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R&D tax relief

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R&D tax reliefs – over view of current schemes

R&D tax relief

The UK government provides some significant tax incentives for companies undertaking research and development work (R&D).

The aim is to encourage investment in R&D and to support technical innovation in the UK.

There are two schemes depending on the size of the company. A company qualifies for the small and medium company (SME) scheme if it has:

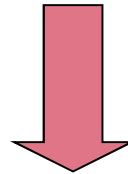
- Fewer than 500 employees; and
- Annual turnover not exceeding €100m **or**
- Balance sheet totalling more than €86m

SME Regime overview – quick reminder

What are the potential benefits?

Revenue expenditure

- *Qualifying expenditure on qualifying R&D*
- Is eligible for a **125% corporate tax extra deduction (100% before 1 April 2012)**
- And a **cash repayment** if losses surrendered



**IMMEDIATE
CASH TAX
SAVING**

SME Regime overview

Cash tax savings

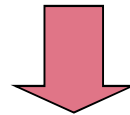
	To 31 March 2011	From 1 April 2011	From 1 April 2012
Qualifying R&D costs	100,000	100,000	100,000
Extra 75% / 100%/125%	75,000	100,000	125,000
The extra deduction will result in:			
Tax saved @ 28% / 26%/24%	21,000	26,000	30,000

SME Regime overview – quick reminder

What are the potential benefits?

Capital expenditure

- Qualifying expenditure on
- *Qualifying R&D*
- Research & Development Allowances



**100% TAX
DEPRECIATION**

Provides a cash flow benefit against the usual 20%/18% reducing balance basis of tax depreciation

Large companies Overview of R&D Tax Relief

	<i>Large Companies</i>
Qualifying R&D	£1,000,000
Extra 30%	£300,000
The extra deduction will result in:	
<i>Tax saved @ 24%</i>	<i>£72,000</i>

Enhanced R&D allowances are available on capital spend

A large company is

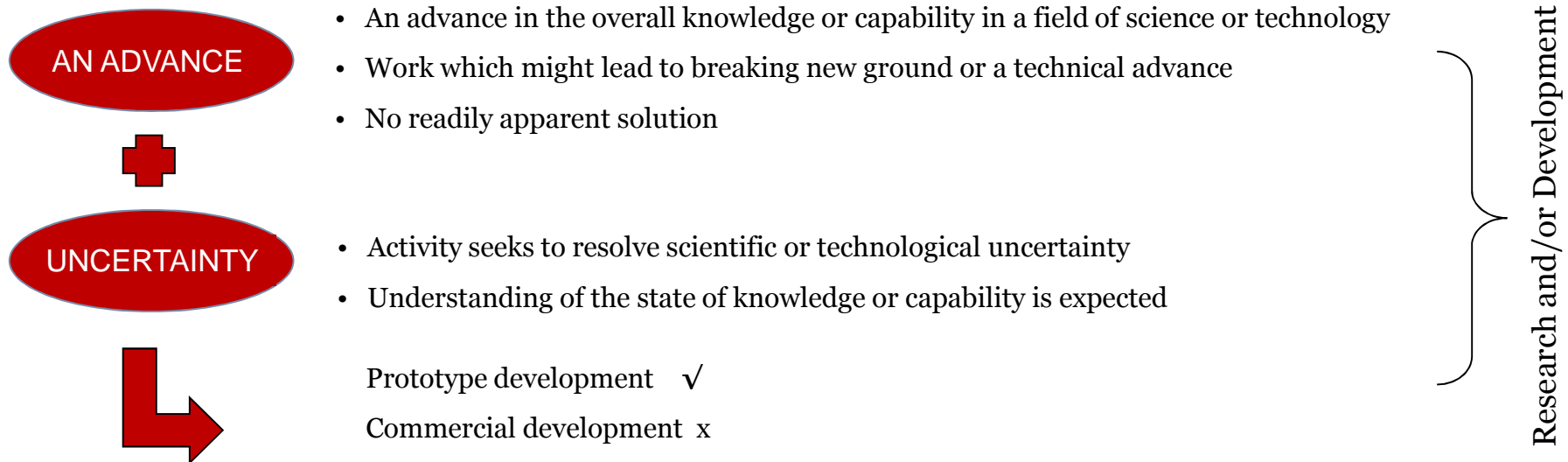
- Over 500 employees
- Annual turnover exceeding €100m **or**
- Balance sheet totalling more than €86m

What is qualifying R&D?

