

# Research & Development

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**CALDWELL PENN**  
chartered accountants • chartered tax advisers

“R&D is not just about laboratories...”



# Overview

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## What are Research & Development tax credits?

Research and development (R&D) tax credits are a government incentive designed to reward UK companies for investing in innovation. They are a valuable source of cash for businesses to use to invest and ultimately continue growing.

Companies that spend money on qualifying R&D activities can make a R&D tax credit claim to receive either a cash payment and/or Corporation Tax reduction. If you're making a claim for the first time, you can typically claim R&D tax relief for your last two completed accounting periods.

### Who qualifies?

Any UK limited company that is subject to corporation tax and has;

- Carried out qualifying R&D activities
- Spent money on qualifying R&D costs.

### What is a qualifying R&D activity?

- Creating new products, processes or services
- Changing or modifying an existing product, process or service.

### Which tax credit scheme is right for me?

There are two tax credit schemes; SME R&D tax credit and R&D Expenditure Credit (RDEC). Which scheme you use to make an R&D tax credit claim will largely depend on whether you are an SME or a large company.

### How much could I claim?

SMEs are able to claim up to 33p for every £1 spent on qualifying R&D costs.

Large companies are able to claim up to 10p for every £1 spent on qualifying R&D costs.

### What costs qualify?

- Staff costs including Employers Class 1 NIC contributions.
- Subcontractor costs
- Testing costs
- Cost of materials
- Water, fuel or power consumed in the R&D process
- Training costs
- Types of software
- Capital costs.

## Contact Us

For the latest news and advice please visit our Facebook, LinkedIn and website pages. If you have any immediate questions or if you would like to discuss anything further please contact us via email or give us a call on our usual office telephone numbers:

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# Qualifying Activities

If you are creating a new or improved product, process or service, your business might be carrying out research and development (R&D). You will probably be attempting to solve a problem where no solution is evident. This can take many forms. And R&D projects can include work undertaken for a client as well as your own business.

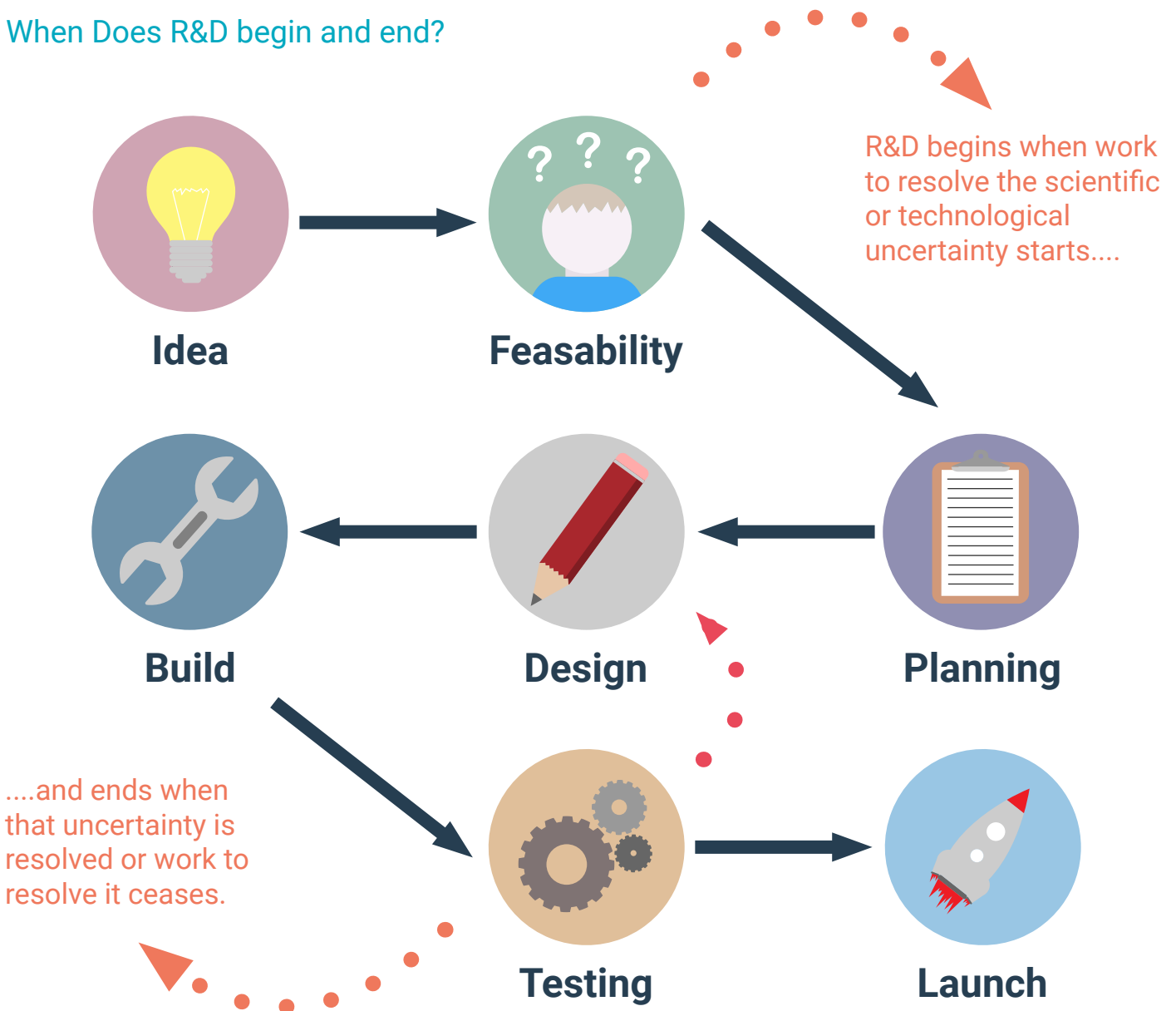
The government's definition of R&D is purposefully broad. Whatever size or sector, if your company is taking a risk by attempting to 'resolve scientific or technological uncertainties' then you may be carrying out qualifying activity.

