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JPA INTERNATIONAL
Audit, Accounting, Tax, Consultancy
A Worldwide Network of Independent Firms

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The International Tax Newsletter

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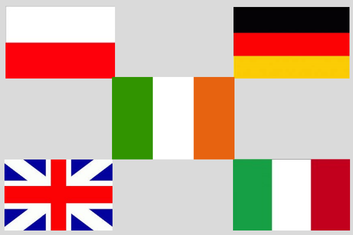
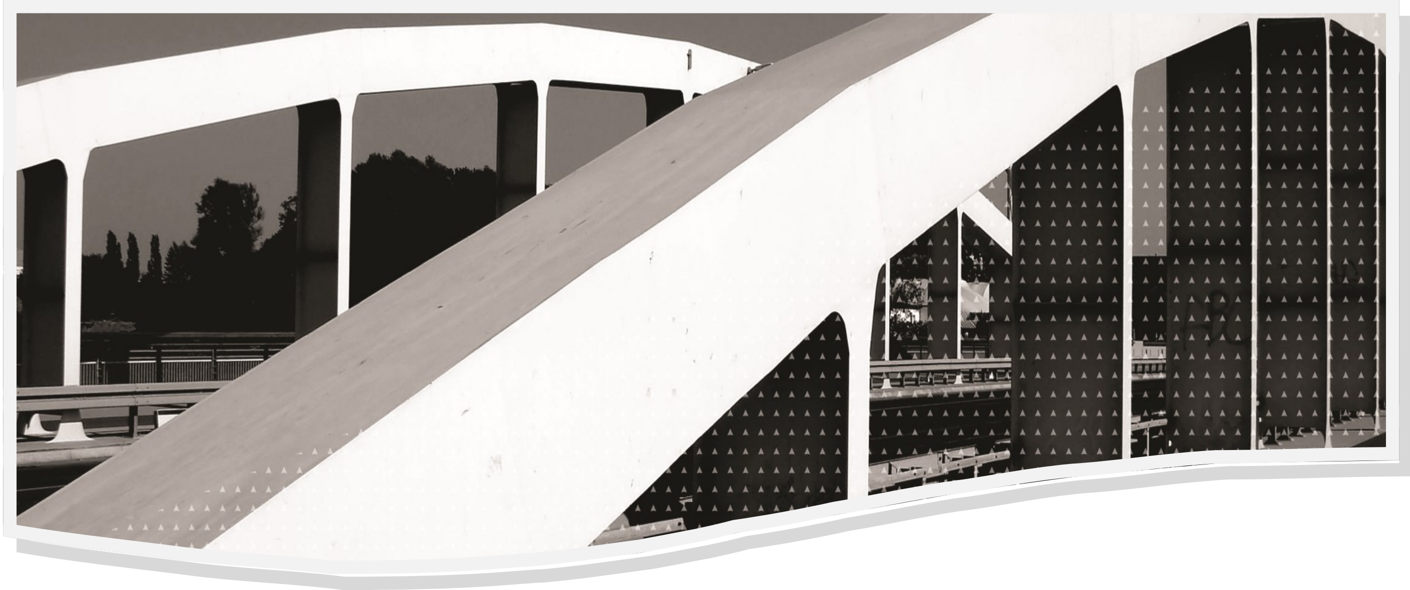




« Countries which sign the Multilateral Instrument will choose which parts of their tax treaties they wish to modify, and with which countries »

Multilateral Convention to Implement Tax Treaty related measures to prevent Base Erosion and Profit Shifting—A revolutionary instrument implementing measures to update international tax rules and reduce the opportunity for tax avoidance

I. Multilateral Instrument (MLI) - What is it?

The MLI is the first multilateral treaty of its kind, allowing jurisdictions to transpose results of the OECD G20 Base Erosion and Profit Shifting (BEPS) project into their existing bilateral income tax treaties.

Thus, the MLI will transform the way tax treaties are modified as there is no need for bilateral treaty renegotiations.

68 jurisdictions have now signed, impacting approximately 1,100 tax treaties when ratified (out of approximately 2,300 tax treaties globally).

The entry into force follows the deposit of the fifth instrument of ratification at the OECD by:

- Slovenia (22 March 2018)
- Austria (22 September 2017)
- Isle of Man (19October 2017)
- Jersey (15 December 2017)
- Poland (23 January 2018).

The entry into force of the MLI on 1 July 2018 will bring it into a legal existence in these 5 jurisdictions.

In accordance with the MLI rules, its content will start having an effect on existing tax treaties as of 2019.

II. MLI—How does it work?

The MLI modifies tax treaties, it does not amend them.

Essentially, it sits beside a tax treaty and modifies the text.

Consolidated tax treaties may be prepared by countries, but they will not be considered as the legal text.

The MLI is written in the OECD's two official languages: English and French. Translation into other languages will likely be available, but the official version is only in these two languages.

Countries which sign the MLI will choose which parts of their tax treaties they wish to modify, and with which countries. The information was released on 7 June 2018 for the 68 countries that signed.

For instance, if two countries wish to apply the MLI, it will modify the text of the existing bilateral tax treaty, once the MLI has been ratified by both countries.

