



## **Key Reasons that Lead to a Revenue Audit Failure in Your R&D Tax Credit Claims**

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If you are making R&D tax credit claims and you have never been through a Revenue audit, there are a few things you need to know. First, if you file R&D tax credit claims on a regular basis, the chances of a Revenue intervention are very high. Secondly, Revenue can look at claims made in prior years and if it determines that you have over-claimed it can ask for reimbursement. Thirdly, Revenue may send out a technical person to review the claim. This means Revenue is not just concerned with the claimed amounts, but it also wants to know whether the projects meet the definition of qualifying R&D under tax rules.

There can be significant amounts of funding at stake, if Revenue audits your R&D claims. Therefore, it is worth considering how you would defend an R&D tax credit claim at the time of preparing and submitting it. Being pre-emptive can always help significantly reduce the risk of being audited. To prevent this from happening, it helps to understand what takes place during an audit process, what Revenue would be looking for, and what the most commonly made mistakes are.

### **The Technical Review**

It is one thing to have a few expenses disallowed claimed in error, but it is upsetting if the claimed project does not meet the definition of R&D. Your project may well be genuinely innovative, but if you can't correctly answer the questions posed by the Revenue auditor—who could have a technical background in the area you are making R&D claims—your claim will be disallowed.

Many executives turn their focus on what makes their new product or solution innovative, rather than explain to the Revenue how the development of their product or solution meets the R&D tax credit criteria. The features of a product and what it does are largely irrelevant.

### **Some typical questions you need to be prepared for from a technical auditor:**

1. I did an internet search and it seems that many other companies have developed the same product/solution as you have. Can you explain what due diligence you did at the beginning of the project to ensure that the solution was not already publicly available?
2. In the project descriptions you submitted, you did not explain what technological uncertainties played a role in developing the product/solution. From my viewpoint, the development was routine with no significant technical barriers to overcome. Can you explain the technological uncertainties?
3. I don't see any systematic investigation in the development work. There is no adequate description of what tests were done or the results of the tests and why you moved to the next phase of testing. Can you explain how you passed the systematic investigation test?
4. Given there is no systematic investigation, I don't see an advancement made. What are the advancements made in this field of science?

As you can see in the above, these questions from an auditor can be quite intimidating, especially if you are not prepared for them.

### **Documentation**

Documentation is an area that most companies struggle with as it is hard to keep documentation you don't naturally record. In addition, Revenue is not just looking for time sheets but for evidence that R&D was conducted. This means contemporaneously created documents that can be evidence for the following:

- Technological uncertainties; do you have emails, meeting minutes, reports that point to the discovery of technical obstacle? What the technical obstacle was and whether you determined a solution was publicly available?
- Do you have emails, reports, notes or logs that are evidence of design, build, and test phases of R&D?
- Do you have notes on why you started the project in the first place with search results that indicate the solution to the technical problems were not public knowledge?

### **What Costs Can I Claim?**

Usually costs are straight forward, either they qualify or they don't. However, we have seen errors made in this area simply because companies assumed certain costs qualify without checking eligibility rules. Typically, companies assume that certain overhead costs qualify when they don't, but this usually has minimal affect. The impact is made with the allocation of labour time to R&D. Understanding what activities qualify for R&D is key.

### **Preparing for Audit**

You do not want to attend a Revenue meeting unprepared. You can bet Revenue will have pre-disposed notions about your R&D credit claim. Revenue can be naturally suspicious, if you cannot immediately demonstrate the basis for your R&D claim, with e.g. technical reports detailing the qualifying R&D activities and costs in your R&D projects. The Revenue can also check your website and perform some Google searches on the technology you are developing.

To assist clients in preparing for their audit, RDP conducts mock reviews, which clients find tremendously helpful. In mock reviews difficult questions are asked so that the best answer can be provided when clients meet with the Revenue.

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