About ICAS

The Institute of Chartered Accountants of Scotland ("ICAS") is the oldest professional body of accountants. We represent around 20,000 members who advise and lead businesses. Around half our members are based in Scotland, the other half work in the rest of the UK and in almost 100 countries around the world. Nearly two thirds of our members work in business, whilst a third work in accountancy practices. ICAS members play leading roles in around 80% of FTSE 100 companies. ICAS is also a public interest body.

General Comments

ICAS welcomes the opportunity to comment on the HMRC consultation document ‘Improving access to R&D tax credits for small business’. The relief has been claimed by many companies – both small, medium and large – and has become a feature of the UK corporation tax landscape. However, in the course of our work we still come across companies who are not aware of the scope of the relief and the precise methods for making a claim. As noted in the Consultation Document there is still a challenge for HMRC to make sure companies are aware of the relief.

The position for small and medium-sized companies is complicated by the fact that these businesses are able to make claims both under the SME scheme in chapter 2 of Part 13 CTA 2009 as well as claims under Chapter 3 (R&D work contracted to the company) and Chapter 4 (R&D expenditure subsidised through State Aid) of that legislation. In effect the relief is more complex for small and medium-sized companies than for larger companies.

The Consultation Document itself indicates how complex the rules are in section 2 which notes that tax legislation sets out what activity qualifies as R&D and then notes that what counts as R&D is covered in guidance from the Department for Business Innovation and Skills. Companies and their advisers have two sets of definitions to get to grips with – tax legislation on BIS guidelines.

ICAS welcomes the introduction of an advanced assurance service for small companies making their first claim for R&D credits. The need for this service demonstrates the complexity of this area of the corporation tax system and the additional support announced would suggest that this view is shared by Government. R&D credits for small and medium-sized companies were introduced in 2000 and it is surprising that it has taken so long to recognise the issues facing small and medium sized companies.

The delay in introducing support for this particular sector is indicative of a much wider issue for corporation tax compliance. There has been real success in the introduction of the Large Business Office for companies with a turnover above £100 million and the relationship with the Customer Relationship Manager. The approach has led to a new relationship between HMRC and larger companies with both increased satisfaction and tax yields.

This has not been seen in the relationship with small and medium-sized businesses and ICAS believes that it is time to review the whole corporation tax compliance regime for this sector. ICAS would support a new approach based on risk rating and greater reliance on audited accounts. The issues for this sector are much wider than making claims for R&D credit and we would like to see the Government show a real commitment to making tax less taxing for this sector.

ICAS is aware that the Public Accounts Committee has raised issues about the cost of the relief when compared to the level of reported R&D expenditure by companies across the spectrum. We believe it would be appropriate to determine if the relief is actually achieving the policy aim of Government to stimulate innovation by UK companies. The scope of the relief is very wide includes projects such as IT systems at financial institutions that the “man in the street” might not immediately categorise as R&D.

The review should cover the operation of the relief as part of the UK corporation tax system as there have been changes to other reliefs given to fund the enhanced relief for R&D. Is the balance between relief for R&D and reliefs for capital expenditure by companies correct – and does it support the Government’s current policy aims? One point to consider is that the level of capital allowances has been reduced since the introduction of R&D tax relief so that the
investment in plant and machinery now attracts writing down allowances of 18% rather than 25%. We appreciate that the annual investment allowance is also available to relieve capital expenditure. There is also the issue of why R&D relief is limited to companies – partnerships and sole proprietor businesses are not able to claim the relief.

Specific questions:

Q1. Do you agree that these are the most relevant factors in ensuring that small businesses can access R&D tax credits?

We agree that these are the most relevant factors

Q2: How can HMRC better engage businesses to help increase take-up of R&D tax credits?

- How could businesses best obtain information on tax reliefs (social or traditional media, trade bodies, agents, other sources of information)?
- Who, within a company, should we target with information (finance, R&D managers, the business owner, agents, others)?
- What is the right time for a business to receive information?
- What other promotional activities could be introduced to ensure maximum take up of the reliefs?
- Do you consider that HMRC works sufficiently well in partnership with other government agencies? If not why?
- Are there any models of good practice we might follow (eg in other countries)?

