



# BRIEFING FOR MPs BY ICAEW'S TAX FACULTY ON RESEARCH AND DEVELOPMENT TAX RELIEF

Issued 29 July 2024

ICAEW welcomes the opportunity to provide an update to the new government on the existing landscape of research and development tax relief.

For questions on this document please contact our Tax team at [taxfac@icaew.com](mailto:taxfac@icaew.com) quoting REP 66/24.

This response of 29 July 2024 has been prepared by the ICAEW Tax Faculty. Internationally recognised as a source of expertise, the ICAEW Tax Faculty is a leading authority on taxation and is the voice of tax for ICAEW. It is responsible for making all submissions to the tax authorities on behalf of ICAEW, drawing upon the knowledge and experience of ICAEW's membership. The Tax Faculty's work is directly supported by over 130 active members, many of them well-known names in the tax world, who work across the complete spectrum of tax, both in practice and in business. ICAEW Tax Faculty's Ten Tenets for a Better Tax System, by which we benchmark the tax system and changes to it, are summarised in Appendix 1.

ICAEW is a world-leading professional body established under a Royal Charter to serve the public interest. In pursuit of its vision to build the economies of tomorrow, ICAEW works with governments, regulators and businesses and it leads, connects, supports and regulates more than 165,000 chartered accountant members in over 147 countries. ICAEW members work in all types of private and public organisations, including public practice firms, and are trained to provide clarity and rigour and apply the highest professional, technical and ethical standards.

© ICAEW 2024

All rights reserved.

This document may be reproduced without specific permission, in whole or part, free of charge and in any format or medium, subject to the conditions that:

- it is appropriately attributed, replicated accurately and is not used in a misleading context;
- the source of the extract or document is acknowledged and the title and ICAEW reference number are quoted.

Where third-party copyright material has been identified application for permission must be made to the copyright holder.

---

## ICAEW

Chartered Accountants' Hall Moorgate Place London EC2R 6EA UK  
[icaew.com](http://icaew.com)

The Institute of Chartered Accountants in England and Wales (ICAEW) incorporated by Royal Charter (RC000246)  
Registered office: Chartered Accountants' Hall Moorgate Place London EC2R 6EA UK

## EXECUTIVE SUMMARY

1. ICAEW welcomes the new government's commitment to maintain the existing structure of the research and development (R&D) tax relief regime over the next parliament as noted in **Labour's business partnership for growth**. Stability is key to improving certainty for businesses that are looking to invest in R&D to deliver growth. Indeed, an effective and stable R&D tax regime is an essential way to support growth and attract investment into the UK from innovative companies who otherwise might carry out their R&D activities elsewhere.
2. We also recognise and support the need for better policing of the regime to minimise the risk of fraud, error and tax leakage. ICAEW has been raising concerns about the claims made by certain R&D agents for some time and is keen to assist the government in this regard.
3. However, HMRC's response to fraud and error – in the form of its current 'volume-based' compliance strategy – is causing significant disruption to many businesses undertaking genuine R&D activities. HMRC is aware of our concerns and accepts that the current approach will result in 'collateral damage'. We would strongly urge immediate action to ensure that this collateral damage does not negatively impact the government's growth mission. Without intervention there is likely to be a substantial impact on investment and growth, with some business already considering moving R&D activity offshore, further impacting the ability to generate UK growth in GDP.
4. There is also widespread concern over the interpretation and quality of data being used to assess the effectiveness of the compliance strategy undertaken by HMRC. For example, we understand many businesses are voluntarily withdrawing compliant claims due to the disproportionate costs of defending a legitimate claim due to the approach taken by the HMRC R&D compliance team. It is not clear how this type of outcome is being recorded in HMRC statistics. It appears that this would be classified as an 'incorrect' claim and as such a 'win' for the compliance strategy which, if so, is misleading and may result in incorrect conclusions being drawn from the data.
5. Our key concerns around the current compliance approach can be categorised into the following issues:
  - a. Poor use of HMRC resources due to the lack of appropriate risk assessment of claims;
  - b. A disproportionate impact on smaller businesses;
  - c. Inadequately trained HMRC staff leading to protracted enquiries and unnecessary compliance costs for genuine claimants;
  - d. Lack of confidence in the data and statistics that are being cited by HMRC in support of the compliance approach; and
  - e. The R&D regime lacks stability and is unattractive on a global stage leading to the UK being less competitive and losing investment in innovation that would drive GDP growth.

