

Research and Development Consultative Committee Minutes

Thursday 24th September 2019

Venue: HMRC office, 100 Parliament Street, London, 1pm – 4pm

Present: Yasmin Achha(YA), Justin Arnesan, Peter Azu, Mike Baker, Gavin Bate, Ian Batkin, Oliver Batt, Dave Beatty, Christopher Brown, Tommy Brown, Angela Browning, Simon Bulteel, Steve Burgen, Iain Butler, David Byrne, James Clark, David Clift, Vanessa Cooper, Mike Crabtree(MC), Emma Craig – West, Ian Davie, James Davies, Caroline D’Cruz (CDC), Mike Dean, Jeff Drennan, Laura Duggan, Kerry Eglington, Mark Evans, Sue Fawkes(SF), Patrick Fletcher, Chrissie Freear, Rowan Gallagher, Ron Gibson, Jasmine Grieve, Philip Hamblin(PH), David Harris , Chris Harrison, Kathy Haunton, Thomas Hayden, Coleen Hillicks, Nigel Holmes, Keri Hopkins, Darryl Hoy, Remy Hussein, Zakir Hussain(ZH), Ramesh Jethani, Maria Kitt, Chris Knott, Anthony Lalsing, Steven Levine, Matthew Lewis, Richard Lewis, Paul Mann, Simbarashe Mareverwa, Alexis Marx, Julia May, John Moore, Ian Moss, John Moxon, Julia Neate, David O’Keefe, Deepash Patel, Shoayb Patel, Jeremy Coker, Mike Price, Makhan Ram, Stuart Rogers, Faye Ruffles, Hari Sandhu, Margaret Savory, Rosie Silk, Mark Smith, Justine Stalker, Weronika Swietch, Hannah Swindell, Neil Taylor, James Tetley, Jenny Tragner, Richard Turner, Tim Walsh, Jing Jing Wang, David Ward, Samantha Webb, Stuart Weekes, Gary Weinstein, Steve Williams (SW)

All the slides which were used during this section of the meeting are being published, please read these minutes in conjunction with those slides.

1. Introductions

MC introduced himself and the delegates, thanking them for their attendance. He noted that members of other government departments were present, as well as other stakeholders such as professional bodies.

MC provided a brief update on BREXIT and that the political landscape was very fluid. He also touched on how much the volume of claims has increased over the past few years and the challenges that brings around turnaround times and compliance.

2. Policy Update

YA provided an update on:

Consultation

To tackle fraud and abuse, Budget 2018 announced the payable credit for loss-makers in the SME R&D scheme would be capped at three times the company's PAYE and NICs liability. We committed to consult on how the cap would be applied, to minimise the impacts on genuine UK businesses and proposed some options and test their effectiveness. These included:

1. Threshold - We asked what level the threshold should be applied at and views on restricting 1 claim per year for any given group of companies under common control.

2. Group or Connected Party PAYE and NICs liability – We asked whether this feature would be beneficial and whether it added any complexity or admin burden.

Amalgamating PAYE/NICS within a group or connected company (whether it was subcontracted or EPW provided by it)

3. Carry forward losses – We asked about the benefits of carrying forward losses to help bank PAYE/NICS and whether 2 years was deemed appropriate.

The Consultation ran between 28th March 2019 – 24th May 2019 and we received 87 responses – from a wide range of stakeholders.

YA thanked the delegates for their feedback and provided a summary of what the responses looked like.

Based on consultation responses the policy is being refined to support companies affected by the PAYE cap and we are considering these in the final policy design.

Anything we consider will need to be compliant with EU State aid, Free Movement of Capital and Freedom of Establishment rules.

Response to the consultation will be published at the next budget. No concrete dates at present and will update via the RDCC mailbox.

Advance Clearance Pilot (ZH)

The pilot was introduced to provide greater certainty to customers who are RDEC claimants, this was the result of feedback received from interviews carried out with large businesses.

Pilot group of 12 customers from a variety of sectors with differing claim sizes, claiming on different types of R&D to broaden our sample.