As noted above, R&D tax credit relief has been available in the UK for 15 years and it is surprising that there are still companies who are not aware of the relief. ICAS has included section on R&D relief in the tax courses we offer to members to raise awareness.

We can only answer these questions on behalf of our members and the businesses and clients they represent. Most members obtain information from online sources but there are still some members who prefer information from traditional sources.

Information about R&D credit reliefs should be made available to companies when they first register for corporation tax and the information needs to be targeted at Board level. As HMRC is aware, claims for R&D tax credit involve different departments of a company working together to identify qualifying projects and collate the figures for those projects. Board interest is likely to facilitate this process – and the Board is best placed to identify those projects that are likely to be eligible.

HMRC should also consider making information available to businesses who apply to the patent office or contact research councils for funding.

Q3: Are you confident that you can contact the right R&D Unit if you need to do so?

We have dealt with a number of queries from members on this issue. For larger companies this is straightforward as the CRM co-ordinates the team dealing with all taxes issues for the group. For small and medium-sized companies there is no named point of contact and no details available of how to direct a query on R&D relief. There would be support from ICAS members for a team to deal with small and medium-sized businesses with details made available on the HMRC section of the .gov.uk website and generally publicised. These do not need to be named individuals – a team email address /message service would suffice provided that the protocols to ensure that queries are dealt with in a set time frame are in place. Directing the query to the team will help HMRC target its resources more effectively.

Q4: There is no question 4
Q5: Is the current definition of R&D a barrier to small companies claiming R&D tax credits?

- Would a change in definition to align it to accounting practice simplify the rules? If so why? What alternatives might be better?
- If introduced, how far should this treatment be optional (say for companies below a certain size) or should it be compulsory?
- What can we learn from other countries?

As noted above, the definition of R&D involves companies being aware of the legislation and the BIS guidelines. This is a complex area as HMRC will appreciate from its own internal team of specialists. The existing rules have taken some time to stabilise and to be used as an effective support to R&D activities undertaken by many companies and we have no information to suggest that such a major change would have overall benefits. We would support simplification measures but aligning the definitions would not achieve this and is likely to change the scope of the relief.

We are unable to comment on the position in other countries but HMRC will be aware that there are studies of R&D reliefs across tax jurisdictions which seek to compare the various regimes.

Q6: Are the rules over which costs qualify for relief a barrier to small companies claiming R&D tax credits?

We believe that the complexity of the rules is a barrier to small and medium-sized companies claiming the relief. We would prefer that the stability of the current system is maintained and that uncertainty resolved by greater clarity in guidelines published by HMRC.

Q7: Are there other specific design features which could be simplified to help small companies?

The rules governing the relief are complex and the legislation is drafted to try to ensure that only real innovation attracts tax relief. There needs to be a careful balance between having clear, simple and consistent rules and making sure that the legislation is comprehensive. As noted above, greater clarity in guidelines published by HMRC would assist small and medium-sized businesses.

Q8: If overall changes or improvements can be identified, would they be better as options or changes to the general rules, or as a particular scheme aimed at the smallest companies?

We do not believe that it would be helpful to introduce further schemes for R&D tax credit. As noted above, small and medium-sized businesses are able to make claims under both the SME scheme and the scheme for larger businesses dependent on the categorisation of the expenditure. Increasing the number of schemes will make the position more complex and increase the administrative burdens and the companies with the least resources.

Q8 (second): Recognising that the R&D manual is used by different groups, what works well/less well and for whom in the current format?

The current format of the manual is considered helpful by our members in practice. Our concern is that this guidance is appropriate for those versed in the basics rather than users who are seeking a basic understanding.

Q9: Is dedicated external customer (rather than intermediary) guidance needed? If so, does the commercial market already provide what is needed?

