

HMRC's Consultation on Advanced Clearances (closed May 26th)

Question 1:

The R&D Community is a membership body for accountants and consultants working in R&D tax relief. We support and represent around 80 firms or companies, and recently hosted a workshop to give members a chance to discuss the key ideas within this consultation.

Questions 2-4: Not applicable

Question 5: Where does your business operate? (please select all that apply)

The R&D Community Ltd is based in Edinburgh, with its members distributed across the UK.

Question 6: Please provide your company's or organisation's name unless you are responding on your own behalf.

The R&D Community (representing the views of our members).

Question 7: Please provide the best email address we can use to contact you.

contact@the-randd-commnity.co.uk

Question 8: To help us monitor the demographic of respondents, please provide the postcode for your company or organisation. EH3 9DR

Question 9: Were you aware of the advance assurance scheme before this consultation?

The majority of our members were aware of the advance assurance scheme before this consultation.

Question 10: Have you or your clients used the current advance assurance scheme?

When we raised this question with our members during our workshop, none of the attending members had had direct experience of the advance assurance scheme. However, some knew or had previously spoken with people who had used it.

Question 11: If you or your clients have used the current advance assurance scheme, please tell us if and how this met your needs.

N/A.

Question 12: If you or your clients have used the current advance assurance scheme, please tell us about what worked less well in the process.

N/A.

Question 13: For those who are aware of the current advance assurances, but chose not to use them, what were the reasons for this?

The main issue seemed to be a general perception that applying for advanced assurance was more work than simply preparing and submitting a claim. Statistically, it was felt that claimants faced a choice between:

- Applying for advance assurance (with a 100% probability of having to convince HMRC about why their work qualified) and
- Submitting the claim without assurance (with an approximate 20% probability of having to justify their claim to HMRC as part of the enquiry process, albeit with the risk of penalties for any inaccuracies).

This meant that advance assurance was generally seen as a barrier to receiving relief, whilst not necessarily guaranteeing protection from further questions or compliance activity should the project(s) be amended.

Members also felt that if taxpayers take professional tax advice when submitting claims for R&D tax relief, or are otherwise knowledgeable about the requirements of the scheme, it seemed superfluous to ask HMRC to double-check the basis for the claims.

The restricted scope of the current advance assurance scheme was also cited as a reason for its limited uptake. For example, there is a requirement that the company's R&D must not change significantly once approval has been granted.

However, the majority of innovative, start-up companies are unlikely to be able to predict with great certainty what form their R&D activities will take in their second or third accounting periods – making it likely that any advance assurance would not be valid for long. (In our members' experience, many start-ups had to be highly responsive to changes in market conditions and emerging technologies, making it extremely difficult for them to predict the direction of their R&D in a few months, let alone over a period of 3 years.)

Also, some qualifying projects may only be active within one accounting period, so any assurance given could be of limited value when compared to the work involved in applying for it.

Question 14: Is the current focus in advance assurances on treatment of a whole claim right or should it focus on a particular issue or number of issues in a claim? (please select)

- focus on the whole claim
- focus on one particular issue in the claim
- focus on more than one particular issue in the claim

Question 15: Which issues in R&D claims are of the most concern?

Our members felt that the following issues were likely to be most commonly raised:

- **Contracted out R&D**
This remains a complex and nuanced area, so it seems likely that companies would want assurance that they would be able to claim for the costs of their contractors (or conversely, that they would be able to make a legitimate claim for R&D activities they decided to undertake while acting as a contractor).
- **Exemptions from the overseas expenditure restrictions**
Similarly, the exemption rules for the overseas expenditure restrictions involve an element of judgement and subjectivity. Where a company is considering significant expenditure on an overseas contractor, it may wish to get confirmation that it would be allowed to claim relief under the exemption rules.
- **Area of science or technology**
There are some areas of industry that are near (or on) the intersection of medical science and social science e.g. software or devices developed with healthcare applications. Where it is not immediately obvious whether a particular area falls

under 'hard' or social science, members felt that companies would be likely to value confirmation of this from HMRC.

