
Research & Development Tax Credit and the Knowledge Development Box

**Response from the American Chamber of Commerce
Ireland (AmCham) to the Department of Finance's
public consultation.**

May 2022

The American Chamber of Commerce Ireland

The Voice of US-Ireland Business

The American Chamber of Commerce Ireland (AmCham) is the collective voice of US companies in Ireland and the leading international business organisation supporting the Transatlantic business relationship. Our members are the Irish operations of all the major US companies in every sector present here, Irish companies with operations in the United States and organisations with close linkages to US-Ireland trade and Investment.

R&D Tax Credit

Section 766 – Research and Development Tax Credit

AmCham welcomes the opportunity to participate in the Department of Finance’s public consultation on the Research & Development Tax Credit and the Knowledge Development Box.

The R&D tax credit has been strategically important in ensuring Ireland remains an attractive, and competitive location for inward investment. AmCham highlights the importance of innovation and R&D each year through our annual Innovation Awards, which shine a light on the global impact that US companies have on driving cutting-edge research in Ireland.

US companies in Ireland, through their R&D activities, have a global impact, both through their own teams and in partnership with SMEs and research and education institutions. In 2022, AmCham presented awards recognising the impact that Irish based teams are having on critical challenges and opportunities for the global community, in the areas of sustainability, enabling technologies, and talent development.

The importance of the R&D tax credit and the Knowledge Development Box for SMEs is an important consideration for AmCham members. While most of the AmCham membership comprises of large multinationals, the AmCham membership includes smaller multinationals, with a compact but growing employee base in Ireland. AmCham members are strongly linked and engaged with SMEs in Ireland as part of their value-chain. Furthermore, the importance of SMEs is also highlighted through AmCham’s SME Masterclass programme, designed in collaboration with Enterprise Ireland and supported by the AmCham’s Board. The AmCham SME Masterclass programme aims to provide a unique opportunity for Irish SME organisations to engage with US MNCs in Ireland, and successfully work with complex international organisations.

AmCham is of the view that the R&D tax credit has been pivotal in encouraging many companies to consider Ireland as an investment location for research, development and innovation. The R&D tax credit has provided the opportunity for Ireland to showcase the additional factors which make it a great location for FDI, including the highly skilled talent pool and the ease of doing business. Without the R&D tax credit, it would be increasingly difficult to deliver this high-value investment for Ireland.

As the international tax landscape evolves, AmCham is of the view that we must support the R&D tax credit to ensure Ireland remains competitive on the global stage. In this regard, the impact of the R&D tax credit has been recognised internationally, with other jurisdictions introducing regimes in their domestic tax code which attempt to emulate the Irish R&D tax credit.

Furthermore, within Ireland, we see how beneficial the promotion of research and development has been for the national and for regional economies. Our R&D ecosystem, underpinned by the tax credit, has supported regional and sectoral clustering, which has benefitted multinationals and SMEs alike, and has also had significant benefits for our third-level institutions.

AmCham is of the view that the R&D tax credit is integral in delivering strategic investment for Ireland, and to ensure its effectiveness into the future, AmCham believes the R&D tax credit must remain adaptable and be reflective of the overall R&D environment in Ireland.

Question 1: What are the key considerations to be taken into account when deciding whether to base your R&D activity in Ireland?

The R&D tax credit is an integral part of Ireland's attractiveness for inward investment. Ireland is a high-cost economy in terms of R&D, in comparison with other jurisdictions. The R&D tax credit, in reducing the cost of R&D activities, entices potential investors to consider Ireland as an investment location, which subsequently allows Ireland to leverage its reputation, talent base, ease of doing business, and other such factors to secure FDI in R&D activities. Without the R&D tax credit to reduce the cost of undertaking R&D activities in Ireland, it would be much more difficult to deliver such FDI into the future.

AmCham members have indicated that, in terms of deciding whether to base R&D activity in Ireland, key considerations include talent, the availability of the labour market, the ease of doing business, and the competitiveness of the R&D ecosystem.