## KEY CONCERNS

### Lack of risk assessment of claims

6. ICAEW members advise us that it is not unusual for HMRC enquiries to be raised with little or no review of the evidence submitted by claimants to support their claims for R&D tax relief. Similarly, we are informed that some companies are being subject to concurrent years of enquiries despite the fact the first enquiry found no evidence of error and has been closed without adjustment. This is costly and unsettling for companies genuinely

undertaking R&D and an inefficient use of HMRC resources. Members advise us that existing escalation routes within HMRC are already becoming saturated with open disputes resulting in delays and heightened uncertainty.

7. The Chair of ICAEW's Tax Faculty, Stuart Lisle, works as a tax adviser to Oxford Science Enterprises plc, a company that nurtures cutting-edge technology from Oxford University into successful businesses, providing access to specialists and start-of-the-art lab and start-up space. Part of his remit is to provide support to the portfolio of companies that are invested in, across three high-growth sectors – Life Sciences, Health Tech and Deep Tech.
8. Stuart explains, in headline terms, the impact of the current compliance environment: *“Our portfolio companies are at the cutting edge of their respective sciences, yet we are seeing an increasing number of ill-informed HMRC enquiries into their R&D claims. We observe HMRC caseworkers with no knowledge or experience of the subject matter challenge the qualifying nature of the work our portfolio companies are undertaking, based only on opensource research, such as google or Wikipedia. The validity of competent professionals, many of whom have published multiple peer-reviewed scientific papers in their field, is also being challenged. There is often little or no evidence to suggest any of the documentation provided to HMRC to support the R&D claim has been reviewed prior to an enquiry being raised. We need to see a change in approach, so that clearly qualifying claims are not subject to such illinformed enquiries.”*
9. ICAEW's Tax Faculty is understandably concerned to receive feedback of this nature from respected members advising companies at the cutting edge of technology in vital sectors such as life sciences. Without a change in approach, the rising costs of defending legitimate R&D claims will be stifling for world-leading research and UK economic growth.
10. We are anticipating a flurry of R&D tax cases but we would also note the recent First-tier Tribunal decision [Get Onbord Limited \[2024\] UKFTT 00617 \(TC\)](#), which found in favour of the taxpayer. This case illustrates many of the issues described above. We provide a telling extract of the judgment below:

*64. We then heard from Mr Umar, who is the HMRC officer responsible for this case. Mr Umar was in a difficult position, as he has no technology experience or expertise, nor (beyond the fact that they are members of HMRC's in-house software development team) was he aware of the credentials of those he sought advice from and who commented on his correspondence with GOL and its advisers. He does not know whether they had industry knowledge of KYC/ALM processes. This was the first software claim Mr Umar had dealt with.*

*65. We found Mr Umar to be an honest, straightforward witness, who was clearly trying to help as best he could, but his lack of scientific knowledge or experience meant that his evidence was of no real help to us in deciding the issues before us.*

### **Disproportionate impact on smaller businesses**

11. The increased compliance burden can often be absorbed by larger businesses. These companies will not only have access to in-house tax resource but also the larger value claims can support the increased costs of defence. By contrast, smaller claimants simply cannot justify the professional fees involved to defend their claims.
12. By way of example, one member indicated they had received an enquiry letter containing 600 questions for a relatively small claim in an industry where genuine R&D is prevalent. Examples of such disproportionate compliance burdens are, unfortunately, widespread.
13. Although enhanced R&D intensive support (ERIS) was introduced to target extra relief to SMEs with a high proportion of their expenses constituting expenditure on R&D activities,

members advise us that this is creating confusion and complexity with ambiguous legislation and inconsistencies in how HMRC applies the rules. The policy, in its current form, is often not achieving what was intended. For example, companies can only claim ERIS if they meet the 40% R&D-intensity threshold (30% from April 2024). The legislation on how to calculate the R&D-intensity threshold is unclear and we understand that HMRC is taking a very restrictive interpretation of the rules. This is likely to result in many companies that you might expect to qualify not meeting the required R&D-intensity threshold (including companies in the life sciences sector).

