

United Kingdom

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What's new?

Summary of updates/Changes to R&D and government incentives from 1 January 2019 through 31 October 2020

The research and development (R&D) expenditure credit (RDEC) increased to 13% (from 12%) for expenditure incurred on or after 1 April 2020.

HM Revenue & Customs are in the process of consulting on expanding the definition of software costs that may be included in R&D claims to include cloud and hosting costs.

The UK left the EU on 31 January 2020 and is no longer eligible to receive any new grants from the EU as from that date. Brexit negotiations are in progress and are planned to be concluded by 31 December 2020. Areas subject to negotiation include ongoing adherence by the UK to EU state aid rules on new grant awards, and access for UK entities to EU grants.

Featured government incentives

Incentive name	Description	Maximum percentage	Qualification standards	Key exclusions or issues
R&D expenditure credit (RDEC, for large companies)	Credit for a proportion of qualifying R&D expenditure, accounted for as an "above the line" "grant" or "other" income and, therefore, taxable Companies without a corporation tax liability against which to offset the RDEC may claim a cash credit (subject to certain limits)	13% of qualifying expenditure (increased from 12% as from 1 April 2020)	Employee costs (company and other group companies) Contracted individuals working under the supervision, direction, or control of the claimant where their services are provided through a third party (restricted to 65% of the costs) Software or consumable items used in the R&D process Contributions to independent research Subcontracting payments to "qualifying bodies" and payments made to volunteers for participating in clinical trials	Consumables may not be included in an R&D claim where they form part of a product that is sold or otherwise transferred in the ordinary course of business Payments to subcontractors do not qualify unless made to a university, individual, or partnership of individuals
R&D super deduction (for small and medium-sized enterprises, SMEs)	Super deduction for qualifying R&D expenditure for SMEs to reduce their tax liabilities or, if loss making, to surrender for a cash credit	230% of qualifying expenditure Cash credits for SMEs in tax loss positions, up to 33.35% of qualifying expenditure	Employee costs (company and other group companies) Contracted individuals working under the supervision, direction, or control of the claimant where their services are provided through a third party (restricted to 65% of the costs) Software or consumable items used in the R&D process Payments to subcontractors (restricted to 65% of the costs)	Consumables may not be included in an R&D claim where they form part of a product that is sold or otherwise transferred in the ordinary course of business Tax benefit available to SMEs is restricted to EUR 7.5 million per R&D project SMEs cannot claim relief for costs that are subsidized or that relate to activities contracted to them, although they may claim under the large company scheme for the excluded expenditure

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Featured government incentives

Incentive	Description	Maximum percentage	Qualified Expenditure	Key exclusions or issues
Patent box	Reduced rate of corporation tax for profits from patented inventions and certain other innovations	10% effective rate of corporation tax on profits generated from qualifying patents	<p>Intellectual property income derived from:</p> <ul style="list-style-type: none"> • Sale of patented products, i.e., the sale of the patented product or products incorporating the patented invention or bespoke spare parts; • Sale or licensing of patent rights; • Infringement income; or • Damages, insurance, or other compensation related to patent rights 	<p>As from 1 July 2016, companies must demonstrate a nexus between the profits falling within the patent box and the R&D activities that generated the underlying technology</p> <p>Companies already elected into the patent box by 1 July 2016 may be eligible to be grandfathered until 30 June 2021</p>

Industries most often affected by government incentives in country

Technology, Media & Telecom	Financial Services
● Telecom, Media & Entertainment	● Banking & Capital Markets
● Technology	● Insurance
Consumer	Investment Management
● Consumer Products	Real Estate
● Retail, Wholesale & Distribution	Life Sciences & Health Care
● Automotive	● Health Care
● Transportation, Hospitality & Services	● Life Sciences
Energy, Resources & Industrial	Government & Public Services
● Power & Utilities	Health & Social Care
Mining & Metals	Defense, Security & Justice
● Oil, Gas, & Chemicals	Civil Government
● Industrial Products & Construction	International Donor Organizations
	● Transport