III. Consolidated versions of modified treaties

For most countries, there is no legal requirements to prepare consolidated texts of modified treaties. Indeed, **the MLI does not amend treaties like an amending protocol but modifies them by sitting alongside.**

However, for clarity purposes, many governments may produce some form of consolidated text as guidance for readers.

As the signatories' positions can change significantly until ratification of the MLI, most governments will not start to prepare consolidated versions immediately.

Step 1 • **Entry into force of the MLI**

Step 2 • **Covered Tax Agreement**

Step 3 • **Reservations and choice of optional provisions**

Step 4 • **Notifications of existing provisions**

Step 5 • **Entry into effect of the MLI**

IV. MLI's entry into force

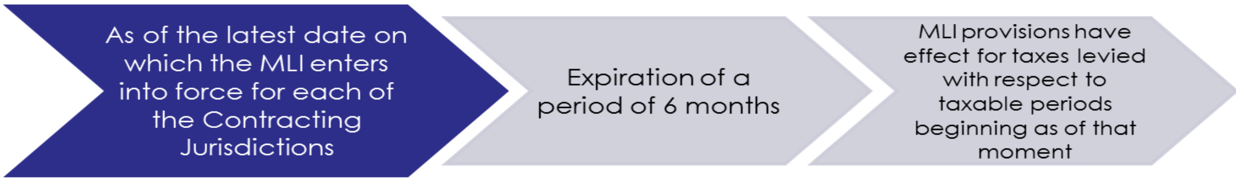
Provided in the Article 34—Entry into force of the MLI:

1. This convention shall enter into force on the first day of the month following the expiration of a period of **three calendar months, beginning on the date of deposit of the fifth instrument** of ratification, acceptance or approval.
2. For each signatory ratifying, accepting or approving this convention after the deposit of the fifth instrument, the convention shall enter into force on the first day of the month following the expiration of a period of three **calendar months beginning on the date of the deposit by such signatory of its instrument** of ratification, acceptance or approval.

V. MLI's entry into effect

With respect to **taxes withheld at source:**

With respect to all other **taxes levied by a contracting jurisdiction:**



The provisional MLI Position of each signatory indicates the tax treaties it intends to cover, the option it has chosen and the reservations it has made.

Signatories can amend their positions until ratification.

Even after ratification, parties can choose to **opt in with respect to optional provisions or to withdraw reservations**. For example, while 25 signatories have chosen to apply the MLI arbitration provisions, other additional signatories can choose to apply those provisions later.

VI. Minimum Standard Provisions

Three articles of the MLI are required:

- Article 6—Purpose of a covered agreement
- Article 7—Prevention of treaty abuse
- Article 16—Mutual agreement procedure.

Article 6 primarily seeks to insert a **statement in the preamble** of tax treaties to remind that the purpose of the treaty is not to create opportunities for double-taxation or reduced taxation through tax avoidance or evasion including treaty shopping.

This being a minimum standard requirement, is mandatory and needs to be incorporated in the tax treaties, either by replacing the existing preamble with the suggested text or adding it if not already included in the tax treaty.

Article 7 gives us **three alternative rules to address situations of treaty abuse**.

The first one is a general anti-abuse rule based on the principal purpose of transactions or arrangements. It is the default choice.

The second one provides a simplified version of a specific anti-abuse rule: the limitation on benefits provision which limits the availability of treaty benefits to persons that meet certain conditions.

The third and last one is a detailed version of the option 2 where a country can make a reservation of the principal purpose of transactions so it does not apply only for covered tax agreements that already have a comprehensive principal purpose of transactions and if the intention is to meet minimum standard.

In essence, signing up to the MLI implies that the country adopts measures to prevent treaty abuse.

Under **Article 16**, the tax payer can approach **competent authority of either of the contracting jurisdiction**.

The tax payer needs to present his case to the competent authority within **three years** of the first notification of the action resulting in taxation, not in accordance with the provisions of the tax treaty.

The agreement reached among competent authorities shall be implemented **irrespective of the time limits in the domestic laws**.

VII. Selected provisions of the MLI which do not constitute minimum standards

Some provisions can be implemented as well but the are not mandatory.

It is the case for dual resident entities, application of methods for elimination of double taxation, dividend transfer transactions, capital gains from alienation of shares or interests of entities deriving their value principally from immovable property.

VIII. Arbitration

The mutual agreement procedure (MAP) article of tax treaties based on OECD and UN Models provides a mechanism to resolve disputes in cases in which a taxpayer considers that he has been taxed in a manner inconsistent with the provisions of the treaty.

One weakness of this mechanism is that the MAP article does not require to parties to resolve the dispute but only to use their best efforts to do so.

As a result, some MAP cases may remain unresolved for long periods or never be resolved when it is not possible to reach an agreement.

Mandatory binding arbitration is a mechanism which, in defined circumstances, obliges the parties to the treaty to submit unresolved issues in a MAP case to an independent and partial decision maker—an arbitration panel.

The decision reached by the arbitration panel is binding on the parties to the treaty and thus resolves the issues than can otherwise prevent agreement in deadlocked MAP cases.

Part VI of the convention is intended to apply only between parties that explicitly choose to apply it.

