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Tax for innovative companies

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UK R & D Tax Reliefs

BREXIT – Future RD reliefs for innovators?

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RD Reliefs – Proceed with caution

MARIA KITT, Corporate Tax Partner at Tax Insight LLP, takes a look at 'Brexit' and how this may impact tech companies in the UK.

Wrong decision, right time; or right decision wrong time?

Uncertainty is never welcome in any business but the special situation for UK innovators means accessing tax and grant funding at some point in the business' lifetime can provide vital cash flow. What is the future of the RD incentives and can the UK really 'go it alone'?

UK R & D spend is traditionally slow to respond to fiscal change but Brexit goes far beyond simple tax reforms and autonomy. If UK RD tax reliefs can provide up to 32% of expenditure who will begin new RD projects in a period of revived uncertainty? For companies with an international footprint, will the UK remain an attractive location for RD or will the wider EU / US or Tiger Economy marketplaces become even more attractive.

Autonomous tax policy may sound attractive but at what cost and with what incentives?

What's the deal?

If the UK votes to leave the EU, it will assume economic responsibility for its own finances, tax policy and tax harmonisation. This would include the RD tax relief package. But what about grant funding in a reformed 'Innovation economy'? At a glance, RD grant support from EU programmes had paid UK's innovators five times the amount of support from tax reliefs. The Sixth and Seventh EU Framework programmes were especially valuable to the UK. Current EU grant funding for RD is as long term as it is multi sector with over fifty EU RD grant funding programmes currently on offer; the UK will have some way to go to provide long term funding stability and match EU generosity.

RD Tax Reliefs

SME RD tax relief is an EU State Aid. This brings with it a strange variety of EC Regulation including an overall project cap of E7.5m. Hardly onerous rules for smaller innovators, but one could also point to the **seven year** delay in introducing the newer creative sector reliefs, particularly the Video Games Tax

Relief, and similar delay in the **large company RD Expenditure credit**. Both caused largely by delayed EU Approval and amendments.

Who spends what, where?
Worldwide RD expenditure is naturally dominated by large companies and that is certainly the case in the UK. So how international is UK R & D? Where are the UK's main RD marketplaces actually located? More than 80% of UK RD activity is exported (commissioned from abroad), reaching $11bn in 2015. Clearly export markets are key. This pattern has become more pronounced with UK to non UK RD increasing by more than a third since 2007.

The EU is a 'poor relation' in international RD expenditure, ranking third globally behind the US and China. The UK then accounts for less than 10% of the top three investor groups. Impeding the UK's contribution to worldwide RD investment is unlikely to make an international impact. But can the UK really compete on this platform?

Go West?
Quite possibly: The EU is not the only option of course, but then 'Brexit' is not the only economic deal affecting the UK / EU under discussion of course. The secretive 'Transatlantic Trade and Investment Partnership' talks have advanced considerably since talks first began in 2010. Although most of the discussion threads are classified material, the leaking of key strategic policy notes last February showed the appetite for a bilateral US / EU trade partnership, a significant marketplace indeed.
Interestingly, innovative industries (Pharma, telecommunications, and renewables), play key roles in the proposed EU/US deal. Brexit may have far wider repercussions. Taken together, the EU / US market accounts collectively for 60+% of global GDP, a very significant opportunity.

A new Lisbon Treaty?
Not quite. Although the EU can trace its origins to the now obscure coal and steel industry agreements Brexit goes far beyond a simple trade deal. It reflects a range of international dynamics including the US appetite for trade globalisation. The innovative sector will continue to be at the forefront of tax incentive policy.

I'll take that as a 'No' then?
The sheer size of the EU economic opportunity whether bolstered by an EU / US trade partnership or not remains irresistible for many UK techpreneurs. The UK's high propensity to export its RD services is a significant part of the annual £21bn invested in the innovative economy. Clearly any innovative company will want to retain both vital tax and grant funding and open market access.

Perhaps the only certainty is that thirty years on from now, we will no doubt review the reformed UK trade and economic associations and ponder the way ahead yet again.

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