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Type	National incentive?	State, provincial, regional or local incentives? ¹	Filing deadlines imposed?	Is the claim made in advance or arrears? ²	Nature of incentive	Maximum benefit available to large enterprises	Maximum benefit available to small and medium-sized enterprises
Innovation							
Research & development (R&D)	●	●	● ●	National: Arrears Local: Not applicable	Super deduction and tax credit for companies incurring qualifying R&D expenditure relating to staff costs, consumables, externally provided workers and subcontractors (SME scheme only). Cash tax credit available subject to conditions under both SME scheme and R&D expenditure credit (RDEC) scheme for larger companies	10.53% of qualifying research expenses (increased from 9.72% as from 1 April 2020) given as a reduction to the corporation tax liability or as a cash amount	An additional 130% super deduction giving a tax saving of up to 33.35% of qualifying research expenses
Patent box	●	●	● ●	National: Arrears Local: Not applicable	Reduced effective tax rate on profits arising from patents for companies owning or exclusively licensing patents.	Effective tax rate of 10%	Effective tax rate of 10%
R&D grant (national)	●	●	● ●	National: Arrears Local: Arrears	Cash grant subject to varying criteria depending on nature of specific grant	50% of qualifying costs	70% of qualifying costs
Investment							
Capex	●	●	● ●	National: Advance Local: Advance	Cash grant or loans for companies investing in medium term investment plans involving capital expenditure	25% of qualifying costs	45% of qualifying costs

Key: ● = PERMANENT INCENTIVE ■ = TEMPORARY INCENTIVE ■ = NEGOTIABLE ● = NO ● = LIMITED APPLICABILITY ● = NOT APPLICABLE

Notes:

- Green means that this incentive is currently in effect. Yellow means that the incentive has limited applicability, i.e., the requirements for this incentive limit its value to most companies. Red means that there is no incentive.
- If the response is advance, this means that the government must approve the award of the incentive prior to the commencement/completion of the project/activity. If the response is arrears, this means that the award of the incentive is determined at the end of the tax period or after the completion of the qualifying project or activity. Most tax incentives are considered to be claimed in arrears because they are reported on tax returns.





















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Investment (continued)							
Employment				National: Advance	Cash grant or loans for companies investing in the creation of new jobs or protection of existing jobs	25% of qualifying costs	45% of qualifying costs
				Local: Advance			
Training				National: Advance	Cash grant for additional training of new recruits or upskilling the existing workforce	50% of qualifying costs	70% of qualifying costs
				Local: Advance			
Annual investment allowance				National: Arrears	Tax deduction for companies incurring capital expenditure qualifying for plant and machinery allowances	100% of qualifying expenditure up to GBP 1 million (for expenditure incurred as from 1 January 2019 through 31 December 2020)	100% of qualifying expenditure up to GBP 1 million (for expenditure incurred as from 1 January 2019 through 31 December 2020)
				Local: Not applicable			
Enterprise zones				National: Not applicable	Business rates discounts, enhanced capital allowances, simplified local authority planning procedure for companies investing in designated areas of the UK	GBP 275,000 business rates discount over five years, 100% first year tax deduction for plant and machinery expenditure	GBP 275,000 business rates discount over five years, 100% first year tax deduction for plant and machinery expenditure
				Local: Advance arrears			
Environmental sustainability							
Intensive energy use (climate change agreements)				National: Not applicable	Discount on the climate change levy (CCL) on the energy bill for companies able to demonstrate that energy is a substantial cost component of their products, and who agree to reduce energy use and carbon dioxide emissions under a climate change agreement	Reduction in the CCL rate of 77% to 92% depending on the commodity	Reduction in the CCL rate of 77% to 92% depending on the commodity
				Local: Not applicable			