Article 18 allows a party to choose to apply Part VI with respect to its covered tax agreements by notifying the depositary of its choice.

As between two contracting jurisdictions to a covered tax agreement, Part VI will apply only if both contracting jurisdictions notify the depositary that they choose to apply it.

IX. Tools and guidance

The OECD secretariat is developing tools and guidance on the MLI. The first tools are already available at oe.cd/mli

These tools include interactive flowcharts on each of the substantive MLI articles and the MLI toolkit on the application of the MLI.

JPA INTERNATIONAL CONSULTING IN POLAND

KPFK Dr Piotr Rojek sp. Z.o.o. has been acting as an audit and advisory company since 1990. We are support for our clients in areas of accounting, finance and tax law. KPFK has widely educated team of employees. We develop steadily having today more than 60 employees (also having ACCA qulifications—Association of Chartered Certified Accountant), inluding statutory auditors and tax advisors. Qualifications, knowledge and experience of our team are guarantee of high quality of performed work.

Our mission is to perform services in most professional way for the success of our clients respecting economical turnover security.

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« The tax adviser is an individual who is entitled under the law of his country to carry out, as his main activity, the full range of tax advisory activities for his clients, both business and individuals »

Comparison of the tax profession in our countries—Qualification requirements and regulation in Europ

We always speak so naturally of the « tax adviser » but the tax profession is diverse in form and density of the regulation, professional activities and competences in our different countries.

Some countries distinguish between **tax advisers** and **tax agents.** Others have the concept of **tax representatives** for filing specific tax returns like VAT returns.

Depending on the country a tax adviser is from, the title « tax adviser » may refer to a **particular qualification** or may be **purely functional**, describing one of the activities carried out by a person who is member of another profession, like lawyers or accountants.

The **European Tax Confederation (CFE Tax advisers Europe)** defines the tax adviser as an individual who is entitled under the law of his country to carry out, as his main activity, the full range of tax advisory activities for his clients, both business and individuals.

These include in particular:

- the rendering of advice in tax matters (e.g. tax planning);
- The filing of tax returns and other compliance obligations;
- The representation of the client before the tax authorities (e.g. in the course of a tax audit or an appeal procedure);
- In some countries, legal representation in tax courts or tribunals.

If categorised according to regulation, we distinguish:

- Tax profession is regulated on its own;
- Regulation as lawyers or accoutnants;
- Only title is regulated;
- Voluntary acceptance of qualification requirements;
- No specific qualification requirements.

In most countries, **qualification requirements** exist, in some countries by law, in other countries by professional bodies.

Most common is a three years or more of academic training in economics or law and another three years of practical training.

In general, there is an obligation to engage in continuing professional development. The qualification, once obtained, is normally valid lifelong. However in Russia, the entry exam has to be repeated every two years.

In most countries, there is an overlap with other professional qualifications, especially in countries where tax advisers are not a regulated profession of their own. However in Belgium, tax advisers may not be lawyers, auditors or bookkeepers.

Compatible activities

Some countries have rules on activities considered incompatible with the activity of tax advisory.

For example, “commercial activities” may be seen as potentially harmful to the special responsibility of a tax adviser.

There might be a potential **conflict of interest** and they are characterised by stronger profit seeking. This is the case for Belgium, France and Germany.

Other countries allow tax advisers to engage in commercial activities. In Austria, they must only refrain activity on a commission basis.

What could be an interesting comparison of our professional life for our next meetings

- Legal form: self-employed or tax/law/audit/accounting firm, ownership and control
- Indemnity insurance of the tax adviser: limitation of professional liability, risk insured, cost
- Formal requirements and engagements letters
- Calculation of fees
- Client information
- Rules on advertising
- Cross border mobility
- Tax advice as e-commerce
- Anti money laundering
- EU Anti Tax fraud and tax evasion policy

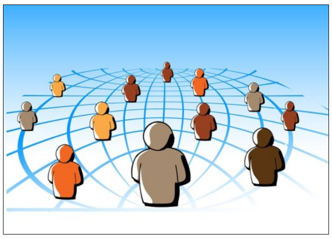
Conclusion

The international tax profession offers a wealth of information that could be interesting to compare through the world.

Having a better understanding of international taxation also goes by understanding the job of the professionals.

The complexity and density are high but thanks to our worldwide network of independent firms in Audit, Accounting, Tax and consultancy, we largely cover the profession and are able to share experiences based on day to day business reality.

Source: CFE Confédération Fiscale Européenne, Rudolf Reibel, European Professional Affairs Handbook for Tax Advisers, Second edition 2013.



JPA INTERNATIONAL IN **GERMANY**

RENTROP & PARTNER is one of the founding members of JPA INTERNATIONAL starting from its head office in Bonn to expand the network all over Germany where at present six different member firms are situated in eight different cities. Nearly all German members have joined JPA Audit AG, a company for common purposes and especially common audit work.

RENTROP & PARTNER, a medium sized company of about 30 people, 10 of them professionals, is serving its clients for more than 50 years with a focus on tax services, consulting and auditing. Hans Ronneberger Wirtschaftsprüfer and Steuerberater, the leading Senior partner, chairman of JPA Audit AG, started his career in PWC as auditor for airline businesses. He is very much engaged now with his team of different professionals to find the right way for medium sized clients in a world of accelerating globalization.