Talent is key to the future of inward investment, and for Ireland's continued competitiveness talent attraction and retention is essential, ensuring that the labour market provides the skills required by businesses undertaking R&D activities. In this context, talent in Ireland also represents a significant cost for businesses undertaking R&D activities, and the R&D tax credit is a significant support for businesses in this regard.

The R&D tax credit has been vital in ensuring Ireland remains competitive in the R&D space, particularly in terms of reducing the unit cost of R&D. Furthermore, the R&D tax credit has been a key driver of the development of the overall R&D ecosystem, spurring greater engagement with, and employment in, third-level institutions and allowing for the development of clusters. Examples of clustering across Ireland include pharmaceuticals in Cork, tech in Dublin, MedTech in Galway and advanced manufacturing in Limerick.

Question 2: When did you first claim, and what prompted you to do so? What do you value about the design of the R&D tax credit?

In relation to the utilisation of the R&D tax credit, a number of AmCham members have used the credit, on a long-standing basis, to strategically land investment into Ireland and support the expansion of their business' footprint in Ireland.

The R&D tax credit has been key in reducing the cost of R&D activities in Ireland, and in ensuring Ireland remains a competitive and attractive location for inward investment in this space.

The capital element of the R&D tax credit is a particularly valuable element of the tax credit, and one which differentiates it from similar regimes in other jurisdictions. Furthermore, the monetisation of the credit is a beneficial aspect of the R&D tax credit.

Successive governments have, over the years, continued to ensure the R&D tax credit has evolved in line with industry needs and the international environment in order to ensure Ireland's regime remains 'best-in-class'. Testament to the effectiveness of the R&D tax credit in this regard is that other jurisdictions have worked to emulate Ireland's R&D tax credit within their own territories. This is particularly relevant given current international tax changes, and the need to ensure Ireland's R&D tax credit remains 'best-in-class' when compared to the supports available in competitor jurisdictions.

Question 3: How do you think the Irish R&D tax credit can remain competitive in the evolving international tax landscape?

- **In answering this question, please have regard to EU State aid considerations and to both multi-lateral and jurisdictional changes in the international tax landscape.**
- **P2 and US tax reform**

Given the evolving international tax landscape, in order for the R&D tax credit to remain competitive, AmCham is of the view that Ireland must maintain an up-to-date regime which reflects the nature of the Irish R&D environment and evolving international tax developments. It is important that Ireland maintains its ability to respond to international tax changes in an agile manner to ensure the continued effectiveness of the R&D tax credit in supporting Ireland's inward investment offering.

Irish subsidiaries of US parents must remain cost-competitive in a changing world. The R&D tax credit is a core strategic instrument utilised by companies in Ireland to control costs. R&D is expensive, and Ireland is viewed as a high-cost location for talent. It is therefore important that there is no diminishment of the regime resulting from international tax changes.

The OECD model rules on Pillar II and the EU Commission's draft Directive "on ensuring a global minimum level of taxation for multinational groups in the Union" (GloBe Rules) were released in December 2021. This will in effect increase the cost of companies' business model in Ireland. It is helpful that provision has been made in respect of Qualified Refundable Tax Credits (QRTCs) in the computation of Pillar II.

While the provision is welcome, it is however imperative that the Irish R&D tax credit architecture will meet the conditions of a QRTC. Failure to enact the required legislation will erode the value of the R&D tax credit and Ireland's competitiveness.

AmCham recommends that the following minimum alterations are made to the Irish R&D regime:

- The Irish R&D tax credit is reconstituted to a fully refundable credit
- The credit is altered to become fully payable as a cash payment or a cash equivalent

- The full payment is issued within 4 years of the date when the entity is entitled to receive the refundable credit.

A further concern is that a QRTC will be treated as income subject to tax under the GLOBE rules. This means that the R&D tax credit would be subject to tax at the 15% global minimum rate. As a consequence, the monetary value of the R&D tax credit will be diluted. This will increase the cost of undertaking R&D in Ireland as heretofore; the credit has not been subject to tax in Ireland. This needs to be considered in the context of the inflationary economic environment as well as the impact on large capital investments, particularly high value manufacturing fields that Ireland has recently been attracting.