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Environmental sustainability (continued)							
Small-scale renewable generation support (including solar, wind, hydro)	●	●	● ●	National: Arrears Local: Arrears	Cash incentives for companies involved in the generation of innovative and environmentally friendly technologies	Varies	Varies
Large-scale renewable generation support (renewables obligation)	●	●	● ●	National: Arrears Local: Arrears	Tradable certificates available to companies involved in large-scale renewable generation assets. Closed for new generating capacity after 31 March 2017	Limited by type of generation technology and annual renewable obligation requirements	Limited by type of generation technology and annual renewable obligation requirements
Funding for environmental projects (landfill communities fund)	●	●	● ●	National: Arrears Local: Arrears	Charitable grants for companies engaged in environmentally driven research	Total fund limited by annual value of landfill tax receipts	Total fund limited by annual value of landfill tax receipts
Funding projects to reduce impact of extraction industry	●	●	● ●	National: Arrears Local: Arrears	Charitable grants for companies engaged in environmentally driven research	Total fund limited by annual value of aggregates levy receipts	Total fund limited by annual value of aggregates levy receipts
Enhanced capital allowances	●	●	● ●	National: Arrears Local: Not applicable	Tax deduction for companies investing in energy/water efficient plant and machinery prior to April 2020	100% first year tax deduction for qualifying capital expenditure	100% first year tax deduction for qualifying capital expenditure

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Country background

The UK headline corporate tax rate currently is 19%.

R&D occurs when a project seeks to achieve an advance in science or technology through the resolution of scientific or technological uncertainty. It also includes certain qualifying indirect activities undertaken as part of a project.

Innovation incentives

Research & Development (R&D)

Nature of incentives

The UK offers volume-based super deductions and credits for qualifying revenue expenditure as defined in the Department for Business, Energy and Industrial Strategy guidelines that vary depending on the size of the taxpayer. A super deduction scheme is available for companies that fall within the definition of an SME, whereas all other companies (large companies) may claim an R&D expenditure credit (RDEC). The RDEC regime is available to SMEs where the R&D activity has been subcontracted to them by a large company or where the activity is otherwise subsidized.

A company is considered an SME where it has fewer than 500 employees, and either turnover not exceeding EUR 100 million or balance sheet total not exceeding EUR 86 million. (The criteria for qualification as an SME follows the EU recommendation, but allows for the criteria to be doubled.) Affiliated companies are taken into account in determining whether a company qualifies as an SME.

SMEs qualify for the following expenditure-based tax incentives:

- 230% super deduction; and
- Cash credits for SMEs in loss positions, up to 33.35% of qualifying expenditure.

A cap restricts the amount of the tax benefit available to SMEs, over and above the benefit that would have been available had the company not been an SME, to EUR 7.5 million per R&D project. The government announced in Budget 2018 proposals to introduce

an additional cap to limit the amount of payable R&D tax credit that a qualifying loss making company may receive in any tax year to three times the company's total Pay As You Earn (PAYE), and employee and employer national insurance contributions (NICs) that the company has to account for within that year. The cap initially was due to come into force as from 1 April 2020, however Budget 2020 delayed the introduction of the measure until 1 April 2021 in order to allow additional time for consultation on the practical application of the cap.

Large companies qualify for the RDEC at 13% (increased from 12% for expenditure incurred on or after 1 April 2020). The RDEC is accounted for as an "above the line" "grant" or "other" income and, therefore, is taxable. With a corporate tax rate of 19%, this results in a net after tax credit of 10.53% as from 1 April 2020 (i.e., 13% x 81% (where 81% is derived from 100%-19%)), (increased from 9.72% (i.e., 12% x 81%)).

The super deduction and RDEC are broadly based on the same qualifying cost categories (see below). Companies without a corporation tax liability against which to offset the RDEC may claim a cash credit of 10.53% as from 1 April 2020 (increased from 9.72%). The cash credit is capped at an amount equal to the PAYE, and employee and employer NICs associated with the employees whose costs are included in the claim.

Unused RDEC benefits may be carried forward to future periods, or may be surrendered to group companies with a UK corporation tax liability in the same accounting period.

For both the SME and RDEC regimes, the cash credit is available only if the most recent financial statements of the claimant company have been prepared on a going concern basis.