- **Competent Professionals**

In some cases it might not be easy to distinguish between a qualified expert and someone who has attained a level of competence through self-directed, experiential learning. In these situations, companies might wish assurance that HMRC would indeed regard their key people as competent professionals (based on their qualifications, experience and track record).

- **Has the definition of R&D been met? (Or is it likely to be met?)**

Finally, and most obviously, companies will want assurance that the work they have conducted (or are planning to conduct) constitutes R&D for tax purposes. As part of this, they are likely to seek assurance that a) their intended advance is considered appreciable b) that it represents an advance over the baseline for their sector and c) that work to resolve technological uncertainty took place.

Question 16: Do you have any views on the current criteria for eligibility for advance assurances?

Generally, as detailed in the answer to Question 13, our members felt the current criteria were too restrictive and the assurance granted too limited in scope.

Question 17: Can you foresee circumstances in which paid-for voluntary assurances might be attractive?

Our members were generally not in favour of paid-for voluntary assurances, as this could restrict any assurance mechanism to companies able to pay for this service.

Additionally, it was felt that if a company wanted to voluntarily engage with HMRC to ensure that its claim was compliant, it should be offered a basic level of assistance for free (especially as during compliance checks, companies are often asked if they contacted HMRC before making a claim, suggesting that there needs to be a responsive and reliable mechanism for them to do so.)

Suggestions proposed were that HMRC could offer a helpline for claimants and/or their advisors, so that more straightforward queries could be addressed outside a formal advance clearance process. However, there was some cynicism about HMRC's ability to provide that service, given advisors' experience of response times from the RD.IncentivesReliefs@hmrc.gov.uk address.

Question 18: Do you agree that a voluntary service could be focused on growing and high-potential companies as well as sectors set out in the government's Industrial Strategy?

If HMRC's intent is to reduce error and fraud, and to promote greater certainty to all taxpayers seeking to claim R&D tax relief, it is unclear how both of these objectives would be met by offering a voluntary service only to certain types of company.

To have the greatest chance of reducing error across the various R&D schemes, members felt that a voluntary service should be available to *any* company that had legitimate concerns or questions about the eligibility of its work. That support could be provided in a variety of ways, perhaps via a helpline, informal meetings, or a paid service, as mooted at Question 17.

Question 19: If not, at which companies should a voluntary service be focused?

Our members generally expressed the opinion that at least some form of voluntary service should be made available to *all* companies that wished to verify the correctness of their approach before making the submission on the tax return.

However, to deliver this in a more scalable way, it was suggested that there could be different levels of service, from helpline queries and informal meetings all the way through to a more heavyweight service designed to provide certainty in more complex matters.

Question 20: Do you agree there is a minimum expenditure below which significant R&D does not take place?

This idea was not supported by the majority of our members, who largely felt that the introduction of a Minimum Expenditure Threshold (MET) could unfairly restrict the availability of relief for start-up companies with limited resources that were nevertheless conducting qualifying work. Some advisors expressed concerns that the R&D scheme was becoming too focused on the needs of very large companies, and that this would have unintended economic consequences in the future.

There were also concerns that the introduction of an MET could require smaller companies to commit resources to evaluating their projects and expenditure only to then find that the MET was not met. This would be a waste of precious resources for companies with few to begin with.

Furthermore, it was noted that the introduction of a MET could lead to an increase in deliberate error and fraud, as some companies will inevitably manipulate their figures to ensure that MET conditions are met.

Question 21: If yes, please give that level (in thousands)

Our members were generally not supportive about the introduction of a MET.

Question 22: Do you agree that the assurances should be mandatory for some?

Our members expressed the view that if advanced assurance was mandatory for all, this would significantly reduce the amount of error and fraud associated with R&D claims. However, it was recognised that the resources required to deliver this would be too large to be feasible.

As a fall-back, members largely agreed that the assurance process should be mandatory for certain high-risk sectors or companies. However it was pointed out that the targeting would need to be designed with care – SIC codes can be easily changed and manipulated to evade scrutiny.

Question 23: If so, what factors should be considered in determining who must seek assurance?

Our members felt that high-risk claims do not only come from high-risk sectors – significant error is also likely to occur when a company:

- Has not involved competent professionals in its R&D;
- Has a limited understanding of the rules and requirements of the R&D scheme; and
- Is using an R&D advisor with an aggressive approach or questionable track record.