In summary, there are two fundamental principles that need to be actioned to help retain competitiveness:

1. Amend the Irish R&D tax credit regime to provide for a fully payable R&D tax credit that meets the definition of a QRTC.
2. Provide enhancements (i.e., rate increase/broadening the expenditure base) to the Irish R&D tax credit regime given that the R&D tax credit will become taxable under the GloBe rules.

In line with AmCham's position in its submission to the Department of Finance's public consultation on a territorial system of taxation, where it outlined that *"AmCham is aware that Pillar II, and its associated timeframe, requires the focus of Department of Finance resources, however, it is AmCham's view that there is an urgent need for a transition to a territorial system of taxation, with an effective date of 1 January 2023."* AmCham is of the view that a similar urgency is required in relation to the R&D tax credit, and it should be a priority for the Department to make resources available to advance the required changes in this regard. It would be a major show of confidence from policy makers if these changes could be brought forward in this year's Finance Bill. AmCham looks forward to receiving an update from the Department of Finance on the Territorial System of Taxation consultation, and on this consultation.

Finally, given the substantial two-way nature of the US-Ireland business relationship and Ireland's reputation as a gateway to European and other international markets, it is important that Ireland has regard to both US and other relevant international reforms. Ensuring that Irish headquartered multinationals with operations in the US and US companies with operations here are not disadvantaged by any US changes is of paramount importance. In seeking to ensure that the Irish tax system "works" for outbound and inbound companies, it is important that Ireland, within the relevant international context, seeks to avoid mismatches with the US tax regime that hinder international trade.

Question 4: In the absence of the R&D tax credit, can you say what proportion of your R&D would take place in Ireland?

AmCham understands from member feedback that, in the absence of the R&D tax credit, there would be a substantial reduction in the proportion of R&D activities taking place in Ireland, in part due to the high cost of carrying out such activities in this jurisdiction. For some members, it is the main reason for anchoring investment in Ireland.

As AmCham has outlined, the R&D tax credit is pivotal in encouraging potential investors to consider Ireland as a location in which to base, and in allowing Ireland to leverage other factors related to its attractiveness including the highly educated and internationalised talent pool, and the ease of doing business. In effect, Ireland's R&D tax credit underpins the country's attractiveness as a location for R&D activities and is key to its overall competitiveness in securing inward investment in this area.

Question 5: One of the main policy rationales of the R&D tax credit is to promote high quality jobs and investment in the Irish economy. In your experience, has your decision to conduct R&D in Ireland resulted in you recruiting additional staff, interns or apprentices?

AmCham members have reported that R&D activities in Ireland have promoted significant job growth, and also supported career development within businesses. Overall, R&D activities in Ireland, underpinned by the R&D tax credit has allowed business to expand job offerings at various levels within their companies, both in relation to new graduates, and those progressing in related fields within organisations.

R&D in Ireland has also had a knock-on impact on third-level institutions, allowing for greater industry-academia collaboration, supporting job creation in third-level institutions, while also providing more graduate entry opportunities within business.

US multinationals in Ireland support over 190,000 jobs directly, and 152,000 jobs indirectly. R&D activities benefit jobs in Ireland both directly and indirectly, and have a significant benefit for the wider economy, particularly in supporting the development of sectoral clusters, which promote innovation, in different regions across the country, and engagement and information sharing with SMEs.

Question 6: How many of your R&D staff are at PhD level or equivalent?

AmCham does not have precise data in relation to the number of R&D staff at PhD level. While all staff working in R&D may not necessarily hold a PhD, they are extremely highly skilled individuals holding many high-value positions of employment. R&D activities have also promoted increased interaction and collaboration with universities and third-level institutions, in terms of both training and research.

AmCham members have also indicated that, as a result of R&D activities being conducted in Ireland, more senior roles have been moved to, or created within Ireland. It has been

identified that, with regard to the pipeline of talent who have experience working in R&D, many of these individuals end up working in the mainstream business operations and utilising their R&D skillset to support and develop the overall business growth further.

