

Research & Development tax relief

Enhanced tax relief for qualifying Research & Development (R&D) costs is available, but to benefit from this, the following conditions and definitions need to be met:

Definition of R & D

The tax definition of R & D closely follows that of the accounting definition in SSAP 13 and the guidelines issued by the Department of Trade and Industry.

An activity can qualify as R & D if it is characterised by work that contains an **appreciable element of innovation and creativity in the fields of science and technology**. The work can range from research into a purely theoretical area to applied research and experimental development towards a practical aim or product. It is research that aims to **break new ground** or **to resolve scientific or technological uncertainties**.

For an activity to qualify it must meet three criteria:

- It must seek to achieve a scientific or technological **advancement**.
- It must seek to resolve a scientific or technological **uncertainty**.
- It must be by way of **systematic investigation**.

R & D can include the development of prototypes and pilot plant to test the R & D, but commercial development without such scientific or technological investigation, or after the resolution of such uncertainties, is not R & D for tax purposes.

Qualifying R & D Expenditure

To qualify for the more valuable enhanced relief available for Small and Medium-sized Enterprises, only expenditure meeting the following criteria is eligible:

- Not capital expenditure (but this may qualify for a separate allowance)
- Attributable to relevant research & development
- It is incurred on staffing costs, consumable items, consumable stores, or qualifying subcontracted work
- Any intellectual property (e.g. know-how, patent, trade mark, copyright, etc.) created as a result of the R & D is vested in the company.
- The company does not incur the expenditure as a subcontractor.
- The expenditure is not subsidised.
- The R & D expenditure must be more than **£10,000** in the year to qualify.

Definition of Staffing Costs

Staffing costs are all amounts paid to directors and employees including:

- Gross pay, bonuses, and fees paid, but not the cost of providing benefits in kind, such as company cars.
- Employer's NIC paid in respect of the employee insofar as they relate to money payments (i.e. not Class 1A or Class 1B NIC).
- All pension payments.

The employees must be directly and actively engaged in R & D, meaning that they are undertaking the R & D or providing technical support, or are managers who plan and organise the programme of research. Indirect support staff do not qualify.

Definition of Subcontractor Costs

If an SME subcontracts all or part of its R & D work to another person, but retains the intellectual property rights, it may be able to claim R & D tax relief on its payments to the subcontractors.

The rules for claiming relief on this type of expenditure are complex and the rules differ depending on whether the subcontractor is a “connected person”.

If the subcontractor is connected, the company can claim relief on the lower of the amount brought into the subcontractor’s accounts in respect of costs related to R & D work and the amount of the company’s payment to the subcontractor.

If the subcontractor is not connected, the company can claim relief in two ways, either by making a joint election with the subcontractor to be treated as connected (as above), or, by claiming 65% of the payment made to the subcontractor.

Large companies can only claim for research sub-contracted to individuals or non-taxable qualifying organisations (universities, etc.).

Definition of Consumable Stores

Expenditure on consumable stores is expenditure on materials and equipment used up in the R & D activity, but not incorporated in the product of R & D (e.g. short-life laboratory equipment such as test tubes).

The Relief

The relief available depends on the size of the company. Small and Medium-Sized Enterprises must have less than 500 employees and either turnover of up to €100m or a balance sheet value of less than €86m (limits were half these amounts before 1 August 2008). In addition, no more than 25% of the company’s shares may be held by large companies.

SME scheme	Large company scheme
175% rate of enhanced deduction (was 150% before 1 August 2008)	130% rate of enhanced deduction (was 125% before 1 April 2008)
Payable credit at 14% of enhanced expenditure on R&D (was 16% before 1 August 2008)	No payable credit
Company can claim for expenditure on R&D it sub-contracts to others	Company can only claim for expenditure on R&D it carries out itself, unless it sub-contracts R&D in certain limited circumstances to certain entities
Company cannot claim for contributions to independent research	Company can claim for contributions to independent research (e.g. universities)
Claim can be reduced if the R&D project is subsidised or a grant-funded	No reduction for grant or subsidy
Company must own the intellectual property arising out of the R&D (accounting periods ending before 9 December 2009)	Company need not own the intellectual property arising out of the R&D

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