

## **R&D: a horror story**

*Paul Rosser relates a brief history of R&D advisor scams – and it makes for shocking reading...*

Since being introduced in 2000 for SMEs and then large companies in 2002, the Research and Development (R&D) tax relief schemes have always been prone to fraud and error. This is due in part to the way a claiming company is allowed to calculate its qualifying R&D spend using reasonable apportionment, and because claims are processed on a self-assessment basis, with very few historically being selected by HMRC for a compliance check.

Overclaiming due to fraud and error, at a cost to the taxpayer, was always a concern, but HMRC tended to focus its attention on the bigger R&D claims. After all, what's the point in tying up valuable resources investigating small R&D claims, where even if discrepancies were found the tax loss prevented would be outweighed by the cost of the investigation?

There were also very few advisors operating and those who did tended to be large accountancy firms, so the number of claims being submitted wasn't that high. In 2008-2009, only 6,600 SME claims were submitted, compared with 2021-2022, when 79,205 SME claims were made.

This way of working continued until around 2014 when, unfortunately, word got out that HMRC weren't doing much to police the R&D tax relief system, especially smaller claims, and there was easy money to be had for anyone willing to convince company owners to unknowingly submit invalid SME claims. So a lot more R&D advisory firms started to spring up, often owned by those with no prior experience in R&D or tax.

Fuelled by misleading marketing statements like '90% of qualifying companies aren't claiming R&D tax credits' and the always-popular 'the Treasury owes Britain's small businesses a staggering £84 billion', this new breed of R&D advisor made millions by convincing company owners that all manner of non-qualifying activities met the criteria for R&D tax relief. And company owners were usually blissfully unaware that their claims were not valid, believing the fallacy told to them by their R&D advisor that once HMRC sent them their payment then their claim had been approved by HMRC.

Despite HMRC being aware of this widespread abuse of the system it did very little to prevent it. Few claims were checked, and advisors knew that if they kept a claim's expenditure below £100,000, the chances of a compliance check were slim. In any case, it was the claiming company who took all the risk.

Some advisors even went so far as to start heavily marketing to sectors that wouldn't be expected to be undertaking much, if any, qualifying R&D – such as

nursing and care homes – and then submitted hundreds of false claims for companies in these sectors.

Finally, at the end of 2020, HMRC decided it was time to do something about fraudulent R&D claims, and the advisors behind them, so they undertook a Mandatory Random Enquiry Program (MREP) to identify the scale of the issue. The results of the MREP showed that around half of all the R&D claims checked contained some level of error or fraud, with the worst offenders being small SME claims.

Since then, HMRC has drastically increased its compliance activities, with a reported 1,900% increase in the number of R&D claims they investigate; these are mostly targeted at advisors they suspect are behind the submission of invalid R&D claims. A new Additional Information Form (AIF), which must be completed to support all R&D claims submitted, was also introduced in August 2023. The AIF was designed to allow HMRC to screen R&D claims much quicker and provide them with information about any advisor involved with the claim to help highlight those being submitted by advisors on HMRC's 'naughty' list.

It has also become a requirement for some companies to pre-notify HMRC that they intend to make a claim within six months of the end of their accounting period. This measure was introduced to make spurious claims less attractive, as advisors targeting companies that haven't yet claimed can usually make a claim for the two most recent accounting periods but now won't be able to. This relates to accounting periods starting after 1 April 2023.

With these new measures, and HMRC's more hostile attitude during enquiries, you would imagine the end of those advisors submitting large numbers of invalid R&D claims. And while we have seen some of the worst offenders liquidated, those who remain have been forced to use even more dubious tactics to ensure they can continue making money out of fraudulent R&D claims.

Such tactics include:

Not using an agent code to submit the AIF: Since HMRC started targeting specific advisors they suspect are submitting invalid R&D claims, some advisors realised that if they get their client to set them up as a user on their online tax account then they could submit an AIF using this, rather than their own agent services account. And if they left the advisor details blank on the AIF this would make it impossible for HMRC to tell they were involved with the claim and increase the chances of it being processed without a compliance check.

HMRC are very clear that advisors must not do this; however, it doesn't deter some. It states: "If you're an agent, you must log in to your agent services account before you can complete an additional information form on your client's behalf. You should not use your client's Government Gateway user ID or access their online tax account."

Fabricating project information: In addition to submitting the AIF using their client's online tax account, some advisors are claiming for projects their clients did not

undertake. Even when HMRC open a compliance check they refuse to provide their client with details of the projects for which they have claimed.

I've spoken to many companies in such a position, and when they finally did get access to project details they found that the projects being claimed for in no way reflected the work they had undertaken. In some cases, they weren't even related to the company's trade.

Compliance checks by proxy: If, after failing to use their own agent code and fabricating the AIF information, an advisor's client is subject to a compliance check, the advisor can still remain anonymous by referring their client to a third party to deal with the compliance check.

Whilst the third party is usually introduced as being 'independent', a quick check on Companies House often shows connections to the original advisor, but HMRC may not undertake this check and so the original advisor can stay hidden.

Using multiple advisory companies: Where a particular advisor is getting a lot of attention from HMRC, it's common practice for the owners to simply setup another company and to start advertising R&D consulting services via the new company instead.

One advisor involved with a dozen invalid claims I've reviewed has at least 11 connected companies set up, all trading from the same address with most of these offering R&D tax relief advisory services.

Making claims without their clients' knowledge: This activity is particularly worrying, and I've spoken to several company owners who claim that they have received a compliance check notification from HMRC for an R&D claim they didn't make.

Upon investigation this appears to be a scam, where a company will sign up with a provider for a package of services, including R&D, whether or not this is relevant to the company. If R&D tax relief is not relevant, then the company owner soon disregards this aspect and is none the wiser that the provider is making a claim on their behalf and without discussing any project details.

In all of the cases of which I'm aware a resulting payment of between £40k and £60k was made directly to, and kept by, the provider.

To date, none of the company owners have been successful in getting the advisor to give them the R&D funds and it is likely that they will have to pay this money back to HMRC even though they have never received it.

HMRC have now (from 1 April 2024) removed the ability for an advisor to have any client payments made to them rather than the claiming company, but how many times this happened prior to this date is anyone's guess.

Liquidating before distributing client funds: Outside of the above, most advisors who receive funds on behalf of their clients would eventually release those funds.

However, some advisors headed toward liquidation would hold onto the funds as long as possible and, in many cases, have no intention of releasing them.

Upon liquidation, many clients not only lose all chance of receiving the funds generated by their R&D claim, but find themselves facing a compliance check

without any support (or having to pay for another advisor). At the end of that process they may need to pay back HMRC for the funds that they never received. The owners of the advisory company, however, are free to set up a new company and start offering R&D advisory services again... and again.

As the fraudulent R&D tax credit market is very lucrative, some advisors are finding more and more ingenious ways to try to avoid HMRC attention, such as the above. In my next article I will look at how HMRC has handled the issue of fraudulent claims, and what action they could potentially take to be more effective.

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