

FOCUS ON

# R&D tax relief - R&D expenditure credit (RDEC)

The Government is committed to encouraging research, development and innovation within the UK economy, to create an attractive regime for companies to develop and exploit intellectual property in the UK.

Research and development (R&D) has a much wider definition than many people think – remember that the Government wants your company to carry out R&D and it wants you to claim R&D tax relief!

RDEC can improve your company's profit margin and cash flow by reducing its operating costs and tax liability and, in some cases, by obtaining an additional tax repayment.

R&D tax relief is only available for companies – and there are two different R&D tax relief schemes depending on the size of your company. The RDEC scheme is available for large companies – those with either annual turnover of over

€100m, or a balance sheet figure of over €86m, and more than 500 employees.

## SME relief

The relief available to small and medium-sized companies (SMEs) is more generous – see our separate 'Focus on' sheet for more details – but is not available in certain cases. Where R&D expenditure is funded (either by a grant or by a different entity) or in certain cases where a large company has a stake in the business, SME relief is denied, however RDEC is available and therefore also relevant to SMEs.

## What relief is available?

RDEC can be claimed on the cost of employing staff who are directly or actively engaged in carrying out the R&D, the cost of the materials that are used in the R&D and on payments made to certain subcontractors (i.e those operating through unincorporated entities) that are assisting with the R&D.

The credit offsets the R&D cost above the 'operating profit' line at an 11% rate; that is, it will increase operating profits by 11% of the eligible costs. This credit is taxable and therefore, assuming a tax rate of 20% the cash benefit is 8.8%. For expenditure pre 1 April 2015, these figures were 10% of costs and 8%.

For a business that is not tax paying, either due to it being loss making, or it using up losses brought forward, a cash credit of 8.8p per £1 spend is available. This cash credit is limited to the amount of PAYE and NIC paid by the company during the period.

## Example

A company spends £20,000 on qualifying R&D. The company's profits will be increased by £2,200 and, with a tax rate of 20%, the tax payable is reduced by £1,760. Therefore, in addition to the standard tax relief for the expenditure, the total tax relief is £5,760 (£20,000 at 20%, plus £1,760). This means that the net-of-tax cost to the company of incurring the expenditure is £14,240 (£20,000 less £5,760).

If the company were loss making it would instead be able to claim a cash refund of £1,760.



“ *The tax relief available is generous, but claims must be properly made to ensure they meet HMRC requirements.* ”

### Transition

For expenditure incurred prior to 1 April 2013, R&D relief for large companies was provided by way of an enhanced tax deduction of 130%, i.e. it could reduce the amount of profits on which it paid tax by an additional 30% of the qualifying spend. For loss making companies, this would merely increase the losses carried forward – no cash credit was available.

The new RDEC initially worked alongside the existing R&D tax credit so that companies had the option to elect into the new regime or continue to claim the 130% deduction. For accounting periods beginning on or after 1 April 2016, this option was removed and RDEC is mandatory.

### What are the qualifying criteria?

What actually constitutes R&D is wide-ranging, but includes the development or improvement of a product or process - there must be a technological advancement and an attempt to resolve a technological uncertainty.

What is a technological advancement? It is not enough that your new product is commercially innovative; it must be an extension to the existing body of technological achievement or make an appreciable improvement to an existing process, device, product or service.

What is a technological uncertainty? It is the practice of taking a technologically feasible idea and turning it into a cost effective and reproducible process, device, product or service.

Note that a project does not have to actually achieve its aims to qualify for R&D tax relief.

R&D claims are commonly made by businesses in the engineering, pharmaceutical, healthcare, software development, energy-saving and biotechnology fields, but successful claims have also been made by some of our architect, manufacturing, design engineers and construction clients too!

### Can I get help to establish my R&D tax relief claim?

The tax relief available is generous, but claims must be properly made to ensure they meet HMRC requirements. HMRC will review all claims carefully – so it is important to work with experienced tax advisers to ensure any claim meets the necessary criteria.

Any business that wishes to claim R&D tax credits should consult with its accountants or professional advisers.

MHA MacIntyre Hudson has significant experience in preparing and submitting R&D claims in a wide variety of industries and has developed excellent relationships with the relevant inspectors at HMRC to enable claims to be agreed in the most efficient manner.

### Contact us

For further information, please contact our R&D tax relief specialist:



**Tom Byng**  
Partner

**E:** tom.byng@mhllp.co.uk  
**T:** 020 7429 4100



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