

BIA submission: Priorities for Budget 2021

January 2021



Summary

The UK is leading the world into a new age of technological advances that **address humankind's greatest challenges, from a vaccine to free us from COVID-19 to biological fuels that will deliver net-zero carbon**. These innovations are being developed in the UK by companies that are attracting increasing levels of inward global investment. This Government can successfully lead the UK out of the pandemic and forward as a global science superpower by backing this growing sector of economy in Budget 2021. This submission proposed targeted policies that will create more high-value jobs across the UK and leverage even greater private investment. **This is backing winners, not picking them.**

The **UK life sciences industry, which employs 256,100 people, two-thirds outside London and the South East**,¹ is ready to bounce back as the UK emerges from the pandemic. A record level of equity capital has been raised by UK-based biotech companies in 2020, which is ready to be invested into high-value R&D jobs and facilities. This budget is an opportunity to fine-tune the policy and fiscal environment to **ensure that capital is invested in the UK and crystalised into long-term economic benefit, including high-value manufacturing and jobs.**

We recommend the **rapid launch of a new Biomedical Catalyst grant competition** to support the youngest companies that are still vulnerable to the financial impacts of COVID-19 alongside an ambitious public-private **Life Sciences Investment Programme to ensure more developed companies can access the capital they need to scale in the UK.**

A pro-innovation tax regime is also required to attract and lock-in investment in the UK, to secure sticky jobs and manufacturing facilities. We urge the Government to deliver its promise to **include data and cloud computing costs in the R&D tax credits scheme** and to go further to **include capital costs, which would incentivise and attract investment that currently is lost to our international competitors.** Finally, changes to capital gains tax must be carefully considered to avoid suppressing entrepreneurial activity and the value of tax-advantaged employee share options schemes maintained, so that innovative SMEs can continue to compete with larger companies to attract the top talent they need.

Table of recommendations

Increasing access to finance for start-ups and scale-ups	Launch a new Biomedical Catalyst competition in 2021 to support early-stage companies and maintain the pipeline of life sciences innovation
	Deliver the £200m Life Sciences Investment Programme complemented by a bold new co-investment fund of scale to unlock pension funds and other institutional finance to super-charge the growth of innovative UK biotech businesses

¹ UK Government (2019), *Bioscience and health technology sector statistics 2019*: <https://www.gov.uk/government/statistics/bioscience-and-health-technology-sector-statistics-2019>

Maintaining a pro-innovation tax regime	Deliver on the Conservative Party Manifesto commitment to include data and cloud computing in R&D tax credit eligible expenditure
	Expand R&D tax credits to include capital expenditure to incentivise greater investment and support expansion of high-value manufacturing across the UK
	Amend the commencement provisions of the PAYE cap to SME R&D tax credits to ensure fair treatment of genuine companies
	Maintain tax advantaged employee share option schemes for SMEs and extend eligibility to allow them to compete for talent

Introduction and overview of the UK life sciences sector

The UK's R&D-intensive life sciences sector is universally recognised as world-leading, and it delivers great benefits to the economy, the health of the nation, and it is key to the Government's net-zero agenda. From improving patients' lives through new treatments and digital healthcare, to the development of environmentally-sustainable technologies, such as biological fossil fuel substitutes and biodegradable bioplastics, our deep understanding of biology is helping to address humankind's greatest challenges.

It is as a result of having a vibrant UK life science ecosystem that the UK has been able to play a leading role in the global response to the pandemic, putting the UK in a strong position to benefit rapidly from vaccines, diagnostics and therapies. The Oxford/AstraZeneca vaccine encapsulates this: the science came from one of our many world-leading universities, the technology was further developed by Oxford spin-out Vaccitech, the regulatory and global distribution capability was provided by the UK-based multinational giant AZ, and Oxford Biomedica and Cobra Biologics provided their existing UK-based manufacturing capabilities to rapidly scale up domestic production. This has been achieved through a public-private partnership that demonstrates the uniqueness of the UK life sciences ecosystem.

This is a growing sector of the future that poses a unique opportunity. The UK life sciences industry employs 256,100 people, with two-thirds of these jobs outside London and the South East.² There are 6,300 life sciences businesses, 82% of which are SMEs, and combined they generate a turnover of £80.7bn. The average GVA per employee is over twice the UK average at £104,000³ and the sector consistently invests more in R&D than any other (£4.8bn in 2019).⁴ The sector is attracting record levels of investment and overseas investors.⁵

This strength is spread across the UK. The North West is the third most concentrated area for life sciences jobs. Pioneering efforts by Eli Lilly in the early 80s resulted in large scale production of recombinant insulin and human growth hormone there, and the past decade has witnessed significant investments, including Allergan's Biologics R&D Centre of Excellence. Elsewhere, Ipsen manufactures Botox in Wrexham and Fujifilm Diosynth Biotechnologies manufacture complex biological molecules in Stockton-on-Tees. Our sector's heritage shows that when done well, investments in life sciences can deliver long-term prosperity in local regions and play a key role in narrowing the productivity gap.