### **Inadequately trained HMRC staff**

14. There is widespread concern among ICAEW members about the lack of experience and expertise of R&D within the HMRC compliance team. This appears to be particularly problematic in the Individuals and Small-Business Compliance (ISBC) Directorate of HMRC where smaller claims are typically handled (exacerbating our concerns for small businesses above).
15. By way of example, many members refer to HMRC caseworkers using open-source research to challenge respected scientific experts in their field as to whether a project meets the definition of R&D and citing this research as evidence in correspondence. This is alarming and indicates a significant lack of experience in managing R&D enquiries. There are many other examples but, for brevity, we have not listed them here.
16. The lack of technical experts in HMRC (and the apparent unwillingness of HMRC to accept the evidence of a competent professional) has resulted in claimants having to 'over-simplify' technical discussions and evidence about the nature of the R&D activities undertaken. HMRC then argues that these projects are non-qualifying as there is no advancement in science or technology. According to members, this issue around over-simplification is affecting many claimants.
17. We are also aware of procedural errors such as the proper enquiry closure process not being followed. This can result in undue stress and costs for claimants. For example, liabilities can be added to a company's tax account and chased by debt management because HMRC has not provided companies with the opportunity to appeal. This is completely avoidable if proper processes are followed.

### **Lack of confidence in the data and statistics cited in support of the compliance approach**

18. As noted above it appears that claims withdrawn by taxpayers in the course of an enquiry may be recorded as an 'incorrect' claim. This would make the statistics being used to judge the success of HMRC's volume-based compliance approach misleading. We have raised our concerns in this regard with HMRC. However, there has been limited sharing of the assumptions behind any statistics being cited by HMRC. This makes positive debate and support extremely difficult.
19. Where decisions are being taken concerning the use of HMRC resources, it is important that they are based on sound judgements and a full understanding of the facts. Taxpayers will be forced to concede valid claims for tax relief if it is commercially unviable to defend them. This is not indicative of a sound compliance strategy. A better way needs to be found to support the progress of legitimate R&D claims rather than pricing them out. The current approach risks hindering growth and investment and making the UK a less attractive place to do business.

### **R&D regime lacks stability and is unattractive on a global stage**

20. Members have indicated that a lack of confidence exists when claiming R&D tax relief within the UK more generally. This has arisen due to various changes to the rules made in quick succession over the past few years in addition to the change in approach by HMRC to

reviewing claims. The impact of such changes is made worse by HMRC's current adversarial compliance approach which is significantly impacting legitimate claimants. This has resulted in considerable uncertainty and a sense of instability. Anecdotally we are receiving numerous reports of companies moving (or considering moving) their R&D operations overseas because of the current environment.

## OUR RECOMMENDATIONS

21. To increase confidence and stability, the government should maintain its commitment to making no significant policy changes to the R&D tax relief regime over the next parliament.
22. A formal plan should be put in place to address the skills gap within HMRC, particularly in the ISBC Directorate of HMRC. It is impractical to expect HMRC to have detailed technical knowledge in all areas of science and technology. However, where there are any gaps in knowledge, reliance should be placed on the evidence of suitably qualified competent professionals in claimant companies. HMRC's due-diligence procedures around the technical abilities of these individuals should be robust, reasonable and consistently applied. This is an area that requires work, as illustrated in both Stuart Lisle's comments above and the judgement of Get Onbord Limited [2024] UKFTT 00617 (TC).
23. Formal risk assessment procedures should be put in place to target HMRC resource to the riskiest claims and ensure that low-risk claimants are not subject to unduly onerous enquiries.
24. We would welcome HM Treasury/HMRC engaging in further consultation with professional bodies to raise standards and improve compliance in this area. As Royal Charter bodies acting in the public interest, we have a shared objective to support HMRC in raising the standards of compliance and improving the UK tax system. We have already been working closely with HMRC in this regard and are keen to explore how we might build on this work as trusted stakeholders.
25. In order that any policy decisions made are based on an accurate evidence base, there should be more detailed interrogation of the assumptions behind any data concerning HMRC compliance activities to ensure that it accurately reflects the reasons as to why claims may have been withdrawn. Similarly, a proper impact assessment should be undertaken to ensure the additional compliance costs for claimants are appropriately captured.
26. Further guidance (or even short videos) aimed at directors of companies undertaking R&D about what constitutes qualifying R&D activities would be welcomed. This is a complex area and there are some common misconceptions. This type of guidance could help steer businesses away from making spurious claims that may be endorsed by less reputable advisers.

## APPENDIX 1

### ICAEW TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. Statutory: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. Certain: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. Simple: the tax rules should aim to be simple, understandable and clear in their objectives.
4. Easy to collect and to calculate: a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. Properly targeted: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. Constant: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. Subject to proper consultation: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. Regularly reviewed: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. Fair and reasonable: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. Competitive: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see <https://goo.gl/x6UjJ5>).