## Examples

Software development, engineering design, new construction techniques, bio-energy, cleantech, agri-food and life and health sciences. Examples of qualifying projects could include those which:

- Increase the life of a battery
- Create a new type of material in an item of clothing
- Develop new spark plugs for use in an existing engine.

## When Does R&D begin and end?





# Qualifying Costs

## Direct R&D Staff Costs

Your company can claim for salaries, wages, class 1 NIC and pension fund contributions for staff directly and actively engaged in the R&D project.

This covers employees who undertake 'hands on' R&D work and the proportion of supervisory and managerial time spent specifically directing such employees in those activities.



## Subcontractor Costs

Your company can generally claim for 65% of the payments made to unconnected parties. The subcontracted work may be further subcontracted to any third party.

Special rules apply where the parties are connected or elect to be connected. Under the RDEC scheme subcontractor costs are generally not allowable.



## Material Costs

Your company can claim for the cost of items that are directly employed and consumed in qualifying R&D projects. These include materials and the proportion of water, fuel and power consumed in the R&D process.

From 1 April 2015, the costs of materials incorporated in products that are sold are not eligible for relief.



## Software Costs

Your company may claim for the cost of software that is directly employed in the R&D activity. Where software is only partly employed in direct R&D, an appropriate apportionment should be made.



## Prototypes

Where a prototype is created to test the R&D being undertaken, the design, construction and testing costs will normally be qualifying expenses.

However, if the prototype is also built with a view to selling the prototype itself, HMRC considers that to be production and outside the R&D scheme, even if R&D was undertaken to create the prototype.

# Which Tax Credit Scheme Is Right For Me?

Which scheme you use to make an R&D tax credit claim will largely depend on whether you are an SME or a large company. You will also need to take into consideration linked or partner companies.

## SME:

**Fewer than 500 staff** and either **not more than €100 million turnover** or **€86 million gross assets**. Most companies, including start-ups, fall into this category.

## Large company:

**500 staff** or more and **either more than €100 million turnover** or **€86 million gross assets**.

## Considering linked and partner companies

You will also need to take into consideration linked and partner companies when determining whether your company is an SME or large company.