Some customers have been issued a clearance via our non-statutory clearance method for three years.

Discussion around which three years we are talking about, and to clarify it is three Accounting Periods from the initial claim – so the first year of clearance is the CY, then it is CY +1 and CY+2. So in total three years.

The areas of clearance has been confined to claim methodology, however we have opened this up to areas of uncertainty:

- Mostly received clearance requests on methodology
- Seen a clearance request for an unorthodox EPW arrangement

- Seen a potential request on types of qualifying IT expenditure

Had our first claim refusal, which makes it interesting as the pilot has essentially protected the exchequer.

As the claim cycle progresses and further pre-filing discussions take place, we can see the benefit of the Advanced Clearance pilot, therefore pushed the first evaluation back to March 2020 where our social researches will interview CCMs within LB and case teams to ascertain how useful the clearance scheme actually is in practise.

EU Exit and R&D Tax credits

YA pointed out that there are no current plans to change the regimes. The SME scheme is a notified State Aid and there will continue to be some form of subsidy control. The U.K's departure from the EU should not have any direct effect on tax reliefs. They are embedded in U.K'S legislation and paid out by HMRC.

R&D National Statistics 2019

YA explained the publication date is later than usual as further improvements are being made to data-sources and processing. Statistics to be published on 10th October 2019.

Annual statistics include information about the number of claims for R&D tax credits and the associated cost to the Exchequer. October's release will include data for accounting periods up to 2017-18, although the latest year's data is still partial and will be revised in next year's publication.

The commentary and tables include –

Number and cost of R&D tax relief claims and associated expenditure - The number of claims is based on the date that the accounting period covered by the claim ends. The figures are based on claims for R&D tax credits made by companies in Company Tax returns received on or before 30 June 2018.

Breakdowns by region - Regional allocation is based on the postcode of the company's registered address, which might not correspond to where the R&D activity takes place, so caution must be exercised when interpreting these figures.

High-level SIC sector - Industry sector is based on primary SIC2007 coding of registered company. This coding might not correspond to the industry sector of the R&D activity, so caution must be exercised when interpreting these figures.

Supplementary tables - with more detailed regional and sectoral breakdowns will be published in Spring 2020. These statistics will expand on the information in the R&D tax credit national statistics, providing granular detail by claim size and geographic region in response to feedback from users.

R & D Evaluation report – Her Majesty's Government formally committed to providing an independent evaluation of the aid scheme to the European Commission to secure the EC's

approval to extend the scheme until 2020. This approval was conditional on the successful delivery of an independent evaluation.

Findings are being analysed and report will be published in due course.

Information Sources

YA talked through some of the information sources available as below:

R&D guidance – This serves as a one stop shop of links to different elements of R&D, depending on circumstances and what you want to know.

CIRD – Corporate Intangibles Research and Development manual - Can be found at CIRD80000

Company Taxation Manual - includes all aspects of company taxation. Can be found at 90000 CTSA.

The Business Income Manual - Supplementary guidance on how to check tax calculations or work out the trading profits of a business for Self - Assessment tax return

Appeals, Reviews and tribunals Manual. All available on GOV.UK. They contain guidance prepared for HMRC staff and are published in accordance with the Freedom of Information Act 2000 and HMRC Publication Scheme.

YA pointed out that guidance, is guidance – it's not comprehensive and does not provide a definitive answer in every case. It is based on the law as it stood when published.

Agent Updates - give guidance and news for tax agents and advisers. Published every 2 months on GOV.UK. The latest publication was a 'BREXIT' special published on the 16th September.

Send HMRC your details if you want them to email you when a new edition of an Agent Update is published.

YA advised the delegates that when relying on HMRC products on-line, they use the official HM Gov. products as information can become out of date very quickly, for example, agents may have put videos on you tube, which are out of date.

3. WMBC - Insight, Growth & Risk

SF explained the position on processing claims.

