

Understanding Research and Development (R&D): What It Is and what are the recent changes – Provided by Sempar and accurate as at 16.09.2024.

When a company embarks on a journey of innovation, it often turns to Research and Development (R&D) to achieve advancements in science or technology. While many people visualise R&D as taking place in a lab filled with test tubes and sophisticated machinery, its scope extends far beyond that. In fact, R&D encompasses any effort aimed at improving products, processes, or technologies across various industries.

What Is R&D?

R&D refers to a company's pursuit of new knowledge or technology to advance its industry. This could involve developing a new product, refining an existing process, or exploring new scientific principles. For a project to qualify as R&D, it must address scientific or technological uncertainties and seek advancements beyond the company's existing knowledge base.

The Evolution of R&D Tax Relief

Tax relief for R&D activities has undergone significant changes in recent years, affecting how businesses can benefit from these incentives. Historically, there were two main schemes:

1. **The SME Scheme:** Designed for small and medium-sized enterprises (SMEs), this scheme offered substantial relief for qualifying R&D expenditure.
2. **The RDEC Scheme:** Primarily used by larger companies that did not meet the criteria for the SME scheme, this was a tax credit scheme providing support for R&D activities.

However, from 1 April 2023, the SME scheme was revised, reducing the tax relief available. The effective tax relief for profit-making companies decreased from 24.7% to 21.5%, while for loss-making companies, the tax credit dropped from 33.4% to 18.6%. Alongside this, the RDEC scheme also saw changes.

In April 2024, both schemes were merged. For accounting periods starting from 1 April 2024, the effective tax rate is approximately 15.5%, and the tax credit is around 16.2%. Companies classified as R&D intensive (those where over 30% of total expenditure is on R&D) can still access tax credits comparable to those available before April 2023.

Qualifying Costs for R&D

Understanding what qualifies for R&D tax relief is crucial. The most common eligible costs include:

- **Employment Costs:** Salaries, employer's National Insurance Contributions (NICs), and pension contributions for employees directly involved in R&D.
- **Agency Workers:** Costs associated with agency staff working on R&D projects.
- **Other Expenditures:** Costs for software, consumables, and subcontractor services.
- **New Categories:** Recently, costs related to datasets and cloud computing have been added. Pure mathematics is also eligible for relief from accounting periods beginning on or after 1 April 2023.

How to Make a Claim

To claim R&D tax relief, you need to include it in your corporation tax return and submit a disclosure to HMRC via the government website. If you haven't claimed before or if it's been a while since your last claim, you must notify HMRC of your intention within six months following the end of your accounting period.

Addressing Recent Concerns

Recent scrutiny around R&D claims has been heightened due to increased reviews by HMRC. Historically, HMRC did not extensively review claims, leading to some advisors claiming for business improvements rather than genuine R&D. With recent investigations, particularly focusing on software claims by small and medium-sized firms, many businesses have faced rejected claims.

Unfortunately, the industry has seen unscrupulous advisory firms taking advantage of the lack of regulation and HMRC's initial reluctance to investigate thoroughly. Given the current climate, it's essential to work with trusted advisors who can help ensure that your R&D claims are legitimate and well-supported.

In conclusion, while R&D remains a powerful tool for innovation and business growth, navigating the evolving landscape of tax relief requires careful attention. Staying informed and partnering with reliable advisors can help you maximize the benefits of your R&D investments.