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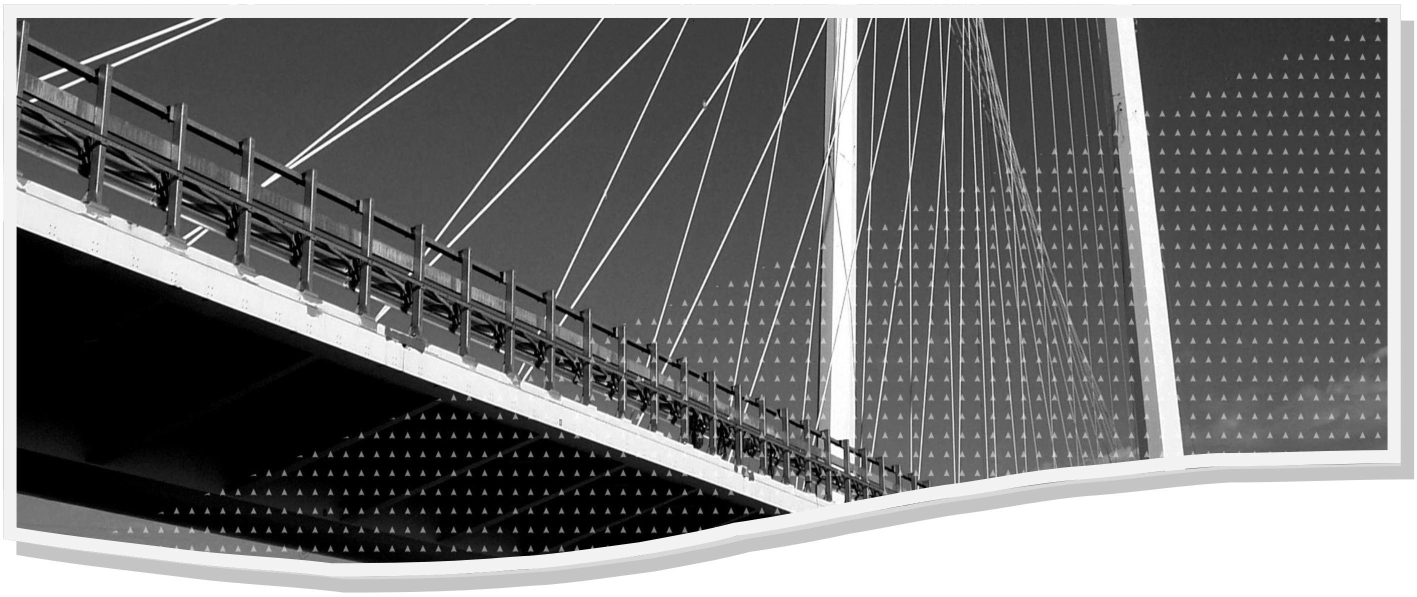

« The new legislation introduced a substitutive tax on all income produced abroad, instead of the ordinary income taxation »

Special Tax Regime for New Italian Residents

The 2017 Italian Tax Bill has introduced Article 24-bis to the Italian Income Tax Code, (ITC) providing for the first time in Italy, a new tax regime for individuals who transfer their residence to Italy.

The new legislation introduced a **substitutive tax on all income produced abroad**, instead of the ordinary income taxation.

Derogating the ordinary "worldwide income taxation principle" in favor of those who, after having lived abroad for many years, move their residence to Italy.

Being this **lump fee tax** a "substitutive tax" of personal income tax (so called "IRPEF"), consequently no rule of ordinary taxation will be applied (i.e. no Italian tax credit is granted for any taxes paid abroad).

Beneficiaries of the special tax regime

The new substitutive regime is available to:

- individuals who have not been tax residents in Italy, according to Article 2 par. 2 of the Italian ITC, for at least nine of the ten previous years before opting for the new regime and moving their residence to Italy;
- According to Article 2, par. 2 of the Italian ITC, individuals who are registered with the Municipal register of resident population for more than half of the tax year (i.e. the calendar year) are deemed to be Italian residents. When fulfilled, this condition is sufficient to irrefutably qualify the taxpayer as an Italian tax resident;
- **Citizenship is not required when applying for the new tax regime;**
- The package can be extended to one or more qualifying related persons (registered partner, children, parents etc. according to Article 433 of the Italian Civil Code);
- Regardless of the tax period in which the package is extended to one or more related persons, the 15 year validity period of the special tax regime starts from the principal taxpayer's option exercise;
- Moreover, the Italian Tax Authority in the Circular Letter No. 17/E of 23rd May 2017 has clarified that the option is inadmissible in any case of ongoing tax assessment.