It is not always clear whether an activity is R&D

For tax purposes R&D takes place *“when a project seeks to achieve an advance in science or technology with activities that directly contribute to the resolution of scientific or technological uncertainty”*

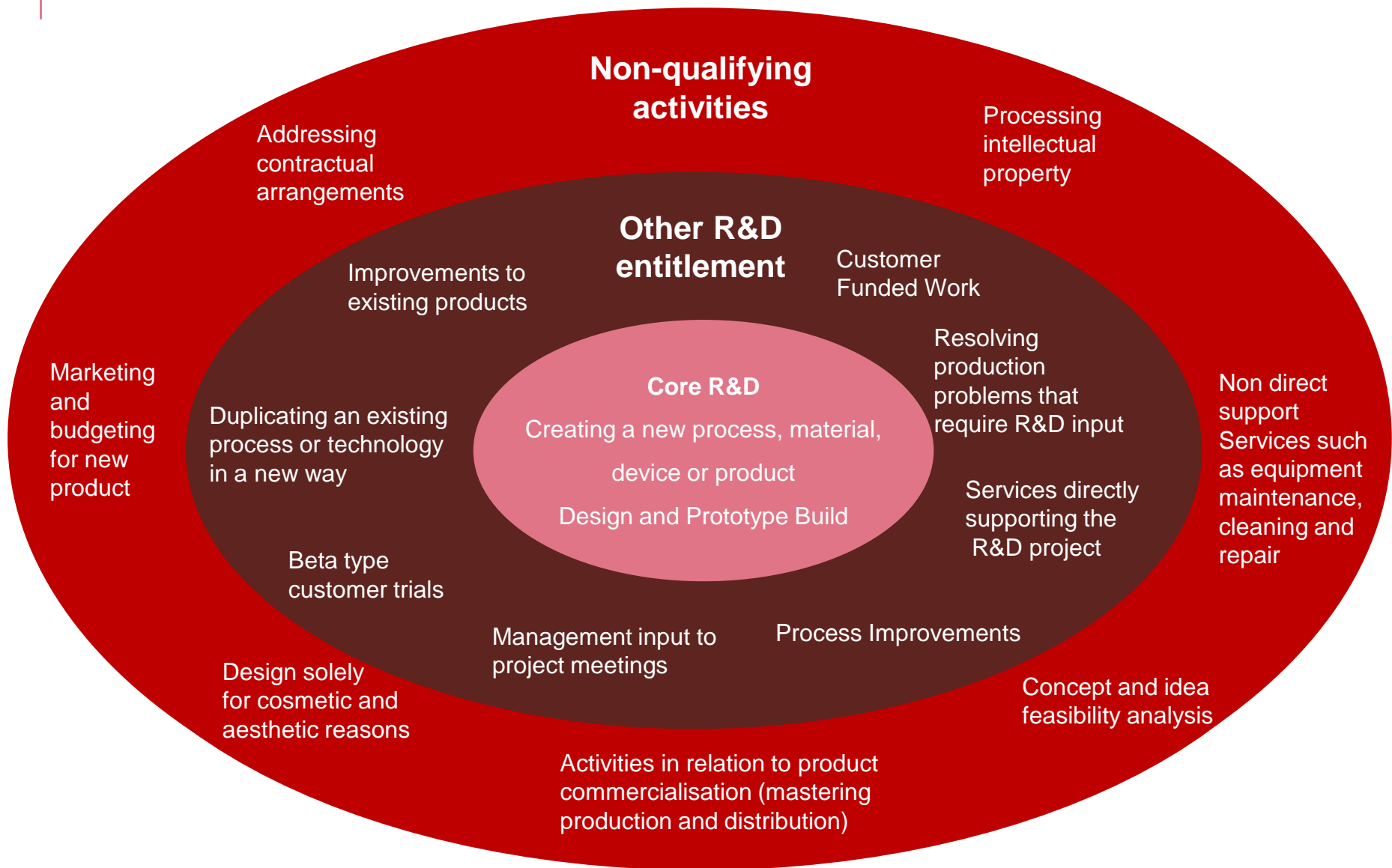
R&D is characterised by:



What is qualifying R&D?

	Advance & uncertain	Cosmetic/routine
New designs and developments Appreciable improvements to existing designs or processes		
Routine but necessary (e.g. testing)		

- Activity should not be discounted because it is not ground breaking fundamental research
- Percentage reductions in time can be estimated to reflect mix of time between R&D and non-R&D time on a project



Regime overview – quick reminder

What is qualifying expenditure?

