

Draft guidance:

Research and Development (R&D) tax reliefs

A public consultation issued by HM Revenue and Customs (HMRC)

Comments from ACCA to HMRC
28 February 2023
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ACCA welcomes the opportunity to comment on the proposals issued by HMRC.

We have consulted our members through surveys and expert interviews and their views are represented in the following.

AREAS FOR SPECIFIC COMMENT:

We believe the House of Lords summed up the UK landscape for research and development (R&D) as outlined in both this consultation and the joint consultation from HMRC and HM Treasury “R&D Tax Reliefs Review: Consultation on a single scheme”.

“...investment in R&D makes an important contribution to the UK’s economy and productivity. R&D relief is seen by business and sector bodies as a crucial element for supporting and promoting R&D activity in the UK. We therefore welcome the Government’s continued support of the relief. Nonetheless, we are concerned by the evidence of the loss of revenue, attributable to abuse of R&D relief, that has escalated in recent years. We were alerted to large scale organised criminal attacks and the activities of rogue advisers which involve targeting small companies, often persuading them to make invalid claims.”¹

“We consider that legislative reforms of this nature will not be effective in isolation and that improvements to HMRC’s compliance capability are also required. This includes a more focused and targeted approach to identifying suspect claims, greater expertise and potentially more resource.”²

“Despite this, the Government’s proposal to refocus R&D relief on R&D activity in the UK may undermine the UK’s competitiveness by causing some UK based R&D to relocate elsewhere. While we understand the Government considers it cannot justify unrestricted relief for R&D expenditure overseas, Research and development tax relief and expenditure credit it should consider introducing a form of transitional relief for expenditure on specialised resources which are not currently available in the UK, especially for R&D being carried out under contracts already entered into.”³

“The Government should continue to look for further ways in which R&D relief can be improved. In seeking to ensure value for the taxpayer, it should look to combat spurious claims, ensure its adaptability to rapidly changing technology and learn from international R&D relief approaches. This is integral for securing the UK’s competitiveness as a hub of R&D activity.”⁴

New draft legislation & HMRC guidance

We welcome many of the proposed changes in legislation and guidance around R&D tax reliefs with effect from April 2023. Expansion of R&D definition to permit specific areas (such as data licences, cloud computing services and mathematics), tightening of the rules (in particular on the

¹ Economic Affairs Committee 3rd Report of Session 2022–23 HL Paper 137 Research and development tax relief and expenditure credit: <https://publications.parliament.uk/pa/ld5803/ldselect/ldeconaf/137/137.pdf>

² Economic Affairs Committee 3rd Report of Session 2022–23 HL Paper 137 Research and development tax relief and expenditure credit: <https://publications.parliament.uk/pa/ld5803/ldselect/ldeconaf/137/137.pdf>

³ Economic Affairs Committee 3rd Report of Session 2022–23 HL Paper 137 Research and development tax relief and expenditure credit: <https://publications.parliament.uk/pa/ld5803/ldselect/ldeconaf/137/137.pdf>

⁴ Economic Affairs Committee 3rd Report of Session 2022–23 HL Paper 137 Research and development tax relief and expenditure credit: <https://publications.parliament.uk/pa/ld5803/ldselect/ldeconaf/137/137.pdf>

concept of a going concern) and the extension of HMRC's powers to curb abuse are to be applauded.

We would ask whether the R&D definition expansion goes far enough and whether the approach taken by HMRC is agile enough for the current environment? There is a lack of coherence between HMRC's R&D definition and that used by the ONS, which is based on the OECD Frascati manual, and more globally aligned. Innovation is high on the Government's agenda along with R&D incentives – shouldn't the inputs and outputs be measured on the same basis?

Nonetheless, we are not clear for which audience this guidance has been designed?

More specific commentary on the guidance itself is outlined below under the following headings:

Transitional measures

Rather than creating uncertainty about what qualifies as UK or overseas, a pragmatic approach could be adopted to applications for a period, let's say until 31st March 2024 after which the Government's current plans for R&D reform are due to take place.

Presentation, language and content of the guidance

Overall, we feel the guidance is self-explanatory although we would make some suggestions to improve useability:

- Index

We suggest the index numbering is continued throughout on a consistent basis with the headings 'wholly reasonable' referenced 1.2.1 and so on. This will make it easier for trusted advisers to refer to and particularly when collaborating with HMRC on areas where the views of the users and HMRC differ.