² UK Government (2019), *Bioscience and health technology sector statistics 2019*: <https://www.gov.uk/government/statistics/bioscience-and-health-technology-sector-statistics-2019>

³ PwC (2017), The economic contribution of the UK life sciences sector: https://www.abpi.org.uk/media/1371/the_economic_contribution_of_the_uk_life_sciences_industry.pdf

⁴ ONS (2020), *Business enterprise research and development, UK: 2019*: <https://www.ons.gov.uk/economy/governmentpublicsectorandtaxes/researchanddevelopmentexpenditure/bulletins/businessenterprisesearchanddevelopment/2019>

⁵ Radnor Capital Partners, commissioned by BIA (2021), *UK quoted biotech performance and investor base in 2020*: <https://www.bioindustry.org/resource-listing/rcp-bia-2020-review-january-2021-final-pdf.html>

The UK is not alone in recognising life sciences as an industry of the future; both the United States and China, among many others, are committing considerable resources to support their life sciences sectors. This submission proposes a fine-tuning of policy to ensure the UK remains at the forefront of this global industry. But the Government must also ensure red tape in other areas does not act as a drag. We recognise the need behind the National Security and Investment Bill and call on the Treasury to ensure the scrutiny unit in the Business Department has the necessary resource and expertise to screen deals rapidly so as not to deter inward investment. Another area of concern is the duplicative red tape and bureaucracy resulting from the UK-EU trade deal that could inhibit the sector's ability to thrive. The EU no longer accepts batch testing of medicinal products conducted in the UK, and from 1 January 2023, the UK is also not planned to accept batch testing of medicinal products conducted in the EU. This results in additional costly testing for both markets, which could easily be removed by signing a Mutual Recognition Agreement with the EU. Failing that, the UK should consider unilaterally continuing to accept batch testing conducted in the EU beyond 2023, protecting medicines supply and fostering a favourable life sciences environment in the UK.

This Government can build on historical success by working with the life sciences industry to improve the health of the population, including building resilience to future pandemics, and to develop and implement environmentally sustainable technologies. In doing so great economic, environmental and societal benefits can be captured, including high-value job creation across the country, new industries of the future and the continuation of the UK's standing as a research and innovation superpower.

Increasing access to finance for start-ups and scale-ups

Launch a new Biomedical Catalyst competition in 2021 to maintain the pipeline of life sciences innovation

The Government has rightly said it will prioritise investment in industries of the future where the UK can take a commanding lead, such as life sciences.⁶ Sector-specific funding streams provide long-term consistency and assurance to researchers and investors that the Government is committed to delivering targeted support for the sector, that funding will be available to their company in the future, and that the grant application will be reviewed by industry experts. These must be balanced with challenge-led funding.

The strength and vibrancy of the UK life science SME community is in large part thanks to the success of the Biomedical Catalyst, a competitive, sector-specific grant funding programme run by Innovate UK. In 2019, an independent analysis from IPSOS Mori⁷, commissioned by Innovate UK and the Medical Research Council (MRC), showed that the Biomedical Catalyst generates £4.72 in public and business value for every £1 invested by government. The study also showed that the programme leverages over £5 of private investment per £1 of public expenditure. As such, the programme outperforms other public funding programmes, which on average leverage £1.40 of private investment from every public £1.⁸ The Biomedical Catalyst therefore provides the new Government with a ready-made vehicle for rapid and efficient investment in life sciences to demonstrate its support for the sector from the outset.

Further statistics on the Biomedical Catalyst:

⁶ UK Government (2019), The Queen's Speech 2019: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/853886/Queen_s_Speech_December_2019_-_background_briefing_notes.pdf

⁷ IPSOS Mori (2019), *Biomedical Catalyst impact evaluation*: <https://www.gov.uk/government/publications/biomedical-catalyst-impact-evaluation>

⁸ HM Government (2019), 'Queen's Speech 2019: background briefing notes': <https://www.gov.uk/government/publications/queens-speech-2019-background-briefing-notes>

- Companies in receipt of Biomedical Catalyst grants increased their R&D investment by 93%, which will help the Government reach its target of raising UK R&D investment to at least 2.4% of GDP by 2027.
- Grants increased employment in companies by 11-15% over 3-5 years, equivalent to creation of up to 330 jobs.
- The 150 companies funded by the Biomedical Catalyst raised as much as £710m in additional VC after receiving the grant. This suggests the grants leveraged £3.99 to £5.09 private investment per £1 of public grant.