In attracting talent to Ireland, opportunities in R&D are an important factor. The R&D tax credit is an integral part of Ireland's offering in supporting businesses to provide opportunities for talent, who then develop and grow within organisations, not just in the R&D function itself.

Question 7: Section 766B Taxes Consolidation Act 1997 places limitations on the R&D credit to be paid under section 766 and 766A TCA 1997.

- **Do you consider the limits to be appropriate?**
- **What is the impact of these limits on your R&D activities?**
- **If you claim R&D tax reliefs in other countries, are similar limitations in place? If so, how do the limitations differ and what are your views on this?**

AmCham is of the view that, the monetisation limitations on the R&D credit to be paid under section 766 and 766A of TCA 1997 have potential negative impacts for US companies making significant R&D investments into Ireland. In particular, where these investments have substantial capital expenditure elements, companies can find their expenditure exceeding the monetisation limits allowable. Furthermore, it can be difficult for a company to accurately model the impact of this which leads to undesirable uncertainty in the forecasting of potential incentives. This reduces Ireland's competitiveness in attracting large-scale R&D investments from US parent companies.

AmCham believes that the current structure of the monetisation limits is not appropriate under the GloBe rules as the excess the R&D tax credit above the limits can only currently be carried forward and used to reduce corporation tax. There is no ability to monetise the excess in future years. The rules need to be amended to either remove the monetisation limits or enable the monetisation of excess credits in a subsequent year.

AmCham is of the view that, to ensure Ireland's R&D tax credit remains competitive given the evolving international tax landscape, it would be beneficial to ensure that flexibility which allows companies to book the tax credit above the line remains in place.

Additionally, allowing for greater flexibility within the rules associated with the R&D tax credit to allow for businesses to avail of the tax credit against payroll taxes fully, within the current period, rather than having to avail of the credit over a three-year period. This increased flexibility would align with the regimes available in other territories.

Question 8: What changes might help R&D tax credit claims to be dealt with more smoothly, while ensuring better compliance?

- **How could the Department of Finance and/or Revenue improve on the quality of information and/or guidance available to companies?**
- **If you claim R&D tax reliefs in other countries, how does the claim process differ and what are your views on this?**

AmCham is of the view that what business requires in terms of the R&D tax credit is greater certainty in relation to the guidance provided. Ensuring to the greatest extent possible that minimal amendments are made to the guidance available to companies would be beneficial in this regard.

AmCham notes that expenditure in relation to the necessary resources to related to the R&D tax credit must be weighed against the benefit of receiving the credit itself. This can prove to be a barrier for some companies who may be eligible for the R&D tax credit, particularly SMEs, given the technical nature of the reports required. Simplification of the required reporting would assist companies in availing of this important support and remove this particular barrier. Clarity with regard to guidance and the simplification of the system would remove any perceived barriers.

To increase certainty around qualifying expenses, Government could amend the wording of Section 766(1)(a) TCA 1997 to ‘wholly and exclusively for the purposes of R&D activities’, rather than ‘wholly and exclusively in the carrying on by it of R&D activities.’ This change will bring the definition of “expenditure on R&D” back in line with the original policy intention and give clarity and certainty to claimants of the relief.

AmCham is of the view that it would be beneficial to ensure the adequate resources, with consistent training are in place within Revenue to assist business with the R&D tax credit, which would provide certainty and consistency for those engaging with the system.

In the context of international tax changes, Ireland’s continued competitiveness as an investment location the R&D is important. Certainty is required for businesses receiving the R&D tax credit given that this factors into the real-time budgets of companies, and therefore any lack of certainty or consistency could have a significant impact on business, and the perceived perspective through which HQs view Ireland, its governance, and its attractiveness as a location for continued and future investment.

Pre-approval of projects, from a science basis, would provide certainty for companies to predict future tax income in advance of making investments, and would work to support future inward investment, underpinned by the R&D tax credit. The option for pre-approval would be particularly beneficial for SMEs and first-time claimants.