30th September 2019 –

- Target date to bring backlog up to date
- Date that processing of R&D claims – Payable Tax credit, RDEC move out of WMBC(Wealthy and Mid-Sized Business Compliance to BT&C where enhancement only are already being handled

Movement of Claims Processing to Business Tax & Customs

CT Services is responsible for all activities associated with the processing of Company Tax Returns filed online and on paper. This helps ensure companies pay the correct amount of CT at the right time.

A key function is to ensure that the CT database (COTAX) holds the correct information about corporate customers. CT Services also handle a range of correspondence and queries, including UK residency certification, dormancy, liquidations, potential strike offs, penalty objections and appeals, repayments, return amendments, claims for loss relief.

- Current claims will be processed by BT&C preventing a similar backlog from building up again
- General queries will be handled by BT&C - CT helpline
Contact number changing within CIRD
- Emails will be routed through BT&C
- Agent update

WMBC Insight Growth & Risk

- Claims up to 30/9/19 will remain and be cleared by IGR staff
- Payment security checks and compliance will remain within IGR
- Technical call backs will be made by IGR staff

28 days on hand

- Regular updates for recovery plan have been shared
- Huge effort gone into clearing outstanding claims
- Already planning to move work into BT&C where larger volume of staff available to manage peaks and flows of claims received
- Additional WMBC staff drafted in from outside of IGR
- Additional staff within IGR moved onto work short term
- Large Business staff assisted greatly to bring RDEC in line with PTC turnaround
- BT&C staff trained up as well as staff from WMBC

Forward look for R&D teams

PTC & RDEC claims will be handled in Cardiff

Enhanced Expenditure claims within other BT&C CT teams

WMBC resources will no longer be processing claims and handling calls which move into BT&C

Compliance work and payment security work will be handled in IGR

4. Agent Strategy(CDC)

CZ, head of Agent policy provided an update on Professional Bodies (PB), how they abide by written codes of conduct and that they follow similar disciplinary procedures.

CZ talked through the Professional Conduct in Relation to Taxation (PCRT) and explained that it sets out what the signatory PB'S expect of their members. She further explained the HMRC Agent standards and set out what Agents are expected to do

A representative from the CIOT (David O'Keeffe) updated the delegates on work around professional standards which he is leading on. David is chairing a CIOT sub –committee to help deliver guidance for agents dealing with R&D claims. They have drafted terms of reference and kicked off the process of drafting a guidance note.

Large Business

SW talked through the claim numbers in large business during 2019/20 including the RDEC claim value.

SW explained the position with processing time and the average number of days to process RDEC claims in LB is 33 days.

Sectors – LB compliance effort remains fairly spread across all trade sectors.

Software claims – SW informed the committee that LB and WMBC continue to use CDIO to support case teams for enquiries related to R&D software projects.

SW reinforced the position on turnaround times highlighting LB's support to bring the claims up to date by 30th September

Digital Form Update – SME version was launched in February 2019 followed by the RDEC in May2019. Numbers received are slow, though increasing.

5. Technical update

a) Dispersed R&D.

PH explained that the above issue was both created and identified when the Large Company scheme was introduced in 2002, and that in the same year legislation covering the situation – but only in some situations- was enacted.

Activities which are routine may be excluded from qualifying as R&D (for example by paragraph 12 of the BEIS Guidelines) but do qualify by virtue of another part of the guidelines (for example testing, paragraph 27. c. of the BEIS Guidelines). When this part of the R&D project is subcontracted to another company that company cannot claim it (it is not their relevant R&D). This feature was irrelevant in the Small and Medium Size company scheme as the company undertaking the R&D and which had subcontracted it to another company could include the qualifying element of that expenditure in their own claim as subcontractor costs. But when the company which is undertaking the R&D is making a claim in (now) the Research and Development Expenditure Credit scheme neither they (if the expense does not fall within s104E, s104H, s104J CTA 2009) or the company to which the R&D was subcontracted (for the reason stated above) can include that element of the R&D project in a claim.

b) S104W CTA 2009

As mentioned above legislation was enacted in 2002 which dealt with the dispersed R&D point in some situations. At the time the rules were found in paragraph 14 of Schedule 12 FA 2002 but they are now found in s104W CTA 2009.