While the biotech sector as a whole as seen record levels of investment in 2020, seed and series A investment in the youngest companies was impacted by the pandemic and there has been a 70% reduction in new companies being formed.⁹ Innovate UK grant funding is vital to keep the R&D programmes of these companies progressing during this difficult period of recovery. The 2020 Spending Review allocated funding to Innovate UK that should be used to launch a new Biomedical Catalyst funding competition to ensure the pipeline of life sciences innovation is maintained with new technologies and companies.

Deliver the £200m Life Sciences Investment Programme complemented by a bold new co-investment fund of scale to unlock pension funds and other institutional finance to super-charge the growth of innovative UK biotech businesses

As the UK life sciences SME sector matures, scale-up capital is becoming more critical and a lack of it is holding back growth and global expansion. Despite record sums being raised by the sector, the investment is largely coming from overseas, which is a vulnerability for our domestic sector and means value is not being captured in the UK. Companies are increasingly looking to the US public markets for capital or being sold to larger business before their full potential can be realised, adding a further pull to move operations across the Atlantic, to the possible detriment of the UK science base. Lord Hill's review of listing rules is welcome but it is investor appetite, not stock market rules that are holding back investment.

The Conservatives' announcement of a £200m life sciences scale-up fund prior to the General Election was a welcome measure to address this. Crucially, it will invest in larger and later-stage deals, and could provide the British Business Bank/British Patient Capital with in-house expertise to expedite investment in the life sciences sector. However, £200m (+£400m leveraged private capital) is not enough to address the challenge, nor is it specifically leveraging-in UK finance.

The fund must be rolled out as quickly as possible and preferably made more ambitious to ensure the British Business Bank can effectively address the scale-up challenge in the life sciences. We anticipate that a £1bn+ fund is required to provide the scale to support life science companies as they grow and meet demand in the short term as we emerge from the coronavirus pandemic.

To truly address the systemic lack of large-scale investment in UK innovation by our domestic financial industry, the Government must be bolder and lead by example. Initiatives stemming from the 2017 Patient Capital Review have addressed many of the real and perceived barriers for pension and insurance firms to invest in venture capital (the direct contribution pension fee cap remains and we welcome the recent consultation published by the Department for Work and Pensions¹⁰, removing this remaining barrier is critical and requires HM Treasury drive). Yet we are not seeing a change in behaviour within the financial community. The British Business Bank identified the need for a bespoke collective investment vehicle

⁹ BIA analysis, to be published in early February

¹⁰ See the BIA's response here: <https://www.bioindustry.org/resource-listing/30-10-20-bia-letter-to-guy-opperman-mp--dwp--pdf.html>

through which these firms could invest¹¹, but the market has not provided one and there is likely a fear of being the first-mover. The UK Government should therefore address this market failure by creating an innovative and bold new fund structure and leading by example.

Maintaining a pro-innovation tax regime

Deliver on the Conservative Party Manifesto commitment to include data and cloud computing in R&D tax credit eligible expenditure

The small and large business R&D Tax Credit schemes are often cited by BIA members as the most valuable form of innovation support. Tax credits provide a minimal-bureaucracy system that rewards and amplifies companies' own investment in R&D. Continuing them and ensuring they function as intended is critical to maintaining the UK's attractive fiscal environment for R&D investment and achieving the Government's stated ambition to raise R&D investment to 2.4% of GDP by 2027 and make the UK the global hub for life sciences.

We welcomed the Conservative Party manifesto commitment and last year's consultation on the inclusion of expenditure on data and cloud computing as an eligible cost for R&D tax credits¹². This change will help maintain the international competitiveness of the UK's tax regime by bringing it into line with our international competitors, notably America, thus ensuring the UK remains a global destination for life sciences investment.

Expand R&D tax credits to include capital expenditure to incentivise greater investment and support expansion of high-value manufacturing across the UK

Capital expenditure (spending on plant, machinery and buildings) has an essential and growing role in the R&D process and is also required to geographically anchor downstream manufacturing activity, but it is not currently reflected in the R&D tax credit system. As a result, businesses are not incentivised to invest in their own capacity, increasing the possibility of outsourcing to other countries, and the UK R&D tax regime is less competitive for attracting global investment. As manufacturing is disproportionately prevalent in less developed regions of the UK, the inclusion of capital expenditure in the R&D tax regime would support the levelling up agenda and lead to the creation of more well-paid jobs in those areas. Moreover, it would help on-shore medicines manufacturing, which the pandemic has revealed is critical to ensure supply chain security. It would therefore support the Government's Vaccine Delivery Plan, which outlines the need for increasing manufacturing capacity permanently.¹³

R&D Allowances currently exist to promote capital investment but they are not competitive and only benefit profit-making companies, and thus are an ineffective incentive for most life science businesses in the UK that are in the R&D phase and pre-revenue. A new incentive direct through the R&D tax credit is therefore required.