In relation to the sub-contracting of R&D activities, and thresholds regarding the qualifying costs, AmCham notes that the 15 percent limit in Ireland is more restrictive than equivalents in competitor jurisdictions. For Ireland to remain competitive in this regard, it would be beneficial to increase the limit on outsourcing to unconnected, given that outsourcing is more attractive in some competitor countries. This would further be beneficial as it would promote greater collaboration between companies receiving the R&D tax credit and outsourced

partners, whilst also reducing the level of delays in progressing R&D activities than business can face as a result of the limit.

Regarding employment on R&D projects, AmCham is of the view that to better support businesses carrying out R&D activities, the salaries of contract and agency staff, who are working on a project for a period of 1 year or longer, should not be viewed as being outsourced specifically for the purposes of the R&D tax credit. Therefore, they should be outside of the scope of the percent limit related to outsourcing. The rationale for this being that such employees are, in practice, embedded in the business carrying out R&D activities, and under the supervision on the relevant team lead. Additionally, given the limited or uncertain timeframes often related to R&D projects, companies require flexibility in terms of the number of personnel on a given project, subsequently necessitating the need for companies to bring in contracted and agency staff on such projects. Limitations in this regard can prove contrary to the goal of developing state-of-the art innovation and can prevent companies from making the required advancements on R&D projects in the most efficient timeframes.

Finally, as mentioned by AmCham in previous consultation responses, Ireland should aim to simplify its overall, existing tax regime. The State should revise its current tax code to increase its agility and adaptability so that the system aligns with 21st century business models and helps Ireland remain a competitive and attractive location for FDI. By enhancing its tax offerings and simplify its existing tax regime, Ireland can retain a best-in-class tax policy that is innovative and competitive.

Question 9: If the rules in relation to how the credit is claimed or distributed were to be altered, for example in relation to the payment or carry-forward of excess credit, what transition provisions or other considerations would be required?

- **In responding to this question, please have regard to multi-lateral and jurisdictional changes in the international tax landscape and their potential consequences for the Irish tax system as a whole.**

AmCham is of the opinion that the payment or carry forward of excess credit need to be altered to apply to any R&D credits claimed in the relevant accounting period in which the new legislation is enacted and should apply to any R&D tax credits carried forward from prior years.

Mindful of multilateral and jurisdictional changes in the international tax landscape, AmCham understands that the R&D tax credit must be fully payable to be considered a QRTC under the Pillar II GloBe rules. As such, any R&D tax credits carried forward from prior years should become fully payable to ensure that they meet the definition of a QRTC under Pillar II.

AmCham has further outlined alterations, particularly in terms of flexibility, which would be important in this context, in response to question 7 above.

SMEs and the R&D Tax Credit

Question 10: Do you think there are ways of improving the current R&D tax credit system to make it more attractive to SMEs, taking account of EU State aid constraints that would militate against the introduction of a targeted element to the existing tax credit?

In making the R&D tax credit system more attractive to SMEs, it will be key to make it more accessible. As mentioned in the response to question 8, the level of resources which SMEs perceived that may be required to navigate the R&D tax credit system may act as a barrier given they, may feel it necessary to undertake a cost benefit analysis of the cost of such resources versus the benefit of the tax credit itself. The cost of entry to the R&D tax credit system should not, in AmCham's view, prevent businesses from availing of the support, given its importance in supporting their development and growth.

In order to encourage uptake, more simplification of the system would be beneficial, particularly relation to perceived barriers in accessing the tax credit.

Question 11: Having regard to overall Exchequer cost, what other measures could be taken to improve supports for SMEs carrying out R&D?

AmCham is of the view that measures which could improve supports for SMEs carrying out R&D would include the acceleration of monetisation periods, given that having such periods spread over three years could act as a barrier for SMEs. Furthermore, the relaxation of pre-trading restrictions would also work to better support SMEs in this field.