- Language

Knowing the target audience is key for deciding what language to use. Parts of the draft guidance suggest a specialist audience (legislative references) and other parts a more general audience. Considering whether there should be versions of guidance for different types of users such as taxpayers, and agents. Or should the guidance be targeted based on needs starting at a general audience, set out in straightforward language, to facilitate a general understanding with the ability to drill-down to content more suitable for a professional? Alternatively, should the audience be segmented using appropriate media for the different audiences such as videos to show how to complete the forms required for new users? Indeed, this seems to be an area of interest and was raised by an attendee at the recent HMRC Stakeholder Conference.

In our view, guidance in this area is best targeted towards specialists (R&D tax specialists or finance people with the responsibility for R&D budget decisions) many of whom would already be party to Professional Conduct in Relation to Tax (PCRT) and to which HMRC endorses⁵. We note from the Gov.UK website⁶ that *"If you're writing for a specialist audience, you still need to make sure everyone can understand what the content is about."* For this reason, there should be a summary for a general audience with more detailed guidance for the specialist. This could be achieved on the website by links to more complex detail such as legislative references and

⁵ The HMRC standard for agents - Updated 23 January 2023: <https://www.gov.uk/government/publications/hmrc-the-standard-for-agents/the-hmrc-standard-for-agents>

⁶ <https://www.gov.uk/guidance/content-design/writing-for-gov-uk>

separate links to frequently asked questions (FAQs) directed at a non-specialist audience. The headings should be referred to as 'legislation' followed by the legislative reference and links to the legislation.

It is expected that most of the 'specialist' users will be from the accounting and tax professional communities and there is a certain language that is expected. For example, the reference to 'excluded factors' in paragraph 1.3 'Legal and regulatory requirement' would be more meaningful if it was referred to as the 'exclusion from the permitted exception'.

- Content

We recommend outlining the approach that HMRC would use to consider whether for example the condition of 'wholly reasonable' is met or the 'excluded factor'.

We would like to understand why the definitions were extended for data licences, cloud computing and pure mathematics?

Administration of R&D Claims

Claim notification

1. Format

Although we understand that the forms will be provided by way of regulations, we note the requirements outlined in the guidance.

We recommend using a system for R&D projects based upon the Advance Assurance used for Venture Capital Schemes (VCS). This long running and generally understood procedure is valued by trusted advisers in the market. We include an extract below from HMRC's Venture Capital Manual (VCM) which outlines the process, what it means in practice and how the HMRC team are involved. We believe this non-statutory approach would be feasible with the benefits of giving confidence, reducing uncertainty in the market and providing an indication of HMRC's view. This has been digitally enhanced with the introduction of the G-form.

For example, there were key performance indicators (the target was 15-day turnaround starting at 30-days and in periods of higher demand this increased to 40 days) that could be used to benchmark HMRC's performance over time and in times of peak demand. Through application management (which we can assume was via disciplined team management) and clear communication from the VCM team. The VCM teams could retrain the R&D specialised HMRC officers on their system. The reasons why the R&D project is not approved to be provided to the company and the potential to make another application should be available. The benefit of this facility is two-fold, it will help the businesses to incorporate this step into their R&D, aid understanding about what in HMRC's view qualifies and it will provide HMRC will real-time information on the areas of activity for R&D which will enable HMRC to be more proactive and agile. This level of agility will be required for the new digital age, in particularly considering new areas that should be covered by the R&D definition. Feedback to the Government and HM Treasury should be provided at regular intervals to ensure that the tax reliefs are targeted and meet the value-for-money objective set by the taxpayers.

The new G-form is linked to the Government Gateway or email address which has the facility to group applications by agent who could be used for risk profiling by HMRC.

"The VCR Team considers each advance assurance application and decides whether a company (or social enterprise) and a proposed share or security issue would qualify for tax reliefs.

The VCR Team does not provide an opinion in certain cases, where there is doubt about eligibility.

The VCR Team gives an advance assurance only in respect of the conditions that apply to the company (or social enterprise) and the particular share or security issue. An advance assurance given in respect of one share or security issue should not be regarded as providing assurance in respect of a different share or security issue.

An advance assurance will not be valid if it is found that the company (or social enterprise) has not disclosed all the relevant facts.

The advance assurance service is a non-statutory, discretionary, service and there is no right of appeal against the VCR Team's decision. The purpose of the service is not simply to agree every application but for HMRC to provide its opinion on whether a proposed investment would be eligible under the specified scheme. HMRC will provide an advance assurance only if it considers the proposed investment will meet the specified scheme rules, and the company and investors abide by the undertakings given in the application.

The VCR Team will not enter into protracted correspondence if it considers that an investment would not be eligible or refuses to provide an opinion because it is unable to reach a decision. The VCR Team will look at new information supplied but may decline to enter into further correspondence once a decision is given.

If the VCR Team declines to issue an advance assurance an investor may go ahead with the investment and the law may be tested through the statutory procedures.

