have their R&D claims 'pre-approved' for three years. The benefit is comfort that the claims for those periods can be made and will be approved without significant query (assuming there is no substantial change in the R&D activity). For a small company, particularly start-ups, this is a big benefit.

Notwithstanding the slightly different terminology between the AA and the proposed Advanced Clearance Service (ACS), from discussions I have had with HMRC it seems that ACS is going to be a variation of AA for larger companies claiming RDEC. The pilot, which looks like being by invitation to a relatively small number of Large Business ‘customers’, will see HMRC discuss the RDEC claims of those companies before they are filed. The aim will be to identify and seek to address any issues before the claim is formally filed along with the CT600.

The certainty will be around the fact that the claim will have been pre-approved. I'm not completely sure at the moment about the three-year period and how that will work.

I do have some concerns, however, over the operation of such a scheme.

First, just how does HMRC intend to resource the ACS? It is clear that R&D specialists within HMRC are currently spread very thin on the ground. An application for clearance will require their attention, presumably within a specified time frame. Is that going to mean resources are diverted from dealing with other claims? Of course, if this scheme is successful I can see that there might be fewer claims that need reviewing in the normal course of events (as they will have been 'pre approved'). That may be the hope but the number of R&D claims is increasing each year and, presumably, not all claims will be suitable for approval through the ACS.

The second concern is to do with the nature of R&D projects. By their very nature they have a significant element of uncertainty. Whilst it may be possible at the outset to scope out a plan, in reality it probably won't be long before the plan has to be revised in real time as challenges materialise. That's fine in that the work may still be qualifying R&D but how will the advance "clearance" deal with changes like this? How far can the R&D plan change before the clearance needs to be revisited? It's true that this is something that AA is already dealing with, but with very small companies where the R&D is likely to me that bit more "stable". Or is the intention simply to discuss each year's claim in advance of the filing? There is clearly still a long way to go before we know all of the details.

I don't want to appear too negative about this proposal; to be fair, anything that helps more companies claim R&D relief is definitely to be welcomed. I guess we will just have to wait and see what the detailed proposals are in due course. There is an obvious question, however: why is this being restricted to RDEC – why do large companies need greater certainty than SMEs? Maybe the plan is to roll it out to all companies if the pilot is successful?

Aside from those SMEs who will be claiming relief on at least part of their R&D expenditure under RDEC, the only help in the Budget for SMEs appears to be a promise to launch a campaign to increase awareness of eligibility for R&D tax credits amongst SMEs. We are told that the Government will work with businesses that develop and use 'key emerging technologies' to ensure that there are no barriers to them claiming R&D tax credits.