Preventing abuse of the R&D tax relief for SMEs: ATT and CIOT responses

OMB

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The ATT and CIOT have both responded to a consultation on capping the payable tax credit available under the SME R&D scheme.

The SME scheme allows loss making companies to surrender the R&D element of their losses in return for a payable tax credit. Whilst this is a valuable relief for many loss making and smaller companies, HMRC are concerned that it has become a target for abuse.

As a result, at Budget 2018 the Chancellor announced that, from April 2020, the amount of payable tax credit that loss making companies can receive in any one year will be capped at three times their total PAYE and NICs liability for that year.

A consultation Preventing abuse of the R&D tax relief for SMEs was launched in March 2019 to consider how this cap could be applied so as to minimise the impact on genuine businesses. The CIOT welcomed the recognition in the consultation document of the importance of R&D to increasing productivity and the commitment of the government to supporting innovation and accepted that HMRC must work to counter fraudulent attempts to claim the SME scheme payable tax credit and support HMRC in this aim. However, the CIOT response expressed concern that the proposed cap will have an impact on and may prevent claims from some genuine businesses, consequently acting as a deterrent to such companies from undertaking R&D. The CIOT therefore welcomed the aspects of the consultation around minimising the effects of the proposed cap.

One of the key proposals in the consultation is that that the cap will only apply to payable tax credit claims above a certain threshold.

Both the ATT and CIOT responses welcome the idea of such a threshold. The ATT stressed that its level needs to be set high enough to provide a valuable simplification yet low enough to ensure it excludes abusive practices. The ATT response also recommends that HMRC use their data on current claims to establish whether the illustrative figure in the consultation of £10,000 is appropriate.

The CIOT said that it would like to see the threshold set as high as possible and said that in its view very few claims would fall below a threshold of £10,000. The CIOT suggested that to allow for a payable tax credit on qualifying expenditure of a realistic amount of around £60,000, a threshold of at least, £20,000 would be more appropriate.

Both the ATT and the CIOT also welcomed the proposal that companies who are subject to the cap would be allowed to carry forward losses to surrender in future periods when they have sufficient PAYE and NIC liabilities. Both said that the proposed two-year time limit for carrying forward losses was insufficient. The ATT questioned whether any such time limit is needed and the CIOT suggested that the rules should be aligned with the rules around carry forward of losses on change of ownership and major change in nature/conduct of trade – so in essence surrenderable losses can be carried forward indefinitely, unless and until such time as those rules bite and then they are extinguished.

The ATT and CIOT both said that the companies most affected by the cap will include the smallest start-up businesses and more established companies where the majority of work is undertaken by director-shareholders. One area of particular concern is the impact on companies which operate employee share schemes such as Enterprise Management Incentives (EMI) which have consequentially low PAYE and NICs bills and could suffer disproportionately under the cap. The ATT recommends that consideration be given to extending the cap where an approved share scheme is in use.

Finally, whilst agreeing that action needs to be taken to combat abuse of the SME scheme, both the ATT and the CIOT questions why HMRC cannot use their existing powers (including invoking the anti-abuse provision in CTA 2009 section 1084) and the data they hold to spot and address such abuse directly. The CIOT said it would be surprised if HMRC does not have a set of indicators that it can apply to claims in order to identify those that are more likely to be abusive.

The ATT response can be found on the ATT website.

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