If the company is controlled by or controls other companies it is a linked company, for example if it has more than 50% of the shareholders' or members' voting rights in another company. All of the data of the linked companies should be added to the data of the company that does the R&D.

If 25% or more of a company is owned by another, or if the company owns 25% or more of another, it is a partner company. The percentage controlled should be added to the data of the company that does the R&D up to 50% after which it becomes a linked company. Please see the next page for examples.

## What next?

If you are classified as an SME, your next step will be to make a claim via the SME R&D tax credit scheme. And if you are a large company, via the Research and Development Expenditure Credit (RDEC).

However, there are a few factors like grants and subcontracting that can restrict an SME from accessing the SME scheme. This means you may need to make a claim via RDEC – or via both schemes.

It is possible to make use of R&D tax credits and grant funding together by using both schemes to ensure maximum value.

		SME R&D Tax Credit	RDEC
		Tax Scheme	
Type of company	SME	YES	YES
	Large Company	NO	YES

# Linked or Partner Companies?

Company D will add 35% of the accounts figures of Company A. So if Company A has turnover of €100m, it will add €35m to its totals.

Company  
A

Company  
B

35%

25%

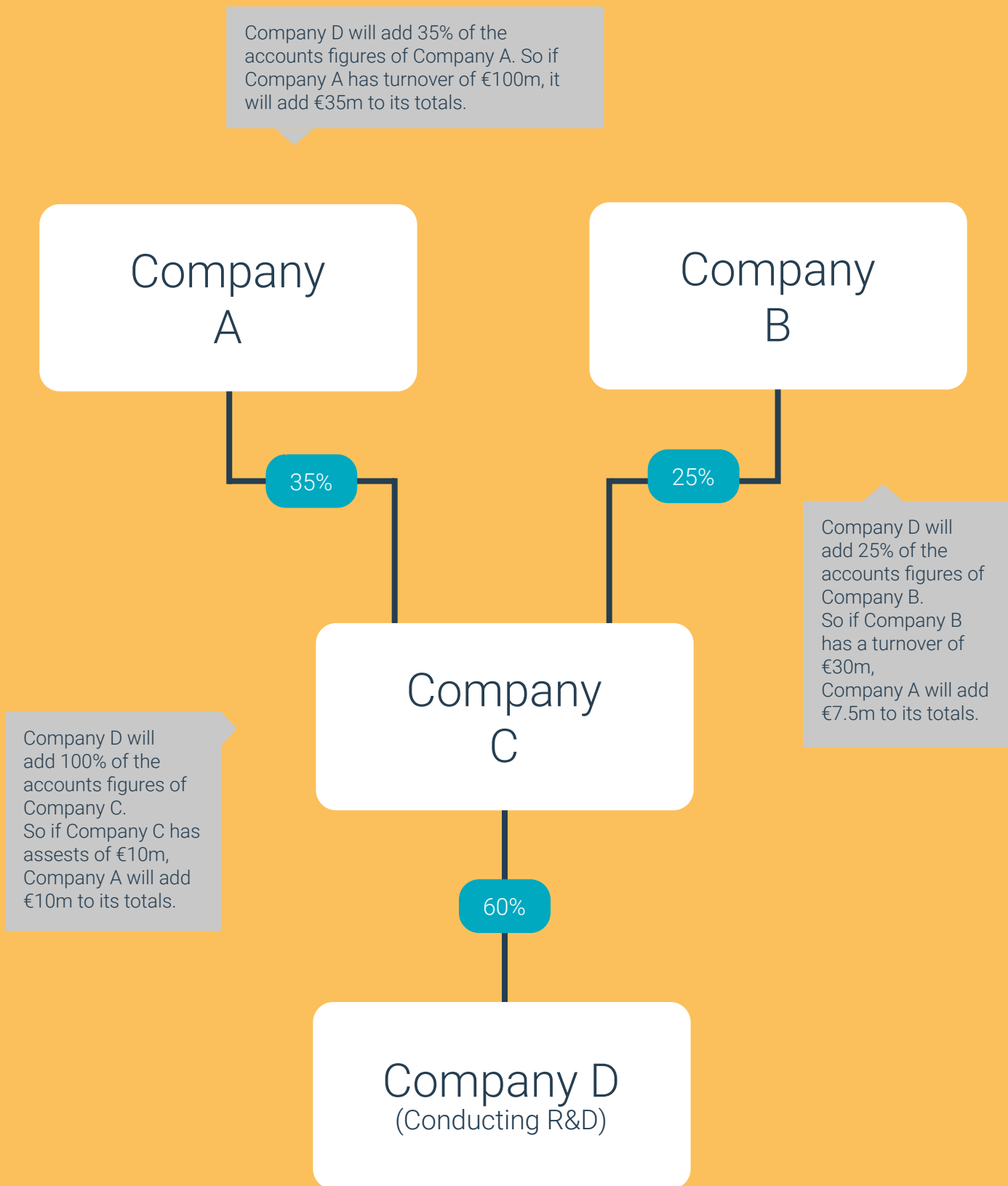
Company D will add 25% of the accounts figures of Company B. So if Company B has a turnover of €30m, Company A will add €7.5m to its totals.

