

Research & development expenditure credits: Large Company & Above the Line schemes

The R&D Scheme for Small and Medium Enterprises (SMEs) is well publicised as one of the most generous Corporation Tax reliefs currently available. However, despite meeting the necessary size criteria, many small and medium-sized companies that undertake qualifying R&D are unable to make to a claim under the scheme.

As part of the ongoing measure to promote enterprise and innovation in the UK, an increasing number of grants for R&D projects have become available from the UK Government and European Union. However, small and medium sized companies are prohibited from claiming relief under the SME Scheme for some subsidised R&D projects, as are SMEs undertaking subcontracted R&D on behalf of other enterprises.

All is not lost, however, as relief is instead available under the well established Large Company Scheme. Furthermore, Finance Act 2013 introduced a new 'Above The Line' scheme, which will, for the first time, see loss making large companies and SMEs undertaking subcontracted or subsidised R&D able to receive a payable credit.

Subsidised Expenditure

The type of funding a company receives for an R&D project will affect the extent to which they may be able to claim relief under the SME Scheme.

Where a company receives funding for an R&D project in the form of notified State Aid, the entire project will be ineligible for relief under the SME Scheme and relief will therefore need to be claimed under the Large Company Scheme.

Conversely, where funding for a project is received in the form a grant or subsidy that does not constitute notified State Aid, the expenditure is subsidised to the extent that it does not exceed the subsidy. As such, it may be possible to claim relief partly under the SME Scheme and partly under the Large Company Scheme for the same project.

Large Company Scheme

From 1 April 2008:

- Enhanced relief at 130% i.e. for every £100 of qualifying costs, a company could have its taxable profits reduced by an additional £30 on top of the £100 spent;
- No repayable tax credit for loss making companies;
- Qualifying expenditure must not be capital in nature and must be from one of the following revenue categories:
 - Staffing Costs – including gross salaries, bonuses, Employers' Class 1 NICs and pension contributions;
 - Consumables and Software – including water, fuel and power costs;
 - Externally Provided Workers – e.g. agency staff and staff employed by other group companies;
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- Relief is also available for expenditure on subcontracted R&D, providing the work is directly undertaken by:
 - o A Qualifying Body (a charity, an institution of higher education such as a university, a scientific research organisation or a health service body);
 - o An Individual; or
 - o A Partnership, each member of which is an individual.

Above The Line Scheme

From 1 April 2013, the Above The Line Credit was introduced to increase the visibility of R&D tax relief. Whilst this is currently optional, the Above the Line Scheme will become mandatory from 1 April 2016, entirely replacing the 130% enhanced-deduction scheme.

The Scheme does not alter the way qualifying activity is identified or how qualifying expenditure is calculated. It is only the method of giving the relief that has changed.

The credit, equal to 10% of qualifying R&D expenditure, will appear as additional pre-tax income in the company accounts. The company's Corporation Tax liability is then calculated on a higher taxable profit, but relief is given for the 10% credit against the Corporation Tax liability. This gives greater relief than under the existing enhanced-deduction scheme, so companies may wish to start using the scheme before it becomes mandatory.

For loss making companies, the credit is payable, subject to the following restrictions:

- The credit is first used to discharge the CT liability of the claimant company for the same accounting period;
- The balance is then subject to an adjustment that is available to discharge future CT liability;
- Any balance remaining is capped by the PAYE/NIC of the R&D staff, with no restriction for time spent on qualifying R&D activity. Any capped amount is carried forward and treated as an expenditure credit for the next accounting period;
- The amount remaining discharges the CT liability for any other period;
- If the company is a member of a group it may surrender any amount remaining for a corresponding accounting period;
- The payable credit element remaining is applied in discharging any other outstanding liability of the company to HMRC;
- The final amount remaining is payable to the company, subject to the company being a going concern.

Summary

This is a very brief outline of a complex relief. It is therefore important that a claim is put together carefully with suitable professional advice. Claims are made on the company's Corporation Tax Return, and must be made within two years of the end of the relevant accounting period.

If you would like to know more, please speak to The Ensors Corporate Tax team – www.ensors.co.uk/corporate-tax-team/

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