ICAS believes that guidance should be provided by HMRC rather than commercial providers.
Q10: Should HMRC design its guidance by task or event rather than around the detail of the legislation?

We would welcome this approach to the guidance.

Q11: What are the top issues for small companies and intermediaries both in terms of the legislation/rules and procedures?

The top issue for companies and intermediaries is the complexity of the legislation. The guidance provided online is helpful for those familiar with the legislation and procedures but is does not assist anyone who does not come with an understanding of the basic position. We have had queries from members in industry who are being advised that the company has qualifying expenditure who have consulted .gov.uk and found the content difficult to navigate and locate the relevant details.

For small and medium-sized businesses we feel that there should be support from dedicated HMRC staff to assist them with R&D tax credit as noted above.

Q12: Who uses the current guidance: companies, intermediaries or both?

In our experience both companies and intermediaries use the current guidance. Advisers will tend to use the manual guidance to address particular issue to understand the HMRC perspective and practice.

Q13: How would companies and intermediaries prefer guidance to be set out?

Alternatives could include:

- In the current format as a manual
- Additional illustrations/ case study, Q&A, decision tree etc
- Via online forums, webinars, YouTube etc
- Embedded in rules based applications (accounting software)

The material in the manual as currently published is used by our members extensively and we would like to see this retained. Additional illustrations and case studies would be helpful and many companies find the content on online forums, webinars and YouTube helpful in raising awareness of staff involved in the particular area.

Q14: Would the approach set out above improve take-up of R&D tax credits among firms who have never made a claim?

We believe that this approach would be helpful. We have outlined above our comments on the need for a fundamental review of all support for small and medium-sized businesses.

HMRC hold significant data on companies as part of their tax return – the accounts and computations. The iXBRL submission made by companies requires information to be tagged and this will include all information in the accounts of the R&D expenditure by the company. We wondered if it would be possible for HMRC to run a study to identify those businesses with R&D expenditure but who do not make a claim in the return and contact them to understand why no claim for R&D tax credits is made.

Q15: We would welcome views on the design of the advance assurance service including:

- The companies that would benefit most (ie in encouraging them to carry out more R&D and grow faster)
- What specific issues do companies encounter in making their first claim?
- For how long an advance assurance should be valid?
- Whether a company (or a company you advise) would be likely to use advance assurances (and if not why not)
Any issues for particular sectors/types of companies in administering and designing advanced assurance?

How the service should be advertised?

It is important to bear in mind when dealing with tax reliefs that companies do not undertake their activities for the tax relief – commercial considerations come first. The Government introduced R&D tax credits to encourage companies to carry out R&D but the choice rests with the company on the balance between its business activities and developing its R&D.

The issue for the first claim is the volume of information that a company needs to collate in support of that claim. A successful R&D claim will need liaison between disparate parts of the company who do not have day to day interactions – engineering departments, finance departments, R&D teams – and all of whom have a very detailed understanding of the definition of R&D for their particular area. The HMRC definition is different again and will need all the parties involved to understand this definition.

We believe that advance assurance would be used by eligible businesses. The scheme would give a company certainty over its position.

HMRC should use its normal channels to promote the service and exploit the new media solutions.

Q16: Another way to improve administration might be to link the advanced assurance service with access to finance. When attracting finance for an R&D project, how is this ability influenced by R&D tax credits? How could an advanced assurance service be structured to support access to funding?

We understand that the advanced assurance service is intended to allow companies to confirm whether their expenditure would be eligible for relief to assist them with fund-raising and planning. This proposal would be of value if the assurance given is binding on HMRC.

Q17: Are there any specific aspects of the way in which a claim is made or processed which could be simplified or improved?

This point is covered in our other comments and we have no specific recommendations in this area.

Q18: Do you agree with this assessment? In particular do you think that changes to R&D tax credits could have any equalities impact?

We cannot comment on the assessment. We would note that there is likely to be an internal cost to HMRC of providing enhanced support and that the take up of the relief would increase if its aims were to be reached. We note that this is not recognised in the assessment at this time.