One of our members suggested that the AIF could be modified to capture more information (for example, on the competent professionals involved, and/or the details of any relevant R&D scheme training recently undertaken by the company). This could then be used to identify high risk claims, with HMRC then mandating that these selected companies engage in the advance clearance process. In other words, the selection criteria could be far more dynamic and nuanced than merely using data like SIC codes.

Question 24: How can HMRC best recognise the role of agents in designing a clearance service?

The AIF already requires all agents involved in the claim to be disclosed. HMRC could make risk assessment decisions based on the data it has built up on tax advisors, and this could be

augmented by evidence that the advisor has undertaken recent relevant CPD in R&D tax relief, or structured, independent training and certification in this area.

The perception of several of our (regulated) members was that some of the professional bodies appeared not to provide much practical, in-depth R&D training or detailed help or oversight, possibly because R&D is now perceived as a high-risk area from a reputational perspective. These members observed that it would be invaluable if the professional bodies could provide more R&D-specific training and support, either by developing this internally or by engaging with third parties that already have this capability.

Additionally, in the context of last year's consultation on raising standards in tax, many of our members felt it important to highlight that membership of a professional body is not necessarily a hallmark of expertise in this area: competent and ethical tax professionals can be found both within and outside the various professional bodies.

On a related point, the introduction of a mandatory advance clearance scheme will increase the work required to prepare a claim for certain types of companies. This could, in turn, lead to a barrier to new R&D advisors providing professional tax services, which may lead to a restriction in the availability of good tax advice for companies seeking to make a claim. This could exacerbate the current trend of smaller accountants leaving the market due to perceptions that the R&D scheme is now too complex and risky to offer to their clients.

Question 25: Do you see value in pre-activity advance assurance?

Our members generally felt that some form of pre-activity support from HMRC would be useful to companies considering various forms of work (or contractual arrangements). However, it was assumed that this early support would lead to largely hypothetical or heavily caveated assurance i.e. 'If you carry out the work on this basis, it might qualify – as long as all your costs are accurate'.

However, as we noted previously, it is very common for companies to need to quickly change the direction of their R&D as they learn more about the market and other competing technologies continue to emerge and mature. It is therefore hard to imagine that a high percentage of assurance given at the pre-activity stage would still apply after the company had carried out the work. By its very nature, the direction of R&D can be hard to predict.

The second obvious problem is one of HMRC's capacity. While it might be possible to provide companies with relatively light-touch assistance (such as informal guidance given in online meetings), the popularity of this service could make it very time-consuming to deliver. It occurred to us (speaking as The R&D Community) that a significant proportion of companies' information requests could perhaps be met through developing a targeted set of training resources, delivered online and on a 24/7 basis so as to be as convenient and

scalable as possible. If we were to provide this for free, or on a low-cost basis, this could potentially take some of the educational burden away from HMRC, allowing it to engage at a higher level with those who have already completed the relevant training or educational resources.

Question 26: If so, what sorts of issue might be raised with HMRC?

The feeling was that pre-activity assurance would be most effective in providing general recommendations on how companies should align with HMRC's expectations for compliant claims, particularly in the areas of record keeping and recording evidence, and potentially greater awareness in the categories of expenditure that could potentially qualify for relief. However, the same issues outlined in our answer to Question 15 could reasonably be expected to be brought up too.

Question 27: What sort of information might companies be able to provide to HMRC at this stage?

At the pre-activity stage, it was felt that a company should be likely able to provide an initial baseline assessment of knowledge and capability and be able to describe early-stage technological uncertainties associated with the advance sought. It's also likely that the company would be able to give details about the competent professionals who it intended to lead the work.

However, information about specific activities, potentially qualifying costs and staff involvement could be limited, and the duration and longer-term direction of the project uncertain.

Question 28: Which of the options A to C do you think would be most useful? (please rate all options: not useful, somewhat useful, useful)

Our members generally favoured option B, mandatory pre-claim advanced clearance, and thought this would be useful.

Options A, voluntary pre-activity assurance, and C, voluntary post-claim pre-payment assurance were considered somewhat useful.