In addition, reducing the administration burden for companies would be beneficial in supporting businesses in availing of the R&D tax credit. The R&D tax credit is an important tool in providing benefit to the exchequer in terms of the returns from companies engaged in R&D activities, and the advancement of innovation within Ireland. As such, the R&D tax credit cannot be viewed solely as a cost to the exchequer, but should also be viewed as a benefit to the exchequer.

The Knowledge Development Box

Question 12: Do you have any views as to how Ireland's KDB could develop in the evolving international tax environment?

- **In responding to this question, please have regard to the Subject To Tax Rule (STTR) element of the Pillar Two agreement and its potential consequences for KDB claimants and the Irish tax system as a whole.**

AmCham is of the view that the complexity of the current Knowledge Development Box model can act as a barrier for business in engaging with this instrument. As such, this complexity limits the impact the Knowledge Development Box can have.

In terms of emerging companies, the Knowledge Development Box is an important part of the ecosystem, however, this instrument has limited applicability in the context of multinationals in Ireland.

With regard to international tax changes, particularly the implementation of Pillar II of the OECD international tax agreement, the Department may need to consider any reforms which may be required in relation the long-term viability of the Knowledge Development Box. In this regard, with the implementation under Pillar II of the Qualified Domestic Minimum Top-Up Tax, the possibility exists that the benefit of the Knowledge Development Box support could be eroded for businesses which fall within the scope of Pillar II. Additionally, in the context of international tax changes, consideration should be given to the irrevocability of the elect-in requirement for the Knowledge Development Box.

Question 13: What do you perceive to be the factors behind the low uptake of the KDB to date among Irish companies?

AmCham is of the view that, as outlined in question 12, that the Knowledge Development model can prove complex for many companies, and as such, this acts as a barrier with regard to uptake of the Knowledge Development Box. This is particularly the case in relation multinational companies in Ireland, whereby the requirements to qualify do not align with the multinational R&D environment. As such, the Knowledge Development Box instrument limits the range of companies who can avail of this instrument and can prove more impactful for emerging companies.

Some of the factors that AmCham has heard from our members that are contributing to the low uptake of the KDB are:

- The narrow scope of what can be considered a ‘qualifying asset’ for the purposes of the Knowledge Development Box relief.
- The nature of the OECD’s modified nexus standard which involves an onerous tracking and tracing requirement.
- Perceptions of the KDB having a limited shelf life due to the sunset clause provision contained therein. The scheme’s extension to 1st January 2023 under the Finance Bill 2020 is welcome but the expiration date is once again approaching.

To increase uptake, the Department of Finance should consider expanding the scope of what constitutes as a qualifying asset and should also adopt a more pragmatic approach when it comes to the tracking and tracing requirements.

In terms of the scope of qualified assets, those that are eligible include copyrighted computer software, inventions protected by patents, or IP for small companies which is certified by the Controller of Patents as ‘patentable’ but not ‘patented’. AmCham notes that a significant

range of discoveries do not fall into the categories of what constitutes a qualified asset, and this acts as a limitation in relation to the uptake of the Knowledge Development Box.

Question 14: Are there any particular elements of the KDB conditions that you have encountered difficulty with? Are there commercial situations which you feel should be in scope of the relief, but which fall outside the current rules?

- **In replying, businesses should be cognisant of the requirement for the KDB to be compliant with the OECD BEPS Action 5 agreement on the modified nexus approach for IP regimes.**

AmCham refers to its response to question 13.

Question 15: More generally, what do you think could be done to better support Ireland's indigenous innovation sector in pursuing productivity growth or the development of patentable advancements?

AmCham is of the view that accelerated payment processing would be beneficial in terms of all business cashflow, particularly for the smaller, indigenous sector. Furthermore, AmCham believes that businesses would be supported by the certainty and predictability which would result from the full amount of the claim being paid within a set timeframe.

AmCham, in its 2022 Budget Submission '*Next Century Ireland*', outlined the importance of supporting research, development and innovation. AmCham, in its 2022 US-Ireland Business Report further outlined the importance of research and development in fostering innovation in Ireland, and in ensuring Ireland remains an attractive location for future inward investment.