HMRC internal manual

Corporate Intangibles Research and Development Manual

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CIRD162000 - R&D Tax Reliefs: reformed reliefs: contracted out R&D: concise examples

More extensive examples can be found in CIRD162100 (https://www.gov.uk/hmrc-internal-manuals/corporate-intangibles-research-and-development-manual/cird162100).

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In this table, A is the customer, and B is the contractor or subcontractor.

Example	Scenario
1	R&D contracted out by A to B
1A	As example 1, but A is an irrelievable client (CIRD161000)
2	R&D undertaken by B to fulfil a contract for A, but not contracted out by A to B
3	A contracts out R&D to B, which is not relevant R&D of B
4	Variation to a contract – A initially ineligible, becomes eligible to claim
5	Longer contractual chain including a company outside the charge to UK CT (see CIRD161000)
6	Both parties able to claim in respect of a single contract on different R&D projects

Please note that except where otherwise specified the examples assume:

- that the transitional provisions (see CIRD165000 (https://www.gov.uk/hmrc-internal-manuals/corporate-intangibles-research-and-development-manual/cird165000)) are not applicable
- that all activity takes place in the UK
- that A is not an irrelievable client (see CIRD161000 (https://www.gov.uk/hmrc-internal-

manuals/corporate-intangibles-research-and-development-manual/cird161000))

Example 1
Company A undertakes an R&D software project. It engages Company B – also a software development company - as a contractor to undertake an aspect of the development work due to insufficient manpower. This work is R&D. Company A specifies in detail the nature of the R&D work to be done in its subscontract with B. It is clear from the contract that A intended or contemplated that R&D of this sort would be done. A can claim, and B cannot claim.

Example 1A

However, if in example 1 A were an irrelievable client (see CIRD161000 (https://www.gov.uk/hmrc-internal-manuals/corporate-intangibles-research-and-development-manual/cird161000)), B would not be prevented from claiming, assuming all other criteria were met.

Example 2
A company, B, is contracted to provide a product or service which is not R&D, such as constructing a building or developing a software product. From the contract, and the nature of the negotiations to agree it, it is clear to all parties that the customer, A, had no understanding or intention that any R&D should take place. If B undertakes R&D in delivering that product or service, it would be able to claim relief even though it is undertaking R&D on an activity contracted out to it.

Example 3
Company A undertakes an R&D project to develop a drug. As part of this project, it contracts out testing to unconnected Company B, which is relevant R&D of A. This testing is not relevant R&D of B. Whether or not Company B is aware of the existence of Company A's project, the R&D activity done (testing) is the sort of R&D activity that it is reasonable to assume A intended or contemplated

would be done. Company A is able to claim.

This example is developed further in example 6.

Example 4
Company A has a trade of property development. It enters into a contract with company B, a building contractor, to build a residential tower block. When the contract was signed, neither A nor B anticipated that R&D would be required to complete the project. However, in the course of groundworks an unexpected issue with the site is identified. B initially attempts to overcome this by undertaking R&D at its own expense. B can claim for this, because the contract and circumstances make clear that A did not intend or contemplate that R&D of that sort would take place when A entered into the contract. Subsequently, B and A agree a variation to the original contract, which makes allowance for the additional unexpected costs of R&D by raising the contract price. From this point, B is not able to claim, but A is able to claim, because it is clear from the variation to the contract that A intended that R&D of this sort should be carried on.

Example 5
UK Automotive company A subcontracts R&D to an unconnected US company B to develop a new gearbox. The development of the gearbox is R&D in its own right but would also form part of the Company A's R&D. The US company B then subcontracts the work on to its UK subsidiary, a connected party, Company C.

Company A can claim. It subcontracted R&D to another person, and the activity is occurring in the UK so CTA09/S1138A does not apply.

The US company B can't claim (because it is not carrying on a trade chargeable to UK CT).

The UK company doing the work, company C, cannot claim because company A is able to claim.

While Company C has been subcontracted the work by a company not within the charge to tax

(the US parent) and therefore apparently meets the condition in CTA09/S1042F(4)(b), CTA09/S1133(4)(b) applies to the activities subcontracted to company C by the ultimate customer (Company A) but neither CTA09/S1042F(4)(a) nor CTA09/S1042F(4)(b) applies to Company A itself so CTA09/S1042F(3) prevents the UK subsidiary (Company C) from claiming.

Example 6
This example is a continuation of example 3.

Company B encounters an unforeseen difficulty in delivering the testing it has been contracted to perform for Company A. Without renegotiating the contract, B decides to undertake R&D which is relevant to its trade (the R&D relates to improved technology in testing). Whether or not A is aware of B's activities, B can still claim for this R&D, as it is clear from the contract and surrounding circumstances that this is not R&D of the sort A intended or contemplated would be undertaken when the contract was entered into.