Question 29: Please give reasons.

Option B was considered most useful, as it would allow companies within specified sectors to correct errors before making a claim and hence reduce the chance of penalties.

An additional suggestion was that mandatory pre-claim assurance could be extended to companies that did not appear (perhaps on the basis of information in an extended AIF) to have access to competent professionals or tax advisors with relevant CPD or training in R&D tax relief.

However, it was noted that if HMRC were able to provide a responsive helpline service to *all* agents and taxpayers wishing to discuss aspects of a claim pre-submission, this could be run in parallel to advance clearances and make a significant contribution to reducing error within claims for relief.

In terms of the scope of the pre-claim assurance, while there is an intention to provide binding assurance for the claim, this would require the company to have finalised all of the necessary costs and information. This may delay the point at which many companies are ready to go through the advance clearance process.

An alternative approach would be to split the scope into two parts. The first could focus on an assessment of the projects' eligibility and the company's competent professionals, while the second could focus on the costs/contracted out issues/claim methodology/tax return. This would allow HMRC to identify significant issues quickly in part one (such as the company not having access to competent professionals or the work not qualifying as R&D), with more refined and detailed issues examined in part two (if the company successfully passed the checks in part one).

In terms of the other options:

- Option A was considered somewhat useful for start-up companies wishing to secure investment to enable R&D activities to commence, but it was noted that the early / indicative assurance granted would likely have limited scope and long-term benefit.
- Option C was considered somewhat useful for more mature businesses going through acquisition or those wishing greater certainty around retaining any tax benefit associated with their claim(s). However, this option would be more valuable if it were open to all companies, rather than just growing and high potential companies.

Question 30: Please give any other suggestions you have for useful changes to R&D relief administration, particularly those that would address error and fraud.

Final points and observations:

- Some of our members noted that a more effective means of raising certainty for taxpayers would be an appropriately staffed HMRC helpline, where taxpayers and/or advisors could discuss their R&D claims to ensure a compliant approach.
- While HMRC provides this level of support for large companies, the lack of similar support for smaller companies can be frustrating.
- In September 2024, HMRC reported a 21% decline in R&D claims being made for the 22/23 tax year compared to the previous year. Our members suggested that perhaps HMRC could divert resources freed up by this decline in claims to providing a helpline service.
- Some of our members suggested that the AIF could be expanded to incorporate elements of an advanced clearance process. The AIF does not count as claim submission, and it is often completed well in advance of submission of the tax return. This suggests that the AIF could act as a trigger for a mandatory advanced clearance process, in cases where potential areas of concern are identified. Furthermore, it is at the point of AIF submission where a company has committed to making a claim, so it should by that point have all the evidence required by HMRC for assurance purposes.
- Our members expressed a desire for HMRC to offer more face to face online discussions with taxpayers and their advisors to resolve issues with R&D claims. This would help companies understand the application of the legislation and could be a faster way to avoid or resolve enquiries.
- Our members proposed that HMRC could consider involving other government/professional bodies in the advance assurance process to ensure that any assessment of a project's or claim's eligibility would be based on the opinion of an independent competent professional.
- Our members recognise that a proportion of error and fraud associated with R&D claims is associated with taxpayer non-compliance, whereas other error and fraud stems from poor or misleading advice given by tax advisors. If access to free or low-cost training were made more readily available concerning the compilation of compliant R&D tax relief claims, this would contribute to a better awareness of the requirements. In turn, this could reduce the burden on HMRC, improve the standard of submissions, and enable companies to more readily challenge poor professional advice.
- There were concerns from our members that any advance clearance scheme could be misused by HMRC to reject claims without resorting to an in-depth compliance check, thus depriving the taxpayer of the means to formally dispute HMRC's opinion. A clear and transparent dispute resolution process in respect of advance clearance outcomes would likely be necessary.
- Our members raised the concern that the current large business/WMBC/ISBC structure of HMRC already generates a three-tier R&D compliance check system. As this structure is also likely to impact the administration of any advance clearance

system, our members highlighted the need to avoid a situation in which smaller companies are subjected to a materially different standard of advance assurance than large companies.