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Research and development draft guidance

Comments by the Chartered Institute of Taxation

1 Introduction

1.1 The Chartered Institute of Taxation (CIOT) is the leading professional body in the UK for advisers dealing with all aspects of taxation. We are a charity and our primary purpose is to promote education in taxation with a key aim of achieving a more efficient and less complex tax system for all. We draw on the experience of our 19,000 members, and extensive volunteer network, in providing our response.

1.2 The CIOT welcomes this opportunity to provide comments on the 'Research and Development (R&D) tax reliefs – draft guidance ('the Draft Guidance') published on 20 December 2022[1]. This guidance relates to a number of changes to R&D relief and new compliance measures that are due to be introduced with effect from 1 April 2023. The reforms include bringing pure mathematics research within scope of the reliefs, including data and cloud computing as qualifying costs, restricting expenditure on some overseas R&D activities. There is also a package of measures intended to target abuse and improve compliance.

1.3 Draft legislation for these measures was published in July 2022, and we understand that the Draft Guidance is based on this draft legislation. It is unfortunate that the legislation for some of the detail, for example in relation to the additional information to be provided by taxpayers and the format of the various new notifications that will be required, remains unpublished so close to the implementation date. In addition, it is noted that the legislation will not be finalised until Finance Bill 2023, and that the final form of the legislation may differ from the draft legislation published on 20 July 2022. However, notwithstanding this, we welcome that the guidance for taxpayers has been prepared in advance by HMRC and that HMRC is seeking views on the Draft Guidance.

1.4 The CIOT's stated objectives are for a tax system that includes greater clarity, so people can understand how much tax they should be paying and why, and also certainty, so businesses and individuals can plan ahead with confidence. HMRC guidance can help to achieve these objectives.

[1] https://www.gov.uk/government/consultations/draft-guidance-research-and-development-rd-tax-reliefs

2 About us

2.1 The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. Our comments and recommendations on tax issues are made solely in order to achieve this aim; we are a non-party-political organisation.

2.2 The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.

2.3 The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries.

2.4 Our members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.

3 Paragraph 1. Overseas Expenditure

3.1 The final paragraph under the introductory paragraphs under the heading '**1. Overseas Expenditure**' says:

> For the same periods, to be qualifying expenditure, expenditure on payments for externally provided workers (EPWs) must be subject to PAYE and National Insurance contributions (NICs), unless it is qualifying overseas expenditure.

We do not think that this language provides a clear and accurate explanation of the position. We suggest that most people would read '*payments for externally provided workers*' as meaning the payment made by the claimant company to the Staff Provider. It is not these payments that must be subject to PAYE and NI; rather it is the payments to the individual EPWs by the Staff Controller (new section 1129(3)(d) and new section 1132A).

3.2 In paragraph 1.2, under the heading '**Qualifying overseas expenditure**' there is a helpful discussion about the 'wholly unreasonable' test in relation to the definition of qualifying overseas expenditure (QOE).

3.3 However, we would query the statement at the end of the third paragraph under the sub-heading '**Wholly unreasonable**' that *'If on the other hand the company <u>or a third-party</u> already operates similar facilities in the UK which could be easily adapted, it would be reasonable to expect it to do so, and the condition would not apply'* (emphasis added). This aspect of the test should only apply to facilities operated by the claimant company and its connected parties, and not those operated by third-parties. Claimants will not always be aware of whether or not such third party facilities exist and, even if they do, they will have no power over whether or not the third party makes the necessary adaptations. It does not seem fair to deny a company relief as a result of what a third party, over whom they may have no influence, does or does not choose to do. It would also be very difficult for HMRC to test compliance with this requirement, as HMRC staff are even less likely to be aware of what facilities third parties might have available.