Claims for all forms of R&D relief must be made within 12 months of the filing deadline for the relevant tax return. In most cases, this will be two years from the end of the accounting period.



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An advanced clearance service is available for RDEC claims that provides a pre-filing agreement for three years. A similar service is available for very small companies that have not previously filed claims.

Although companies that earn profits from oil extraction or oil rights in the UK or UK continental shelf are subject to a higher tax rate of 40%, such companies are able to claim a higher rate of the RDEC at 49%, resulting in a net after-tax benefit of 29.4%.

Capital expenditure is excluded from the volume-based incentives, but a full deduction for capital costs incurred for carrying out R&D or providing facilities for carrying out R&D may be claimed in the year the expenditure is incurred, rather than being depreciated for tax purposes in accordance with the normal rules. While tax deductions generally are not available for capital expenditure on land and buildings, an immediate tax deduction may be claimed where the buildings are used for R&D purposes, providing an absolute tax benefit.

Eligible industries and qualifying costs

The type of industry has no bearing on the availability of the incentive. Qualification is based solely on the nature of the activities.

Companies may claim the incentive for their expenditure on the following:

- Staff costs for employees who are directly and actively engaged in carrying out R&D.
- Contracted individuals working under the supervision, direction, or control of the company where their services are provided through a third-party staff provider. The costs are limited to 65% of the payments where the staff provider is unconnected, and to the underlying staff costs where the staff provider is a connected entity.
- SMEs may claim 65% of R&D-related subcontracting costs. Large companies can claim up to 100% of subcontracting costs, but only where they are paid to a university, health authority, charity, scientific research organization, individual, or a firm where each member is an individual.
- Large companies may include contributions made to independent R&D that is relevant to their business, and is undertaken by a university, health authority, charity, scientific research organization, individual, or a firm where each member is an individual.

- Software or consumable items used in the R&D process, although consumables may not be included in an R&D claim where they form part of a product that is sold or otherwise transferred in the ordinary course of business.
- Payments to volunteers for participating in clinical trials.

Expenditure on rent, land, patents, and patent protection are not included.

Large companies may claim the relief on costs associated with work that is contracted to them provided it was contracted by another large company, or a person not subject to UK tax, e.g., a UK large company performs research for a US company that is not subject to UK tax.

SMEs cannot claim the more advantageous SME relief on costs that are subsidized or related to activities that were contracted to them, although they may be able to make a claim under the less generous large company scheme for the excluded expenditure.

IP and jurisdictional restrictions

There is no IP ownership requirement under the UK R&D schemes, and it is not necessary for the employees or contract staff undertaking the work to be doing so within the UK.

Patent box

A patent box regime introduced for profits earned on or after 1 April 2013 from patented inventions and certain other innovations enables companies to apply a lower rate of corporation tax. The relief has been phased in and, as from 1 April 2017, effectively applies a 10% rate of corporation tax to profits generated from qualifying patents.

The OECD's BEPS project has driven a change in preferential intangibles regimes, including the UK's patent box. These changes, which apply as from 1 July 2016, require a company to demonstrate a nexus between the profits falling within the patent box and the R&D activities that generated the underlying technology. Companies that elected into the patent box by 1 July 2016 may be eligible to be grandfathered until 30 June 2021.

The "new" regime requires claimant companies to track their R&D expenses and how they relate to specific patents, products, or product families, creating a much stronger link between the R&D tax relief and the patent box regime.

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R&D grant (EU)

There is an extensive program of calls provided by the EU. Some permit a company to apply directly, while many require collaboration between three or more partners (including the UK applicant) from three or more EU member states. The UK left the EU on 31 January 2020 and is no longer eligible to qualify for EU grant assistance, although a UK applicant still may participate in an EU funded project. (This is subject to further negotiation with the EU which is expected to be concluded by the end of 2020.) An SME for these purposes is defined as a company with less than 250 employees, and either turnover not exceeding EUR 50 million, or balance sheet total not exceeding EUR 43 million.