¹¹ Oliver Wyman and the British Business Bank (2019) The Future of DC Pensions: Enabling Access to Venture Capital and Growth Equity: <https://www.british-business-bank.co.uk/research/the-future-of-dc-pensions-enabling-access-to-venture-capital-and-growth-equity/>

¹² See the BIA submission here: <https://www.bioindustry.org/resource-listing/bia-submission-to-the-hmt-consultation-on-the-scope-of-r-d-tax-credits-pdf.html>

¹³ UK Government (2021), UK COVID-19 vaccines delivery plan: <https://www.gov.uk/government/publications/uk-covid-19-vaccines-delivery-plan>

Amend the commencement provisions of the PAYE cap to SME R&D tax credits to ensure fair treatment of genuine companies

The BIA has welcomed the positive and detailed engagement it has had with HM Treasury and HMRC on the proposed PAYE cap to R&D tax credits. The measure was proposed to prevent abuse of the regime but would have had the unintended consequence of severely restricting payments to genuine UK biotech companies. Amendments consulted on since 2018 have addressed many of these problems allowing the cap to achieve its policy objective.

However, the commencement provisions effectively introduce the cap for R&D from 1 April 2021 by splitting straddling periods. It will therefore impact some accounting periods that have already started before the legislation has been finalised or any guidance released. This is a clear deviation from the expectations set through the entire consultation process and, specifically, the most recent round of consultation and the related tax information and impact note published on 12th November. We would like to make a very strong request that the commencement date is amended back to accounting periods beginning on or after April 2021 with no measures for straddling periods and that this is confirmed as soon as possible to provide certainty to companies, many of which will already have set their cashflow forecasts and committed expenditure to R&D.

Maintain tax advantaged employee share option schemes for SMEs and extend eligibility to allow them to compete for talent

The BIA understands that tax increases may be required to address the significant impact of the pandemic on the public finances. It is critical that these changes are targeted to avoid negatively impacting investment and producing a greater loss of economic activity than they generate in tax receipts.

Capital Gains Tax reforms, if explored, must not negatively impact the value of the Enterprise Management Incentive (EMI) share options, which most biotech start-ups and SMEs find essential for attracting and retaining employees at all levels. More than 77% of biotech companies utilise an EMI scheme according to a 2020 survey of employee equity incentives within the industry.¹⁴ All these respondents were from early-stage companies, including Seed, Series A and Series B, which make up the majority of the BIA's membership base.

Previous changes to CGT, when taper relief was removed in 2008, inadvertently negated the EMI scheme, requiring further legislation to re-implement it using entrepreneur's relief. This caused unnecessary disruption to both business and government policy, which the current Government should aim to avoid in any reforms it is considering. Moreover, any changes to EMI schemes amount to retrospective taxation, if they affect options that have already been granted. It is not permitted for companies to make changes to options after they have been granted, and it would be unfair to employees if HM Treasury does not also respect this principle. And forward-looking changes that reduce the value of EMI share options will make it harder for SMEs to compete with larger, more established companies for the talent that they need to innovate and grow in the future.

Furthermore, we would recommend a review of the thresholds for eligibility criteria for gross assets (currently £30m) and number of employees (currently 250). It would be more appropriate to extend this to be closer aligned with the UK SME thresholds for R&D tax credits (500 employees), and the gross asset threshold should no longer be tied to an EU-derived value in Euros.

¹⁴ Confluence Tax (2020), *Biotech Employee Equity Survey 2020* <https://www.confluencetax.com/the-employee-equity-survey-webinar-was-run-for-biotech-companies/>

About the BIA

The BIA is the trade association for innovative life sciences in the UK. Our goal is to secure the UK's position as a global hub and as the best location for innovative research and commercialisation, enabling our world-leading research base to deliver healthcare solutions that can truly make a difference to people's lives.

Our members include:

- Start-ups, biotechnology and innovative life science companies
- Pharmaceutical and technological companies
- Universities, research centres, tech transfer offices, incubators and accelerators
- A wide range of life science service providers: investors, lawyers, IP consultants, IR agencies

We promote an ecosystem that enables innovative life science companies to start and grow successfully and sustainably.

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