Submission on the Research & Development Tax Credit

June 2019

If a company spends money on research and development activities, these activities may qualify for the R&D Tax Credit, which is calculated at 25% of qualifying expenditure and is used to reduce a company's Corporation Tax. Where a company has offset current and previous years' CT liabilities, it may apply for a credit payable in instalments. A company may qualify for if is within the charge of Corporation Tax in Ireland, it carries out qualifying R&D activities in Ireland or the EEA, and the expenditure does not qualify for a tax deduction in another country. To qualify, the R&D activity must:

- *involve systemic, investigative or experimental activities*
- *seek to make advancement in the field of science or technology*
- *involve one or more of these categories of R&D: basic research, applied research, or experimental development.*
- *involve the resolution of scientific or technological uncertainty.*

Dublin Chamber welcomes this opportunity to make a submission to the Department of Finance in respect of its public consultation on the review of the Research & Development Tax Credit.[1] Dublin Chamber is the largest Chamber of Commerce in Ireland, representing businesses across the Greater Dublin Area. Our cross-sectoral membership base of 1,300 firms, spanning the spectrum from small start-ups to major multinationals, gives the Chamber a keen insight into the issues facing enterprises at various stages in the business life cycle. Dublin Chamber has a longstanding interest in public policy on entrepreneurship and enterprise support, including the R&D Tax Credit introduced in the Finance Act 2004.[2] The Chamber makes observations below with respect to questions 6-8 in the consultation document.

6 - What are the factors that are relevant to the relatively low uptake of the current credit by SMEs?
7 - Are there ways of improving the current credit system to make it more attractive to SMEs?
8 - Having regard to overall Exchequer cost, what measures could be taken to amend the current relief to improve supports for SMEs carrying out R&D?

[1] Research & Development Tax Credit Review 2019, Public Consultation Document, https://assets.gov.ie/8279/f41bc90b2f1246f0a6e21ee5c0c7e7d3.pdf
[2] Revenue Tax & Duty Manual Part 29-02-03, Research & Development (R&D) Tax Credit, https://www.revenue.ie/en/tax-professionals/tdm/income-tax-capital-gains-tax-corporation-tax/part-29/29-02-03.pdf

The present review of the R&D Tax Credit is timely, in light of the changing international tax landscape and the pressures facing Ireland's indigenous business base. As a small open economy, Ireland is highly vulnerable to fluctuations in the international market, or even to restructuring by a small number of multinational firms. Meanwhile, US tax reforms have begun to blunt the competitive edge of Ireland's FDI offering. While Ireland must maintain its attractiveness to international investors, it must also take decisive action to avoid excessive reliance upon a narrow number of highly mobile businesses.[3] This will require the strengthening of Ireland's indigenous business base, both to increase the size of the overall economy and to increase the proportion of it accounted for by Irish firms. With this in mind, Ireland must take a broader view of industrial policy that places greater emphasis on scaling indigenous firms.

Research & Development by businesses in Ireland remains dominated by larger, foreign-owned MNCs, with only 1% of small firms engaged in R&D.[4] Last year, the OECD Economic Survey has again highlighted the existence of a two-speed economy in Ireland, confirming that the productivity gap between the indigenous and multinational sectors is actually widening rather than narrowing.[5] To address the growing productivity gap between the indigenous and multinational sectors, Government must take steps to improve the low levels of innovation among Irish SMEs.

The Research & Development Tax Credit is one of the principal schemes the Government uses to encourage R&D among businesses, but it does not contain any specific provisions for SMEs. As currently designed, it is failing to drive R&D among indigenous businesses on the scale that Ireland requires. The European Commission has advised that the emphasis in Ireland's R&D strategies for business should be to build up research and innovation capability within Irish SMEs, and has recommended that the R&D tax credit scheme must be targeted at SMEs specifically.[6]

Feedback from Dublin Chamber members indicates that there is a low take-up of the R&D tax credit outside the multinational sector at present. It is particularly low among firms founded in Ireland and among firms that are SMEs by the European Commission definition. The same study indicates that use of the Research & Development tax credit is almost twice as common among large firms as among SMEs, and is almost four times more common among foreign firms as among firms founded in Ireland.[7]

Up-front Claim for SMEs

Many SMEs, and virtually all start-ups, face cash flow issues which make the 3-year deferred claim model impractical or unattractive. Allowing an upfront payment would make the R&D tax credit a more realistic option for early stage firms with lower cash resources. As

[3] National Competitiveness Council, Competitiveness Bulletin 18-2: Economic Concentration 2018, http://www.competitiveness.ie/Publications/2018/Concentration-Bulletin.pdf
[4] European Commission Research & Innovation Observatory Country Report 2017: Ireland, pp. 24-26
[5] OECD Economic Survey of Ireland 2018, https://www.oecd.org/eco/surveys/economic-survey-ireland.htm
[6] European Commission Research & Innovation Observatory Country Report 2017: Ireland, p. 26
[7] Dublin Chamber Business Risk Outlook Survey Q2 2018

this purely a cash-flow measure, it is would be cost-neutral over a three-year period, with minimal exchequer impact.

R&D Tax Credit Rate for SMEs

In the competitive context of Brexit, it is also worth noting the UK regime, where there is a special R&D Relief available to SMEs with extremely attractive conditions, including a super deduction of 130% of qualifying costs for SMEs.[8] To improve Ireland's relative position and to focus the incentive on the SME sector, Dublin Chamber recommends raising the rate of the R&D Tax Credit to 30% for SMEs as defined by the European Commission. This has been costed at €30 million per annum, which should be put in the context of overall tax expenditure on the credit.[9] The cost of the R&D tax credit was €448 million in 2017.[10]

Recommendations

- ✓ Allow an upfront claim of the R&D tax credit cash refund for SMEs, instead of the three year lagging deferred cash-flow mechanism that currently exists.
- ✓ Increase the R&D tax credit rate from 25% to 30% for SMEs, to compare better with the UK's SME R&D Relief. Cost: €30 million.

[8] HM Revenue & Customs internal manual, Corporate Intangibles Research & Development Manual, CIRD90000, https://www.gov.uk/hmrc-internal-manuals/corporate-intangibles-research-and-development-manual/cird90000

[9] Dáil Éireann Debate Thursday 5 July 2018, Question No. 87, Reference No. 29777/18. Answered by the Minister for Finance Paschal Donohoe.

[10] Revenue, Research & Development Tax Credit Statistics, May 2019, https://www.revenue.ie/en/corporate/documents/statistics/tax-expenditures/r-and-d-tax-credit-statistics.pdf