JPA INTERNATIONAL IN **ITALY**

Studio Righini was founded in the mid nineteen sixties and has been doing business in Verona for 50 years as a firm of chartered accountants and auditors. Today it is a second generation Firm that, by now for over a decade, has also integrated legal advice and Judicial Authority advocacy with its accounting services. Since its establishment the Firm has always distinguished itself for its high quality support for Italian entrepreneurs and for foreign investors who do business in Italy and Italian companies in their internationalization process. The goal of the Firm is to provide professional services that focus on quality. To pursue this goal it has set up various specialized departments that assist Clients according to their specific requirements. The 7 Partners, personally involved in managing the dossiers, assisted by young professionals have different specialized skills but share the same spirit of dedication to ensure expertise and quality to the Clients thanks to their ongoing updating.

Studio Righini, as a member of JPA Italia, provides full and tailored services to facilitate the development of global activities in accordance with the local and international rules.

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JPA Italia provides Accountancy and Taxation, Consultancy, Personnel Administration and Audit services. The firm is built on a solid foundation of ethics where traditional business methods are merged with the most innovative solutions. Strategically located in Milan, Verona, Como and Cernusco, JPA Italia has been providing its services to foreign and Italian companies according to the international standards for over 30 years. Retaining a personal touch, we provide a real alternative to the 'big four': each stage of the processes is customized to meet the unique need of the client. Our services are built by combining various multi-disciplinary skills to guarantee solutions using integrated processes and activities.

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Applying procedure

In order to apply for the substitutive tax regime, the new residents, after moving their residence to Italy, should opt in the new regime through their **Italian tax return** related to the tax year in which they move to Italy and eventually issuing a **preliminary tax ruling request** in order to obtain a confirmation by the Italian Tax Authority that each specific case fulfills the conditions required.

The optional preliminary ruling request shall provide the following information:

- The taxpayer's **personal details**, his **tax code** and, whether available, his **Italian residence address**;
- The **status of non Italian tax resident** for at least the previous **nine years**;
- The name of the **last residence countries** before opting in the new regime;
- The name of any **country he /she wants to opt out** from special regime (so called "cherry picking"). The circular no. 17/E specified that once a country has been opted out, it cannot be included in the regime during the following tax periods. Income produced in those countries will be subject to ordinary taxation;

The taxpayer must also fill in a duly **check list** provided by the Italian Tax Authority, with all information requested.

Termination of the regime

The special Tax treatment can last for **maximum 15 years**.

In any case, it can be **voluntarily terminated** at any time by the tax payer.

It is supposed to be expired if the **tax fee is not paid** by the due date.

The option is void if the Tax Authority confirms that the **conditions required are not met**.

Whether the taxpayer is not admitted to the special regime or in case of voluntary termination, the tax benefit ends **also for family members**, who have opted in.

The Tax Fee

The applying taxpayer will be liable to taxation on the Italian sourced income.

The tax fee is due on the foreign sourced income. The tax fee is a flat tax as following:

The taxpayer opting in	100,000 €	Per eachtax period
Any family members	25,000 €	Per each person applying Per each tax period

Capital gains derived from disposal of qualified capital shares in foreign countries (≥ 25% of the capital; or ≥20% of the voting rights) are expressly excluded from the special regime if realized within the initial 5 years of the validity of the option, and are therefore subject to ordinary taxation on the 58% of the income amount, less any related losses (from 2019, withholding tax of 26%).

The wealth tax (IVIE & IVAFE) are not due, only on the assets held in the countries covered by the options.

If the taxpayer opts for the special regime, he does not have monitoring tax obligations regarding the countries covered by the option.

Income subject to the substitutive tax

The benefit is reflected on the yearly flat imposition of 100,000 € on the foreign-source income.

While the Italian-source of income are subject to the ordinary Italian taxation and also deduction are entitled, with the exception of the one connected to foreign income subject to the substitutive taxation.

To identify the foreign-source income on which the lump sum is due, the Italian tax agency refers to the article 23 of the ICT. Therefore, are considered produced abroad the followings:

- income generated by land and real estate properties located abroad;
- Interest, dividends and similar received from entities located abroad;
- Employment income performed abroad;
- Business income earned from activities done by S.O. abroad;
- Capital Gains earned on the participation in companies resident abroad;
- Other income produced from activities performed abroad.

The 2017 Italian Tax Bill provided that foreign assets are excluded from inheritance and gift tax if the transfer takes place during the period of validity of the option. Assets located in Italy are subject to the ordinary inheritance and gift tax.

The same exemption applies to the transfer of assets located abroad, in connection with the establishment of a trust or other asset protection legal instrument.

German and UK tax advice

Employee share scheme in an international group

This tax case is based on a real experience, a mandate that two of our JPA members worked on.

The background is as follows:

A UK company (UKholdco) is a 100% shareholder of another UK company (UKsubco) which has a 100% subsidiary (GmbH) located in Dusseldorf. The GmbH company has two directors, JS and PH.

The UKholdco is reorganizing its share structure and is offering an employee share reward scheme called tracker shares which track the performance of the underlying subsidiary for dividend distribution), in UKholdco to the 2 directors of the GmbH.

Eventually the tracker shares in UKholdco will be sold when the group is sold.

PH is a British citizen, has been working for the client for many years. He moved to Dusseldorf with his family and is working full time for GmbH since April 2014. He was UK tax resident until April 2014 after which he has been German tax resident.

JS is a German citizen and tax resident, has been a director of the GmbH since moving to Dusseldorf in April 2014.

