



The Research & Development Expenditure Credit

OVERVIEW

As part of its strategy to continue its encouragement of R&D activity, the government has introduced a new and enhanced method for large companies to receive corporation tax relief on qualifying R&D activity.

The Research & Development Expenditure Credit ('RDEC'), formerly known as the 'Above The Line' Credit, enables a company to claim a 10% tax credit, increasing to 11% from 1 April 2015, on qualifying R&D spend, which can be used to reduce its corporation tax liability or, if no liability, repaid in cash.

The RDEC is designed to allow the tax credit to be recognised 'above the line' in the financial statements, with the intention that this will encourage companies to consider the post-tax financial benefit of R&D in planning budgets and assessing performance.

The introduction of the RDEC scheme does not change the definition of R&D or the range of expenditure qualifying for tax relief.

The RDEC scheme becomes mandatory from 1 April 2016. Until then, companies can choose whether to use the RDEC scheme or to use the existing large company scheme.

What is the benefit of the tax credit?

From 1 April 2015, the tax credit is 11% of the qualifying R&D spend. This tax credit can be used to offset a company's corporation tax liability or, if no liability exists, can be repaid directly to the company.

Also from 1 April 2015, a single corporation tax rate of 20% will apply to all profits of all UK companies, including the tax credit. Therefore the post tax benefit of the 11% tax credit will be 8.8% from 1 April 2015.

Examples

(a) Profit making company

| | RDEC scheme (£'000) | Large company scheme (£'000) | No claim (£'000) |
|-------------------------------------|---------------------|------------------------------|------------------|
| Turnover | 2,400 | 2,400 | 2,400 |
| R&D expenditure | (1,000) | (1,000) | (1,000) |
| Enhanced R&D deduction | - | (300) | - |
| Tax credit @ 11% | 110 | - | - |
| Other expenditure | (1,000) | (1,000) | (1,000) |
| Taxable Profit | 510 | 100 | 400 |
| Corporation tax @ 20% | 102 | 20 | 80 |
| Tax credit | (110) | - | - |
| Tax payable/(repayment) | (8) | 20 | 80 |
| Tax saved compared to no R&D relief | £88 | £60 | - |

Business Tax Guide

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(b) Loss making company

| | RDEC scheme (£'000) | Large company scheme (£'000) | No claim (£'000) |
|-------------------------------------|---------------------------|---------------------------------------|---------------------|
| Turnover | 1,400 | 1,400 | 1,400 |
| R&D expenditure | (1,000) | (1,000) | (1,000) |
| Enhanced R&D deduction | - | (300) | - |
| Tax credit @ 11% | 110 | - | - |
| Other expenditure | (1,000) | (1,000) | (1,000) |
| Tax adjusted loss (carried forward) | (490) | (900) | (600) |
| Repayable tax credit | 88 | - | - |
| Tax withheld and carried forward | 22 | - | - |
| Tax value of loss carried forward | 98 | 180 | 120 |
| Tax value of losses and R&D relief | £208 | £180 | £120 |
| Tax saved compared to no R&D relief | £88 | £60 | - |

As illustrated above, a loss making company making a claim under RDEC on R&D expenditure of £1million would receive an £88,000 cash payment. In addition, £22,000 of tax withheld by HMRC is carried forward to set-off against future corporation tax liabilities. Thus, the net benefit to the company (assuming it has a future corporation tax liability) is £110,000. By comparison, under the existing R&D rules, the enhanced loss carried forward of £300,000 results in the lower corporation tax saving (£60,000), available only at some undefined future date. Should the loss making company not return to profit (and assuming no ability to claim group relief) then under the large company scheme the benefit of the losses will be wasted. The significant advantage of the RDEC scheme, (in addition to the enhanced R&D credit) is that monies are refunded and retained by the company, even in the absence of actual corporation tax liabilities.

Claiming RDEC

As under the current system, RDEC is administered through the corporation tax system. Therefore, claims to RDEC will continue to form part of the company's tax return. R&D tax credits can continue to be claimed retrospectively, up to two years following the end of an accounting period to which the claim relates

How can Rawlinson & Hunter help?

Rawlinson & Hunter can assist in identifying whether a project will qualify for R&D relief, and can prepare a detailed R&D tax report for submission to HMRC in order to claim the relief. We will assign a member of our team to liaise directly with HMRC on the R&D claim, and they will work to resolve any queries as they arise, and seek to secure the success of the claim.

Many companies miss out on claiming R&D relief because they do not fully identify those activities or costs which qualify for the relief. If you would like to find out whether and to what extent your company and activities may be eligible, or you wish to reassess your current claims process, please contact your usual R&H contact, Craig Davies or Andrew Shilling.

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