Company  
C

Company D will add 100% of the accounts figures of Company C. So if Company C has assets of €10m, Company A will add €10m to its totals.

60%

Company D  
(Conducting R&D)



# How Much Could You Claim?

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## How a does a claim work?

R&D tax credits are calculated based on your R&D spend. To make an R&D credit calculation, you need to identify qualifying expenditure and enhance it by the relevant rate (see below). This produces your 'enhanced expenditure'.

When you deduct your enhanced expenditure from your taxable profits, or add it to your loss, it will result in:

- a Corporation Tax reduction if you are profit-making
- a cash credit if you are loss-making
- or a combination of the two.

# 33%

Profit making SMEs are able to claim up to 33p for every £1 spent on qualifying R&D activities. The average claim made by SMEs in the UK is £53,876 (2016-17).

Loss making SMEs are able to claim up to 25p for every £1 spent on qualifying R&D activities. This will be claimed as a cash credit which can help with cash flow for start-up companies.

# 25%

# 10%

Large companies are able to claim up to 10p for every £1 spent on qualifying R&D activities. The average claim made by large companies in the UK is £272,881 (2016-17).

## The benefits



**Cash Injection**



**Growth**



**Global Leader**

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“You might already be conducting R&D... but just not know it yet”

# The Process

## Introduction and Fact Find

- We will schedule a brief call with you to establish the company's eligibility to claim R&D tax relief.
- We will obtain background information about the company and outline how our R&D process works.
- If a claim is eligible and likely to be beneficial for you, we will issue you with our formal proposals to assist with processing a potential claim.



## Full Consultation

- We will schedule a consultation with you to run through the R&D process and to explore your R&D projects in more detail.



## Claim Maximised & Project Report Created

- We will prepare your claim and create an R&D report for each project for you to review and approve. This will include a technical narrative, a summary of the costs you have incurred and a breakdown of how the total benefit has been calculated.
- Our team will schedule a call or meeting with you to run through the report and to discuss the optimum tax treatment of the R&D expenditure for the company.



## Submission

- We will submit your report and amend your Corporation Tax return (CT600), incorporating your R&D tax credit calculation.
- We will follow up with HMRC to check on your claim's progress.
- In the unlikely event that HMRC opens an enquiry relating to your R&D tax credit claim, we will resolve this for you at no extra cost.



## Benefit Obtained from HMRC

- HMRC aim to process all claims within 4 – 6 weeks.
- If your business is profitable, your overall Corporation Tax bill will be reduced, or if you have already paid your bill for the period, you will receive a repayment.
- If your business made a loss for the period, you will receive a R&D tax credit cash refund.



## Follow Up

- We will arrange a follow up call to commence discussions and preparation of future R&D tax relief claims.
- This will include recommendations and advice in respect of streamlining the R&D process and maximising the value of future claims.

## Our Fees

- To align our goal of maximising claim value, our fee is calculated as a percentage of the cash benefit you receive.
- Payment of our fee is not due until after the payable credit and/or Corporation Tax reduction has been received.
- Our fee covers a full, end-to-end service for each claim period with no added extras or multiple year contracts.