The VCR Team monitors companies to ensure that the company continues to meet the requirements of the particular scheme for the entire duration of the qualifying period. If a company does not meet all of the requirements during a qualifying period then the tax relief can be withdrawn, or a VCT may be required to dispose of the holding.”⁷

An advance assurance application with all the details of the project would be a more open and inclusive step in incentivising innovation and R&D activity (rather than the blunt force of a claim notification). Ultimately, the outcome of using the claim notification is that agents will be even less likely to engage with the process than they were already. Due to the potential for legal claims based on this new additional advanced time-based hurdle from their clients, where it is unclear if their activity qualifies for R&D tax relief, could effectively amount to a barrier rather than opening up the scheme and collaborating with stakeholders on the availability and usage of R&D tax incentives. Using the VCM approach companies could receive feedback on whether their plans would meet the conditions and, when used alongside the guidance may mean a more streamlined approach for companies and HMRC. Projects can be referenced and it provides two opportunities to check the details (before and after the activity).

2. Time limits

We recommend that the time limits are aligned with existing time periods provided to trusted advisers to ensure the tax system is not made more complicated.

HMRC R&D Specialist Team approach

Managing the compliance function and maximising the R&D expertise by HMRC will determine the success in implementing the changes. Digital applications could be triaged at application

⁷ <https://www.gov.uk/hmrc-internal-manuals/venture-capital-schemes-manual/vcm60050>

stage to those who are already registered as agents with HMRC in a way to leverage those existing good relationships.

Genuine trusted advisers and, in particular, those signed up to PCRT (which has been updated most recently effective from 1st January 2023⁸) are interested in the public interest. As stated in PCRT *“Advice on R&D tax credit claims is considered by the PCRT bodies as the provision of advice in the area of taxation and therefore subject to AML supervision.”*⁹ Our members raise issues of technical competence (non-accounting or tax technical areas) in reviewing R&D claims and for this reason we have issued our own factsheet on this high-risk area¹⁰.

CONCLUSIONS

The draft guidance does not appear to be consistently written with a specific audience or objective in mind. In our view, further consideration of its purpose is required for the guidance to be as useful as it can be.

Collaboration via a digitised iterative process based on input from the companies and HMRC specialist R&D team would be more fitting for the R&D sector and align the customers expectations. Are there any lessons to be learned from global competitors for R&D activity?

Ultimately, the success of the changes will be dependent on HMRC’s capacity to implement in a timely manner.

⁸ [https://www.accaglobal.com/sg/en/technical-activities/technical-resources-search/2019/february/professional-conduct-in-relation-to-taxation-pcrt.html#:~:text=Professional%20Conduct%20in%20Relation%20to%20Taxation%20\(PCRT\)%20sets%20out%20the,members%20who%20undertake%20R%26D%20work](https://www.accaglobal.com/sg/en/technical-activities/technical-resources-search/2019/february/professional-conduct-in-relation-to-taxation-pcrt.html#:~:text=Professional%20Conduct%20in%20Relation%20to%20Taxation%20(PCRT)%20sets%20out%20the,members%20who%20undertake%20R%26D%20work)

⁹ Professional Conduct in Relation to Taxation (PCRT): [https://www.accaglobal.com/sg/en/technical-activities/technical-resources-search/2019/february/professional-conduct-in-relation-to-taxation-pcrt.html#:~:text=Professional%20Conduct%20in%20Relation%20to%20Taxation%20\(PCRT\)%20sets%20out%20the,members%20who%20undertake%20R%26D%20work](https://www.accaglobal.com/sg/en/technical-activities/technical-resources-search/2019/february/professional-conduct-in-relation-to-taxation-pcrt.html#:~:text=Professional%20Conduct%20in%20Relation%20to%20Taxation%20(PCRT)%20sets%20out%20the,members%20who%20undertake%20R%26D%20work).

¹⁰ Topical guidance covering the application of professional standards to the provision of R&D tax credit services 1 June 2020: [https://www.accaglobal.com/sg/en/technical-activities/technical-resources-search/2019/february/professional-conduct-in-relation-to-taxation-pcrt.html#:~:text=Professional%20Conduct%20in%20Relation%20to%20Taxation%20\(PCRT\)%20sets%20out%20the,members%20who%20undertake%20R%26D%20work](https://www.accaglobal.com/sg/en/technical-activities/technical-resources-search/2019/february/professional-conduct-in-relation-to-taxation-pcrt.html#:~:text=Professional%20Conduct%20in%20Relation%20to%20Taxation%20(PCRT)%20sets%20out%20the,members%20who%20undertake%20R%26D%20work).