The questions of the client were as follows:

How can the directors benefit from tracker shares whilst being based in Germany? What are the tax consequences of receiving tracker shares on the two directors of GmbH?

Is the tax applied to a transaction the country of residence at the time of the transaction? Or is it when the shares / options have been granted?

What would the tax rate in Germany be for a disposal of shares (capital gain for the directors) based on current situation?

I. General tax situation

In Germany, the worldwide income of individuals will be taxed in Germany if they are tax resident in Germany. The German income tax law is based on a residence or (common) habitual place (minimum 6 months) and not based on nationality.

To avoid any double taxation the double tax treaty agreement (DTA) between UK and Germany should be considered.

As both directors have their tax residence in Germany, they will be subject to German taxation on their worldwide income or gains subject to the DTA.

In UK, similar rules apply with some particularities. The taxpayer has to live in UK at least 183 days with his main home in UK, working full time in UK. The system is a worldwide taxation of income and gains.

JPA INTERNATIONAL IN UNITED KINGDOM & GERMANY

In today's ever changing tax environment you must be well advised and kept up to date on tax.

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Certainty that your company tax and personal tax liabilities are managed to suit your business goals. And to be certain you are legally only paying the least amount of corporate and personal tax.

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II. What are the consequences of receiving tracker shares on the two directors?

If the directors receive the shares they will be shareholders of UKholdco.

The tax consequences of any transaction (purchase, options, wage income/compensation payment, dividend, disposal) depend on the kind of agreement.

The director can purchase shares based on "market value price". The price is negotiated on arms-length-principles. The purchase is not a benefit for his work as employee.

The director receives the shares as a salary payment (compensation) concerning his work as employee.

Therefore, the tax question is "purchase" or "compensation".

III. What are the tax implications?

1. Purchase

In Germany, if they choose the purchase of shares, the taxation of shares and their income depend on the percentage of the participation of the shareholder in the UKholdco (threshold at 1%).

If less than 1%, there is no taxation on the purchase and the profit on the disposal is taxable. (sale price minus purchase price and sale cost). The tax rate is 26.38% (25% income tax and 5.5% surcharge) on the capital gain and on the dividend also.

If 1% or more, there is no taxation on the purchase and 60% of profit on the disposal is taxable. However, the tax rate is based on the individual income situation of this year. Individual tax rate can be from 14% up to 42%/45% (+5.5% surcharge) for capital gain and dividend.

In UK, if the purchase is made at market value, there is no tax issue regardless holding. If there is sale, the tax rate is at 20% on gain or 10% on gain if the shareholding is higher than 5%, with an entrepreneurs relief available. The dividend taxation is 7.5%/32.5%/38.1%.

2. Compensation

In Germany, if they choose tracker shares or stock options as salary payment, the benefit of a reduced price is taxable. The benefit will be calculated based on the value situation at the time of purchase contract or at the time when you are shareholder.

In case of gratuitous acquisition of shares, the benefit will be calculated at the time when the (incentive) stock option of the share is executed and not at the time when stock options are granted.

The tax rate is the individual income tax rate (see above).

However, if the employee stayed abroad at any time before purchase, the period between granting the option and the vesting time must be divided. Only the benefit of the part of the period is taxable where the employee is not abroad. However, the employee has to provide the German tax authorities with documentation that the abroad benefit is taxed in the foreign country.

In UK, the compensation or shares acquired under value is taxed under the employment related securities legislation (basically income tax).

IV. What would happen if the GmbH was a UK limited company and the group holdco located in Germany?

The shares awarded to officers/employees are charged to income tax if shares not paid or sold for less than market value.

There is no income tax or social security on the grant.

On acquisition of shares, the taxable income is the market value less anything paid on grant of shares. If shares are readily marketable securities, then there will also be social security. The income tax rate is at 20%/40% or 45% and the social security effective rate is 5.625% and for company 13.8%.

A company could loan funds to employee. If the loan interest is free it is considered as employee benefit.

The capital gains tax on increase in value between date of exercise and date of disposal is 20% or 10% (entrepreneurs relief).

If the employee stayed abroad at any time before purchase, it is necessary to consider the period from grant to vesting or exercise of an award or option ('relevant period'). The UK will tax a 'just and equitable' proportion of the award or option equivalent to the proportion of the relevant period during which the employee was UK tax resident.

V. If PH already owns shares in Uksubco (60%), can he swap these for shares in UKholdco?

In Germany, if PH owns less than 1% of shares of the company, in general the swap is neutral (no taxation). Acquisition costs of the shares of the "old" company are now acquisition costs of the "new" company. If you move abroad (to another country) the capital gain is taxable in Germany.

If PH owns 1% or more, in general the swap is not neutral. A swap will be treated as disposal. The capital gain/reserves will be taxable.

PH owns 60% shares in Uksubco and swaps these for 30% in new holdco –there will be capital gains tax on the 60% which will be subject to the exit charge (indirect method as PH has not lived in Germany for 10 years).

The capital gain is calculated on the difference between the market value at time PH held the shares when he lived in Germany and the market value at date of swap, time apportioned for the time he lived in Germany. The acquisition of the 30% in holdco has no German tax consequences if executed while PH is not resident in Germany.