3.4 Also, the following paragraph appears at the end of this section:

> *It may be that there is time pressure, requiring use of a facility abroad which could be replicated in the UK, but would take too long, or that UK facilities are available, but are fully booked on the required timescale.*

Whilst we agree with the statement itself, it is unclear whether the guidance is suggesting that this is to be considered a situation where it would be 'wholly unreasonable' for the company to replicate the R&D in the UK. The guidance should be extended to confirm that, in these cases, the condition would apply.

3.5 It may be helpful for the guidance to clarify that the new rules apply only to EPWs and contracted out work, and do not apply to the employees of the company itself; as such there is no requirement for company's employees to be in the UK.

4 Paragraph 3. Claim notification

4.1 We are not clear why there is a sub-heading of '**FA98 Sch 18 part 9A para 83EB**' under paragraph 3.1. Paragraph 3.1 deals generally with the requirement to supply a Claim Notification form for their R&D claim to be valid. FA98 Sch 18 part 9A para 83EB is a new provision that relates to removing invalid claims from corporation tax returns, rather than dealing with the requirement to make a notification itself. Although we agree that this provision in Schedule 18 would include claims for which a notification is not made, the text under paragraph 3.1 does not relate to this specific legislative reference. The sub-heading may, therefore be confusing.

4.2 The description of companies that need to supply a Claim Notification is inconsistent as between the Draft Guidance and the draft legislation. The legislation defines this by reference to not having made a claim or a notification in the relevant time period, whereas the Draft Guidance makes no reference to having previously made a claim notification. Thus:

- paragraph 3.1 of the Draft Guidance indicates that no notification is required if a claim has been made in any of the previous three calendar years, with Example 1 going on to reinforce that this period is based on the date any previous claim was submitted, and not the accounting period it related to.
- the draft legislation instead refers in new section 104AA of CTA 2009 to whether or not a claim has been made in respect of any of the three accounting periods immediately preceding the claim period.

Please can you confirm which is correct and update the Draft Guidance or the legislation as appropriate.

4.3 We suggest that the draft legislation is the better approach and companies should consider the past three accounting periods. Otherwise, the period to consider will vary depending on exactly when returns for previous years were submitted. This could cause confusion, and it also seems odd that a company being either late or early in filing its return in the past should affect whether or not a notification is required in the future.

4.4 Also the wording Example 1 is confusing. As mentioned above, the test in the legislation is by reference to claims or notifications made *for any of the three accounting periods …*, not *in any of the three accounting periods*. In Example 1 we do not know what accounting period either of the claims relate to. The first one could be a year end 30/4/20, the second for the year end 30/4/24. We suggest this example, and the wording overall, should be a lot clearer to correctly reflect the situation in the legislation.

4.5 Under the sub-heading '**Time limits**', the Draft Guidance indicates that the latest date for submitting a claim notification is six months after the end of the period of account that includes the relevant accounting period.

This differs from the Draft Legislation, which states at the new section 1054A CTA 2009 that the deadline is *'six months beginning with the last day of the claim period'* (the claim period being the specific accounting period, and not the overall period of account). It needs to be clarified which deadline is correct. In our view, the position in the Draft Guidance is likely to be the most pragmatic approach where there is a long period of account, as there would only be a single deadline for both accounting periods, and we understand from HMRC that the revised legislation will be amended to this effect.

5 Paragraph 2. Data licences and cloud computing services

5.1 The discussion in the first paragraph under paragraph 2.2 is confusing because it talks about a licensee obtaining ownership of the data set. We are not clear about what is being considered here: our understanding of the nature of a licence arrangement necessarily means that the licensee does not acquire ownership of the thing that is being licensed. Similarly, a purchase of data would not involve the acquisition of a licence. We suggest that this paragraph is re-considered, and is possibly not required at all. However, if it is retained then the underlying legal nature of the transactions referred to should be corrected/clarified.

6 Acknowledgement of submission

6.1 We would be grateful if you could acknowledge safe receipt of this submission, and ensure that the Chartered Institute of Taxation is included in the List of Respondents when any outcome of the consultation is published.

The Chartered Institute of Taxation
28 February 2023