R&D grant (national)

Assistance may be available in response to a specific call or based on a direct application. The assistance level will depend on the nature of the work packages and whether they qualify as industrial research or experimental development. If an SME also benefits from R&D tax incentives, the company must consider that the award of the grant may reduce otherwise qualifying R&D expenditure, or, if the grant constitutes state aid, exclude the whole project from the SME R&D tax incentive regime. Maximum grants are up to 50% and 70% of qualifying costs for large companies and SMEs respectively. An SME is defined as under "R&D grant (EU)," above.

All national R&D grant programs currently comply with EU state aid rules. However, this is subject to further negotiation with the EU, which is expected to be concluded by the end of 2020.

Investment incentives

CAPEX/employment

This scheme encourages investment by private sector companies in medium term (three- to five-year) investment plans that involve capital expenditure and the creation of net new jobs and/or the safeguarding of jobs that otherwise may be lost. For service sector projects, the grant may be influenced by the salary costs of the net new jobs to be created. In all cases, a need for assistance must be demonstrated. Cash grants of up to 25% or 45% of qualifying costs are available to large companies or SMEs, respectively. An SME is defined as under "R&D grant (EU)," above.

Training

Assistance may be available to support additional training for new recruits and/or upskilling of the existing workforce. Eligibility rules are defined by EU state aid rules. Cash grants of up to 50% or

70% of qualifying costs are available to large companies or SMEs, respectively. An SME is defined as under "R&D grant (EU)," above.

All national grant programs for CAPEX/employment and training currently comply with EU state aid rules. However, this is subject to further negotiation with the EU, which is expected to be concluded by the end of 2020.

Annual investment allowance (AIA)

The AIA is a government tax incentive to encourage businesses to invest in plant and machinery. Businesses can write off 100% of capital expenditure qualifying for plant and machinery allowances in either the plant or special rate pools up to a set limit (temporarily increased to GBP 1 million from GBP 200,000 as from 1 January 2019 through 31 December 2020) against taxable profits for the same period. Any qualifying expenditure over the limit is subject to the normal writing down allowances of 18% or 6%. AIAs are not available to trusts or mixed partnerships, and group or related companies under common control receive a single allowance.

Enterprise zones (EZs)

EZs are designated areas set up to incentivize business investment in these areas through business rates discounts, enhanced capital allowances (ECAs), and government support for businesses. Established in 2012, there are 48 EZs across England, 16 in Scotland, eight in Wales, and one in Northern Ireland.

Benefits available to businesses that locate in an EZ include the following:

- Up to a 100% business rates discount worth up to GBP 275,000 per business over a five-year period;
- A simplified local authority planning procedure; and
- High speed broadband throughout the zone.

In some EZs, accelerated tax relief through ECAs are available, providing 100% relief in the year of expenditure for large investments in plant and machinery purchased before April 2020 (see "ECAs," below). ECAs cannot be claimed where other forms of state aid are received.

There are rules relating to the timing of the investment.

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Environmental sustainability incentives

Intensive energy use

Where energy-intensive sectors demonstrate that energy is a substantial cost component of their products and that the imposition of climate change levy (CCL) on energy costs will make the sector uncompetitive, the UK government may agree to significantly reduced rates of CCL in return for a commitment to reduce energy consumption and carbon dioxide emissions under a climate change agreement. As from 1 April 2020, there is a maximum tax reduction of 92% for electricity, 77% for liquefied petroleum gas, and 81% for gas and any other taxable commodities. The discount for gas will increase to 83% from 1 April 2021.

The government announced in Budget 2018 that, as part of a longer term plan to equalize the rates of carbon tax applying to gas and electricity, the rate of CCL applying to electricity will fall during the years 2020-22, while the rate of CCL on gas will be increased. As a result, the level of the tax reduction available for eligible sectors will be adjusted to recognize the changes in the carbon tax rates.

EU emissions trading system (EU ETS)

The EU ETS works on a “cap and trade” basis, so there is a cap set on the total greenhouse gas emissions allowed by all participants in relation to installations covered by the system (e.g., power stations, oil refineries, and industries that produce iron, steel, chemicals, etc.). The cap is reduced over time so that total emissions fall.

