

R&D tax credits - Life Sciences

Crediting innovation*



The UK Government has recognised that encouraging innovation is a vital component in a strategy for improving the UK's productivity, performance and competitiveness. To this end R&D tax credit schemes are available to Small and Medium Enterprises (SMEs) and large companies.

Industry Specific Issues

Clinical Trial Volunteers

Prior to the 2006 budget, pharmaceutical and biotechnology companies were unable to include payments to volunteers who take part in clinical trials as qualifying expenditure for R&D tax credit purposes. These costs can represent a significant proportion of the R&D expenditure in such companies. From 1 April 2006, qualifying expenditure has been extended to include payments to clinical trial volunteers for large companies. SMEs will also be able to include such expenditure from later this year, but the date has not as yet been confirmed.

Intellectual Property Ownership

Under the SME scheme, the IP created must be vested in the claimant company. This can invalidate the claim where the IP is owned by the parent company and the R&D claim is made by the subsidiary. However, the IP can be jointly vested

with other persons and therefore it may be possible to structure licence agreements in order to ensure the company qualifies for relief. There is no such IP requirement under the large company scheme.

Subsidised R&D

The receipt of grant income can significantly reduce the R&D claim under the SME scheme, but does not necessarily prevent a claim altogether. Specialist advice in respect of R&D tax credits should be sought when applying for any grant income.

Funded R&D does not qualify for relief under the SME scheme. This can cause issues where companies enter into collaboration agreements and specialist advice should be sought when drafting such agreements.

Companies are able to make an R&D claim under the large company scheme in respect of grant funded or subsidised R&D expenditure.

Subcontracting R&D

Under the large company scheme, expenditure on activity sub-contracted to a third party (outside of qualifying bodies such as universities) is not usually eligible for the credit uplift.

If the majority of the work is subcontracted to other companies, such as contract research organisations, it is likely that a significant part of the project expenditure will be ineligible for the

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company, although the CRO may well be able to make a claim. If the work is subcontracted to overseas companies, then this may be qualifying expenditure.

The cost of work carried out by 'externally provided workers' (EPW) under the direction, control or supervision of the company may be eligible. The analysis will be dependent on the legal form and working practices between the EPW and the company.

Capital v Revenue analysis

The tax treatment of the expenditure will be critical in determining the value of the benefit that is potentially available.

If it is determined that the expenditure is capital for tax purposes, the 125% /150% uplift is not claimable, as only revenue expenditure is eligible for this incentive. Capital expenditure attracts a Research and Development Allowance (RDA) which allows for an immediate tax deduction of costs (with no uplift) – resulting in a cash flow benefit as opposed to an absolute benefit.

Recent developments

Reduction in time limit for making claims

Large companies previously had 6 years from the end of the claim period to make a claim. That time limit has now been reduced to 2 years. Therefore companies need to act much faster to ensure that claims are filed in time.

Consumable or Transformable Materials

Expenditure on power, fuel, water and software used in R&D qualifies from April 2004.

How can PwC help?

Identifying Qualifying Expenditure

PwC has expertise and experience in identifying and qualifying R&D and are close to current HMRC thinking and policies.

Claim Computation

There are detailed technical rules in computing the claim amount.

Fast submission of claim, based on PwC experience to maximise your benefits.

Advice on SME status

The distinction between SMEs and large companies is not always clear cut – particularly for marginal companies and those transitioning into large companies.

Recent legislative and definitional changes have made the distinction between SME and large companies more complex.

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