Staffing costs

The following costs qualify for staff directly **or indirectly** involved in qualifying R&D activity

- Salaries, wages, etc
- Employers Class 1 NIC
- Payments to pension funds

But not

- Benefits
- Class 1A, 1B NIC on benefits

Universities / Independent R&D

In some instances payments to qualifying bodies such as Universities contributions will qualify

Externally provided workers

In some instances payments to agencies/group employment companies for staff will qualify

Consumable or transformable materials

Expenditure on materials and equipment used up in the R&D activity but not incorporated in the product of the R&D

- Heat, light, power

But not

- Rent, rates, interest or lease payments
- Capital items

Subcontracted R&D

Any subcontracted R&D payments can be claimed, usually for 65% of the costs

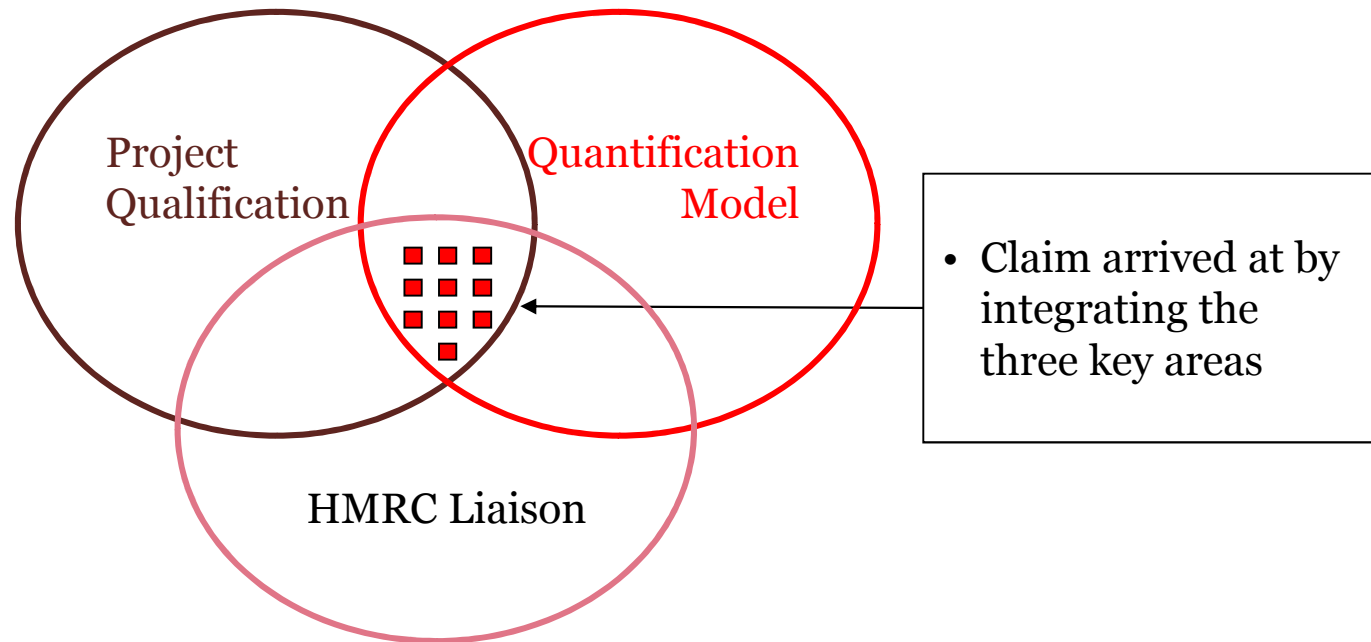
Grant/subsidies

These may impact on SME R&D claims and can reduce the enhanced R&D relief uplift

Approach to a claim

Three Key Areas

- Establishing qualifying activity
- Creating a qualification methodology
- Documentation
- Devising the methodology
- Collect eligible expenditure



• Claim arrived at by integrating the three key areas

Managing expectations

Reducing risk of future enquiries

R&D tax reliefs – proposed changes

The R&D consultation

What was in the consultation?	What has happened?
Qualifying indirect activities ('QIA')	Retained
Subcontracted activities which are routine in nature	No changes at present
'Above the line' credit for large companies	To be introduced in April 2013 following further consultation
Externally provided workers	Tripartite relationship rules relaxed for unconnected parties.
SME rates increasing to 125%	Confirmed, effective from 1 April 2012
PAYE/NIC cap to be abolished	Confirmed, APs ending 1 April 2012
SME 'going concern' condition	Definition to be amended

Why above the line?

- Reduces the actual cost of R&D making the UK more competitive.
- Affects R&D budget holders directly and their decisions.
- Is payable to innovators with no CT liability so there is now a cash value for R&D investors with losses.
- May no longer reduce the UK tax charge for parent foreign tax credit calculations, thereby preserving the cash saving in the group.

Now	Dr	Cr
Cr: P&L tax charge		x
Dr: Balance sheet CT payable	x	

ATL credit	Dr	Cr
Cr: P&L R&D cost		x
Dr: Balance sheet CT payable	x	

- Accounting treatment is driven by the scheme design so results in ATL treatment regardless of the tax profile of the company.

Summary

R&D tax credits here to stay – Dyson Innovation Report

SME reliefs increasing – now up to 125% of qualifying spend

Large company ATL – tax repayments?

Many companies under claim R&D – PwC can help

Bigger R&D claim, larger patent box relief!