

RESEARCH & DEVELOPMENT TAX RELIEF IN MANUFACTURING INDUSTRIES

Is your business making the most of this relief?



The Government continues to support innovative businesses by encouraging companies to apply for R&D tax relief and by increasing rates of relief

Manufacturing

The current economic climate is placing huge demands on UK manufacturing to be more competitive, to develop new and innovative products in shorter timeframes and to improve the efficiency of manufacturing processes. In addition, manufacturing companies are having to meet the increasing demand of customers for lower prices and comply with the demands of the regulatory and environmental bodies.

The UK R&D tax regime is part of the Government's strategy to raise overall levels of R&D and improve long term productivity growth rates. It provides incentives to encourage manufacturers to retain their operations in the UK.

What is R&D?

R&D is broadly defined for these purposes as activities carried out that "seek an advance in science or technology, through the resolution of scientific or technological uncertainty".

Though new product development is clearly an area to explore, experience is showing that the definition of R&D for tax purposes can be met in activities outside of the R&D team such as manufacturing, production operations and testing and trialling departments. Examples of areas which may potentially contain eligible R&D:

- Introduction of new or alternative materials to replace and improve existing materials;
- Improvements to manufacturing processes to improve quality, reduce waste and shorten manufacturing times;
- Scaling one off trials to full scale experimental trials on production volumes;

- Technical problem solving by engineers or technicians that is over and above routine troubleshooting;
- Developing tooling for new materials or processes.

What is the benefit?

There are two regimes for R&D relief, the SME scheme and the Large Company scheme.

SME scheme

Under the SME scheme, the benefit is delivered as an enhanced deduction that reduces taxable profits/increases trading losses, or alternatively a cash tax 'credit' can be claimed.

Companies can claim under the SME scheme provided the company or group has:

- Fewer than 500 employees and either
- Turnover of less than €100m, or
- Gross assets of less than €86m.

Qualifying expenditure incurred on or after 1 April 2012 will qualify for enhanced R&D tax relief at 225% (i.e. 125% beyond the original P&L deduction). Qualifying expenditure incurred on or after 1 April 2015 will qualify for enhanced tax relief at 230%. The value of the tax credit is:

Date of claim	Pre 1 April 2014	Post 1 April 2014	Post 1 April 2015
Credit rate	11%	14.5%	14.5%
Value of credit per £ of R&D spend	24.75p	32.62p	33.35p

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Large company scheme

For costs incurred after 1 April 2013, two schemes run in tandem - the legacy scheme and the new R&D Expenditure Credit (RDEC) scheme.

Under the legacy scheme qualifying expenditure will benefit from R&D relief at 130% with no availability of a payable credit.

Large company scheme - to RDEC or not to RDEC for pre 1 April 2016 expenditure?

The time limit to make a R&D claim is two years from the end of the accounting period. With the two reliefs running in parallel until April 2016 (when the legacy relief ceased) companies face the decision of when to 'opt in' to the RDEC regime.

For most companies, the decision is simple:

- The RDEC offers a higher rate of relief (7.9% vs 6.3%) based on a corporation tax rate of 21%. After 1 April 2015, this increased to 8.8% based on the future tax rate of 20%.
- The RDEC will increase the company's EBITDA by 10% of qualifying expenditure (11% after 1 April 2015).
- The RDEC offers a payable credit to loss making companies.

There will, of course, be other factors to consider which we can assist you in navigating, but the opportunity is clear.

Steps to make a claim

1. Scope your claim

When preparing and submitting a claim for R&D tax relief, the key is to really look at what the company does. This will include engaging with other areas of the business, particularly technical staff, to ensure the claim is correctly scoped.

2. Design your methodology

You need to design a methodology that avoids using significant internal resource to provide details of qualifying costs and activities.

3. Submit with a supporting report

The claim is made within a company's tax return, but we recommend that this is supported by a self-contained report that explains the nature of the work on which a claim is being made and addresses the questions that HMRC typically ask.

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R&D submissions from your team are head and shoulders above those that we see from other firms - 99.9% of submissions are agreed without question.

SENIOR INSPECTOR
HMRC - R&D Unit

Our experience of working with HMRC since the relief was introduced, and more recently through representation on the consultative committees, means that we know what HMRC are expecting to see from a claim and ensures that we minimise the risk of lengthy enquiries after submission of the claim.

Where BDO make the difference

Since the relief was introduced in 2000, BDO has built close relationships with the HMRC local specialist teams and has seen a real shift in their focus from the early days when agreeing a claim was a very arduous task.

The local R&D Inspectors have been trained to actively support claims from companies undertaking R&D and our experience has been that HMRC have become increasingly knowledgeable of the relevant industries.

With the focus of the guidance becoming increasingly complex, it is crucial to involve an R&D specialist at an early stage to ensure that the relief is maximised.

From recent discussions with R&D Inspectors, we understand HMRC is toughening its stance on record keeping and looking to use the existing penalty regime where adjustments are subsequently made. This reinforces the need for a robust, supportable methodology.

How can we help?

BDO can assist you in identifying and claiming R&D tax relief. We have strong working relationships with the local HMRC specialists and through our detailed understanding of the legislation we can help you maximise the benefit of a claim. Our pragmatic, commercial approach helps capture all the relevant information required without taking up excessive management time.

Next steps

If you would like more information in relation to the availability of R&D tax relief, please contact your usual BDO contact or a member of the local R&D team listed overleaf.



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