HM Revenue
& Customs

Targeted anti-avoidance loss buying rules: exclusion of Research and Development Allowances

Who is likely to be affected?

Non-trading companies that have incurred capital expenditure on research and development, and those buying such companies in whose hands the expenditure will qualify for Research and Development Allowances (RDAs).

General description of the measure

In Finance Act 2013 (FA 2013) the Government introduced, as a new Part 14A of Corporation Tax Act 2010 (CTA 2010), targeted loss buying anti-avoidance rules to bring the tax treatment of unrealised losses more closely into line with the longstanding treatment of realised losses by restricting their set-off against other profits (including by group relief). This measure will exclude RDAs from Part 14A CTA 2010.

Policy objective

The anti- loss-buying rules had a more significant adverse impact on RDAs than intended. The rules catch situations where a company does preliminary capital work in the furtherance of research and development, but does not reach the point of trading, and then is sold on to trading groups. Before the rules introduced by FA 2013 the trading groups could claim the Research and Development Allowances under Part 6 Capital Allowances Act 2001 (CAA 2001).

Although these rules contain an avoidance motive test their introduction has caused uncertainty and risks undermining capital investment in research and development.

Background to the measure

Representations were made by business following the introduction of the Budget 2013 loss buying rules, and the measure was announced at Budget 2014 following informal consultation.

Detailed proposal

Operative date

This measure will have effect for ‘qualifying changes’ within Part 14A CTA 2010 occurring on and after 1 April 2014.

Current law

Disallowance of deductible amounts

The anti- loss-buying rules within Part 14A of CTA 2010 apply where there has been a ‘qualifying change’ in relation to a company. It restricts the use of ‘deductible amounts’ against total profits within the company, or as group relief outside the company, and restricts any use of those amounts within the company (or one connected to it) following the transfer of profits to that company. There is an avoidance motive test so that the rules will only apply where the main purpose, or one of the main purposes, of the arrangements is to utilise the deductible amounts.

A ‘qualifying change’ is a change in the company’s ownership meeting one of the conditions in section 212C of CAA 2001.

Under section 730B ‘deductible amounts’ covers expenses of a trade or UK or overseas property business, management expenses of an investment company, and non-trading debits from loan relationships, derivative contracts or intangible fixed assets.

Research and Development Allowances

RDAs are defined in Chapters 1 and 2 of Part 6 of CAA 2001. RDAs are available as a 100 per cent allowance within the period for capital expenditure incurred by a person on research and development directly undertaken by him or on his behalf if he is carrying on a trade connected with the research and development or (importantly) after incurring the expenditure he sets up and commences a trade connected with the research and development. An expense crystallising as RDAs would form part of the ‘deductible amounts’ of a company.

Proposed revisions

Legislation will be introduced in Finance Bill 2014 to amend the definition of ‘deductible amounts’ in section 730B of Part 14A of CTA 2010 to exclude expenditure that crystallises as RDAs.

There will be no amendments to the RDA rules themselves.

Summary of impacts

<table>
<tr><td rowspan="3">Exchequer impact (£m)</td><td>2014-15</td><td>2015-16</td><td>2016-17</td><td>2017-18</td><td>2018-19</td></tr>
<tr><td>negligible</td><td>negligible</td><td>negligible</td><td>negligible</td><td>negligible</td></tr>
<tr><td colspan="5">This measure is expected to have a negligible impact on the Exchequer.</td></tr>
<tr><td>Economic impact</td><td colspan="5">The measure is not expected to have any significant economic impacts.</td></tr>
<tr><td>Impact on individuals and households</td><td colspan="5">There is no impact on individuals because this measure only affects companies.</td></tr>
<tr><td>Equalities impacts</td><td colspan="5">No equalities impacts have been identified because this measure only affects companies.</td></tr>
<tr><td>Impact on business including civil society organisations</td><td colspan="5">This measure is expected to have no impact on administrative burdens of businesses or civil society organisations

For companies involved in pre-trading activity who make capital expenditure on research and development this will preserve the value of their investment on the sale or partial sale of the company.

For those who rely on the preliminary capital research and development work of unconnected companies this will enable them to benefit from the expenditure made on their behalf.

There will be no amendments to the RDA rules themselves.</td></tr>
<tr><td>Operational impact (£m) (HMRC or other)</td><td colspan="5">There will be no significant impact on HM Revenue & Customs.</td></tr>
</table>

Other impacts	Small and micro business assessment: the impact of this measure on small and micro businesses is not anticipated to differ from that on large businesses. Other impacts have been considered and none have been identified.

Monitoring and evaluation

This measure will be kept under review through communication with affected customer groups and their industry bodies.

Further advice

If you have any questions about this change, please contact James Konya on 03000 544525 (email: james.konya@hmrc.gsi.gov.uk).