

BriefingNote

Research & Development (R&D) tax credits

Why are R&D tax credits important?

R&D tax credits provide potentially substantial tax incentives for companies that incur expenditure on research and development (see below). The tax benefits are different depending on the size of the company.

For SME's, from April 2011 for every £10,000 of qualifying expenditure incurred, the company can claim a deduction of £20,000 (previously £17,500) from its taxable profits. Additionally, loss-making companies can choose either to increase the value of their losses carried forward, or to surrender the tax credits in return for a cash payment. HMRC will repay £25 for every £100 of qualifying expenditure (up to the maximum of the PAYE, tax and National Insurance) paid over during the year.

Subject to EU State aid approval, a further enhancement of the relief has been announced. From 1 April 2012, the total deduction will increase to 225% and the cap on repayment by reference to PAYE paid will be removed.

For large companies, the claim is 130% of expenditure. Large companies are unable to surrender their tax credits for a cash payment.

What is R&D?

There is a lot of confusion over what constitutes R&D. Essentially you have to be doing something new to the market in a field of either science or technology where, at the outset, you are looking to resolve an uncertainty. That covers a lot of areas - see the reverse of this sheet for some examples.

What is a small or medium-sized company?

A company is small or medium-sized if it has less than 500 employees and either:

- An annual turnover of not more than €100 million (around £87 million – but check current rates), or
- Total assets on its latest balance sheet of not more than €86 million (around £75 million, but again check current rates).

The company must also not be owned 25% or more by companies which are themselves not small or medium sized for these purposes.

Which costs qualify for R&D tax credits?

All companies can claim R&D tax credits on the costs of:

- Employing staff for R&D.
- Consumables used for R&D.
- Certain costs of subcontracting R&D (although the claim is restricted on such costs).

Large companies may also be able to claim relief for expenditure on 'independent research'.

When do these costs not qualify?

Costs do not qualify if:

- They amount in total to less than £10,000 in one year, or
- They are met by another organisation.

There are two additional tests for small and medium-sized companies. Their costs do not qualify if:

- They are part of a project which receives state aid, or
- Before 9 December 2009, the company did not own the rights to the intellectual property resulting from the R&D.

	£
Qualifying labour costs (including pension and Er's NIC)	120,000
Qualifying direct costs	75,000
Attributable overheads	<u>30,000</u>
	225,000
Marginal tax rate 27.5%	
Potential reduction in CT liability	<u>£61,875</u>

Research & Development – the unusual

Here are just a few examples of where we have agreed with HMRC that tax relief is due under the R&D provisions. These are not necessarily businesses that are typically regarded as being in the R&D area.



Making balloons and bunting
- looking to mechanise and streamline processes.



Tuning cars to improve performance
- software, brakes, suspension, etc.



Time spent on improving processes for waste disposal.



Developing new, more environmentally friendly, sandwich packs.



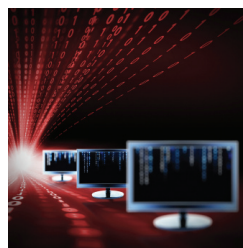
A company that has created a new light bulb.



Creating new food coating and marinades by taste, ingredient, meat type and customer.



Customising emergency vehicles in terms of interior specification, animal crates, safety features, etc.



Bespoke software development
- developing your own software including the changes you make to an 'off the shelf' package.

For further information, please contact **Cathy Corns (Tax Partner)** on **01908 605552**, or alternatively email **cathycorns@mercerhole.co.uk**.

This Briefing Note is a short selection of items extracted from complex legislation. Further specific advice on any matters referred to must be taken at all times. The information is given for general guidance only and publication is without responsibility for loss occasioned to any person acting or refraining from acting as a result of the information given. No part of this publication may be reproduced without the prior permission of Mercer & Hole.

St Albans

T: +44 (0)1727 869141
stalbans@mercerhole.co.uk

London

T: +44 (0)20 7353 1597
london@mercerhole.co.uk

Milton Keynes

T: +44 (0)1908 605552
miltonkeynes@mercerhole.co.uk