VI. If PH already owns shares in GmbHsubco, can he swap these for shares in GmbHholdco?

As PH is UK tax resident at the time of the swap, he will be liable to capital gains tax on the disposal of shares in GmbHsubco at 20% or 10% as he is disposing of 60% in subco. Disposal will be at market value.

VII. If JS moves in July 2018 for a number of years, during which time he will have no German income?

JS is tax resident in Germany and will move in July 2018 to UK.

If purchase of shares after 1 July 2018 (abroad), the purchase and disposal are neutral in Germany (not taxable in Germany).

If purchase of shares before 1 July 2018 and he lived already 10 years in Germany, in general when moving abroad the situation is like a purchase, the capital gain/reserves will be taxable.

If you come back to Germany within 5 years (temporary absence), and the shares are not sold during this time, you do not need to pay taxes.

In UK, if purchase after 1 July 2018, there is no UK taxes as he is not a tax resident but if purchase after 1 July 2018, he is liable to UK capital gains tax as UK tax resident.

« *Qualifying Research and Development expenditure qualifies for a tax credit of 25%, in addition to the normal deduction for R&D expenditure* »

Ireland's Research and Tax Credit Regime

Qualifying Research and Development (R&D) expenditures qualifies for a tax credit of 25%, in addition to the normal deduction for R&D.

The credit is available for expenditures incurred in any European Economic Area country, and not just in Ireland. However, there are restrictions on the deductibility of non-Irish expenditure where a tax deduction is available in another jurisdiction.

A repayment of excess R&D tax credits is available over a 33 months period. The repayment is limited to the higher of the total corporation tax payable by the company in the previous ten years or the payroll tax liabilities of the company for the period in which the R&D expenditure is incured.

Excess R&D tax credits can be carried back to prior periods generating a cash refund of tax paid.

R&D tax credit is available on buildings which qualify for the relief. The credit can be claimed in full in the year the qualifying expenditure is incurred.

R&D tax credit claims must be made within 12 months of the end of the period in which the expenditure is incurred.

The credit may be used to reward key employees.

This Tax Credit Regime is reasonably successful in increasing business R&D.

In the period 2009-2014, there was 60% more R&D conducted due to the tax credit and an estimated 40% may have been conducted without the tax credit.

According the Exchequer, the cost was in 2009 €216 million and in 2015 €639 million.

Foreign-owned companies incur two-thirds of overall R&D expenditure.

For instance, the largest 100 enterprises in terms of R&D accounted for over €1.4 billion, or 70% of the total R&D expenditure in 2013. Of these top 100 entreprises, 80% of the spend can be attributed to foreign owned-enterprises.

Only 20% of all Irish owned business spent over €500,000 on R&D in 2013, compared to 55% of all foreign-owned businesses.

When comparing BERD expenditure across the EU, the latest data available is from 2012. Foreign-owned sector invested €1.4bn in R&D in Ireland in 2012, which equated to approximately 0.84% of Irish GDP in that year. By contrast, domestic enterprises invested the equivalent of 0.35% of GDP in 2012. Without the innovation expenditure of the foreign-owned sector, Ireland would have been one of the lowest overall performers in the EU as a share of GDP.

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The contribution of foreign direct investment in 2013 in Ireland has been €124.5 billion in exports, €174 thousands in employment and €122 thousands indirect jobs, 11,522 jobs created in R&D and Irish materials, services and economy purchases.

The advantages to Multinationals start with the resources. Indeed, they have more resources and an availability of technical expertise to support claims. They also are in house support. Bigger the investment the bigger the benefites (37.5% of costs and cost of buildings and other capital costs).

The background for **Small and Medium Enterprises** is different:

Only 1% of all small companies consider themselves to be R&D active and 16% of medium companies consider themselves to be R&D active.

Older companies (over 16 years old) are investing more in R&D, and those firms have been driving increases in R&D activity.

Innovation in younger companies (less than 3 years old) has stagnated since 2009, and even declined between 2013 and 2014.

The number of young firms claiming has declined over time, with a peak of 525 firms in 2010 and a trough of 253 firms in 2014.

The disadvantage to SME's are echo to the advantages to Multinationals, namely the lack of resources, tracking when R&D starts and ends for the documentation to support claim, the lack of uncertainty and the famous dilemma "New to the world" versus Reality.

A look at the measures

1. Outsourcing and Collaboration restrictions

Are subject to restriction, the University Sector Collaboration best practice, the sharing knowledge, the outsourcing commonly used in certain sectors and testing.

2. Two Revenue Commissioners Tests that apply

Both of the following tests must be satisfied in full.

The **Science test** is in the field of science or technology, seeks to achieve scientific or technological advancement and involves the resolution of scientific or technological uncertainty.

To be approved, companies need to prove the passing of the science test, an opinion from industry experts, need to know when the resolution of scientific or technological uncertainty commences and ends.

The **Accounting test** has to be wholly and exclusively incurred, includes salaries and wages and other costs, provides records.

To be approved, companies need to provide sufficient records, to prove allocation of costs. The Revenue bases its analysis on the lack of clarity approach.

