



Research and Development Tax Relief

Innovation is an essential driver of economic growth. Some of the UK's leading exports include defence, aerospace, pharmaceutical and financial services. Each of those markets is under threat with the exit from the EU. The UK needs to remain innovative therefore research and development tax relief is likely to be around for a long time. However, it is widely reported that there is a significant discrepancy between those who innovate and those who claim relief.

Companies that incur expenses developing new or enhancing existing products, processes or services are eligible for research and development tax relief. A company can make an R&D tax credit claim and either reduce their corporation tax or receive a cash payment! If a company is making its first claim, the claim can typically be for the last two completed accounting periods.

The scope for identifying R&D is huge. Research and development exists in every market sector.

The common areas of qualifying R&D expenditure, which are often overlooked, include:

- Internal projects that are unsuccessful and which could still qualify as R&D

- Expenditure on changes or modifications of an existing product
- R&D expenditure on relevant to services and processes

Do you have qualifying expenditure?

The legislation defines R&D as those activities treated as R&D in accordance with generally accepted accounting practices. FRS 102 and IAS 38 contain the accounting definitions, although modified by guidelines issued by the Secretary of State for Trade and Industry on 5 March 2004.

FRS 102 states that

- Research is the *“original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding”* and that
- Development activity is *“the application of research findings or other knowledge to a plan or design for the production of new or substantially improved materials, devices, products, processes, systems or services before the start of commercial production or use”*

FRS 102 also tests whether an entity has created an intangible asset which could generate probable future economic benefits.

For tax purposes, guidelines further define R&D as:

- When a project seeks to achieve an advance in science or technology
- The activities directly contribute to achieving an advance in science or technology through the resolution of scientific or technological uncertainty
- Certain qualifying indirect activities related to the project
- An advance in science or technology means an advance in overall knowledge or capability in a field of science or technology
- The adaptation of knowledge or capability from another field of science or technology
- An advance in science or technology that may have tangible consequences
- An advance that may have more intangible outcomes such as cost improvements

What relief do you get?

Relief for expenses against profits chargeable to corporation tax will depend whether those expenses are revenue or capital in nature. Relief against profits for capital expenditure is normally restricted. However, expenditure on R&D can be relieved in the following ways:

- **Large trading company:** Revenue expenses are allowable as a deduction against the profits of the trade, and capital expenditure may be eligible for 100% R&D allowance. In addition an R&D expenditure credit, which is 12% (for expenditure after 1 January 2018) of qualifying expenditure. The credit can be used to discharge a liability to corporation tax.
- **SME trading company:** Qualifying expenditure is eligible for additional research and development tax relief, giving a total deduction of 230% of the original costs. If the SME realises a trading loss, it can surrender that loss for a tax credit of 14.5%.

Potential areas where research and development tax relief may be obtainable:

- Developing a new software
- Adaptation of premises and software development
- Developing a new material for use in engineering
- Creating new and innovative construction systems
- Modernisation and quality control improvements
- Integrating new technology with existing systems
- Adapting a product for a new market
- Creating new medical equipment
- Certain food produce developments
- Advancing eco-friendly technology
- Developing communications systems (for example in aeronautics)

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Featured Image Alt Text research and development tax relief

The logo for Edge Tax Specialists features the word "edge" in a large, lowercase, sans-serif font. A thick, grey diagonal line cuts through the letters from the bottom left to the top right. Below "edge", the words "THE TAX" are written in a smaller, uppercase, sans-serif font, and "SPECIALISTS" is written in the same font size and style below that. The entire logo is rendered in a light grey color.

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