The rules only apply to groups (it's the worldwide group) and only when one company in the group (company 'A' in the legislation) sub-contracts the activity directly to another company in the group (company 'B' in the legislation). It is the company to which the activity was subcontracted which can make the claim, and the legislation at s104W enables that company to make the claim because it treats (as far as would not otherwise be the case) the activities carried out by company A as having been carried out by company B for the purposes of Chapter 6A of Part 3 CTA 2009.

With Chapter 6A of Part 3 CTA 2009 applying to company B the subcontractor rules at s104E, s104H, s104J CTA 2009 apply, meaning that it is only in limited situations that any activity subcontracted out by company B it will be qualifying expenditure for the purposes of Research and Development Expenditure Credit.

c) The SME Test

Adjusting the figures for the s1120 (2) *qualification 1* CTA 2009 changes article 2(1) of the Commission Recommendation 2003/361/EC reads;

'...enterprises which employ fewer than 500 persons and which have an annual turnover not exceeding €100 million, and/or an annual balance sheet total not exceeding €86 million.'

HMRC's view of the above is that there are two tests.

First, is the result of applying the staff test that there are under 500? If it is not that is the end of the matter, the company to which the test is being applied is not an SME for the purposes of the SME R&D relief. If, however, the result is less than 500 it is necessary to move onto the second test.

If we get as far as the second test we look at the annual turnover figure and balance sheet total. If this results in an annual turnover in excess of €100m and a (gross) balance sheet total in excess of €86m then the company is not an SME for the purposes of the SME R&D relief. If this results in an annual turnover of €100m or less or a (gross) balance sheet total of €86m or less then the company is an SME for the purposes of the SME R&D relief.

d) Claims by a corporate member of a partnership.

S1259 CTA 2009 allows partnerships to calculate their profits according to the CT rules as though the partnership were itself a company, meaning that adjustments are allowed. This means that as long as the other conditions for SME relief are met the partnership can (as

allowed by the 'authorised by law' element of s46 (1) CTA 2009) take the R&D Relief. Flowing from this the proportion of the resultant losses or profits which are applied to a corporate member will reflect their share of the SME R&D Relief. Since s1259 only extends to calculating the profits of the trade it does not encompass the legislation which allows SME's to claim Payable Tax Credit, meaning that a claim for Payable Tax Credit cannot be made by the corporate partner.

Since RDEC is an adjustment authorised by law in calculating a company's profits for corporation tax purposes (s104A (1) CTA 2009) the appropriate proportion of RDEC is incorporated in the corporate partners share of the profit or loss of the partnership. The corporate partner has to claim the RDEC in the usual way in its CT600.

Guidance on the above can be found at pages 81220 (for claims within the SME scheme) and 89850 (for claims within the RDEC scheme) of the Corporate Intangibles Research and Development Manual.

e) The Employer Allowance

A delegate queried whether the new Employer Allowance was a notified State aid and the effect of the allowance on claims for R&D relief. PH advised that he had, recently, checked with the colleague who introduced the relief and was advised that it was not a notified State aid. One delegate had been told that this was the case but that the status would be changing next year. PH undertook to check this point, and did so immediately after the meeting. He can therefore use these notes to confirm that the Employer Allowance is not a notified State aid and that there is no expectation that it will ever become one.

Given the above the information provided to the delegates at the meeting was correct. Receipt of Employer Allowance would not mean that the s1138 (1) (a) CTA 2009 rules are applied.

However, the nature of the relief is that an element would represent a subsidy under s1138 (1) (b) CTA 2009 meaning that that element (generally a fair and reasonable apportionment) must be excluded from R&D claims. A delegate correctly pointed out that the nature of the relief means that the amount is not paid, meaning that the payment condition at s1123 (2) CTA 2009 is not met so that amount cannot form a part of a Research and Development Relief claim because of s1138 (1)(b) and also cannot form a part of an Research and Development Expenditure Credit because of s104Y(2) and s1123(2), both CTA 2009. PH, thanked that delegate for her timely intervention!