3. The Claim Process

There are documenting processes and time costs, cost of time and resources, cost of professional advice and uncertainty.

4. Verification Process by Revenue Commissioners

For the Science test, the criteria required are:

- detailed description of activities and methods
- Evidence that uncertainty has not been addressed
- What you did, how, what you found and your conclusions

For the Accounting test, the criteria required are:

- project plan with milestones and deliverables
- Record of start date, progress and completion dates
- Record of staff working on each project and timesheet etc.
- Record of expenditure directly connected with R&D projects
- Business methodology for apportioned costs
- Records of outsourcing costs and how they relate to claim

Recommendations and conclusion

Our recommendations would be to get a higher deduction and refund for SME's (UK model), no limits for outsourcing, no restrictions on collaboration between Irish businesses and other businesses/ Universities, a sector public guidance, Revenue commissioners pre approval and service and expert checking based more on business reality.

To summarize, R&D Tax Credit is valuable to businesses, with a system in favor of multinationals.

It contributes to overdependence on foreign direct investment for tax receipts, so policy makers have to see the dangers of this for the long term economy.

Strong SME sector needs targeted revised R&D Tac Credit regime to assist innovation so it will reduce the reliance on foreign direct investment.

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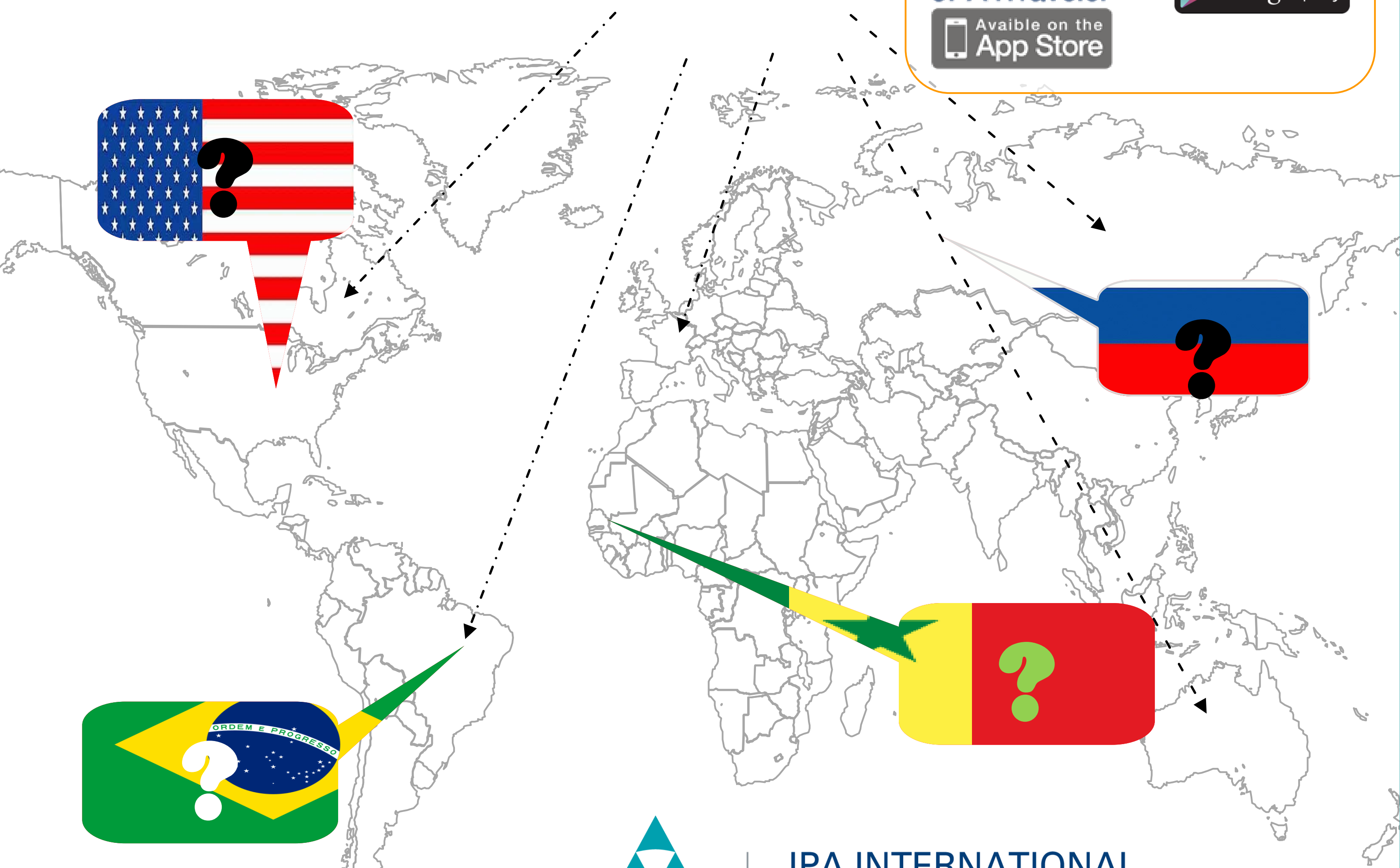

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