Businesses operating the installations must acquire (and then surrender) sufficient emissions allowances to meet their installation’s cap. Companies receive or buy emission allowances that they can trade with one another as needed. They also may purchase limited amounts of international credits from emission-saving projects globally.

Heavy fines are imposed where a company is unable to surrender adequate allowances each year to cover all its emissions. Where a company reduces its emissions below the cap, it may keep the spare allowances to cover its future needs, or sell them to another company that is short of allowances.

The EU ETS is supported in the UK by the carbon price floor (CPF). The CPF is intended to underpin the price of carbon at a level that encourages low carbon investment. The CPF taxes fossil fuels used to generate electricity through the carbon price support rate of CCL.

At the end of the transition period for the UK’s departure from the EU, the UK no longer will be part of the EU ETS. The UK government has indicated that it is committed to carbon pricing as a key policy tool for decarbonizing the economy but it currently is unclear whether a UK ETS or a carbon emissions tax will replace the EU ETS.

Small scale renewable generation support

Innovative and environmentally friendly generation technologies may be eligible for support in the form of cash incentives from regulated energy utilities. In practice, this support usually is in the form of tariff payments made to the generator under the feed-in tariff (FIT) scheme for each megawatt of qualifying renewable energy generated. A higher value tariff typically is paid for energy that is surplus to the generator’s own needs.

The FIT scheme is an incentive that supports small scale renewable and low carbon electricity installations up to a capacity of five megawatts, or two kilowatts for combined heat and power. Generators are paid a tariff for the electricity units produced through qualifying generation assets (e.g., solar, wind, and hydro). The tariff varies depending on specified factors and is paid from energy suppliers. The FIT scheme generally closed to new applicants as from 1 April 2019, with some exceptions.

Large-scale renewable generation support (renewables obligation)

Several tradable certificates are available to large-scale renewable generation assets, such as renewable obligation certificates (ROCs) and renewable guarantees of origin. Traded commercially, the value of these certificates is subject to market forces. In the case of ROCs, an annual “true-up” of the scheme usually leads to additional cash payments to participating generators. The ROC regime was closed for new generating capacity after 31 March 2017.

Contracts for Difference (CfD)

This scheme is designed to act as an incentive for investment in renewable energy as it provides project developers who incur significant upfront costs and are involved in long-term projects with direct protection from variable wholesale prices, while protecting consumers from paying higher costs when electricity prices are high.

UK renewable generators that meet specific requirements may apply for CfD by way of a “sealed bid” process.

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Successful developers of renewable projects enter into a private law contract with a government-owned company, the Low Carbon Contracts Company. As a result, developers are paid a flat (indexed) rate for the following 15-year period of their electricity production.

Resources taxes recycled into local communities (funding for environmental projects and funding projects to reduce the impact of the extraction industry)

Environmentally driven research and smaller local community projects can be supported by “grants” funded from certain resource taxes and limited by the annual value of the tax receipts (e.g., the Landfill Communities Fund from landfill tax).

ECAs

ECAs provide a 100% tax deduction in the year of expenditure on assets that are energy or water efficient and are included on the government’s “Energy Technology Product List” or “Water Technology Product List,” or meet specific criteria as set out on the “Energy Technology Criteria List.” It may be possible to surrender the allowances for a 19% tax credit where the company is in a loss making position.

Capital allowances including ECAs are not available where the expenditure incurred on an asset is met by another entity. In these circumstances, where the parties are not connected, it may be possible for the contributor to claim capital allowances in relation to any payments made towards qualifying assets. Relief would be available at 18% or 6% per annum, depending on the nature of the underlying assets.

ECAs generally are available for qualifying plant and machinery purchased before 1 April 2020. ECAs are to be extended to 31 March 2023 for companies investing in electric vehicle charge points. This will help achieve the government’s ambition for the UK to become a world-leader in the ultra-low emission vehicle market.

