

R&D relief

2018 report

A MILESTONE TOWARDS
BUSINESS INNOVATIVENESS

Market research conducted by

KANTAR  **MillwardBrown**

ayming



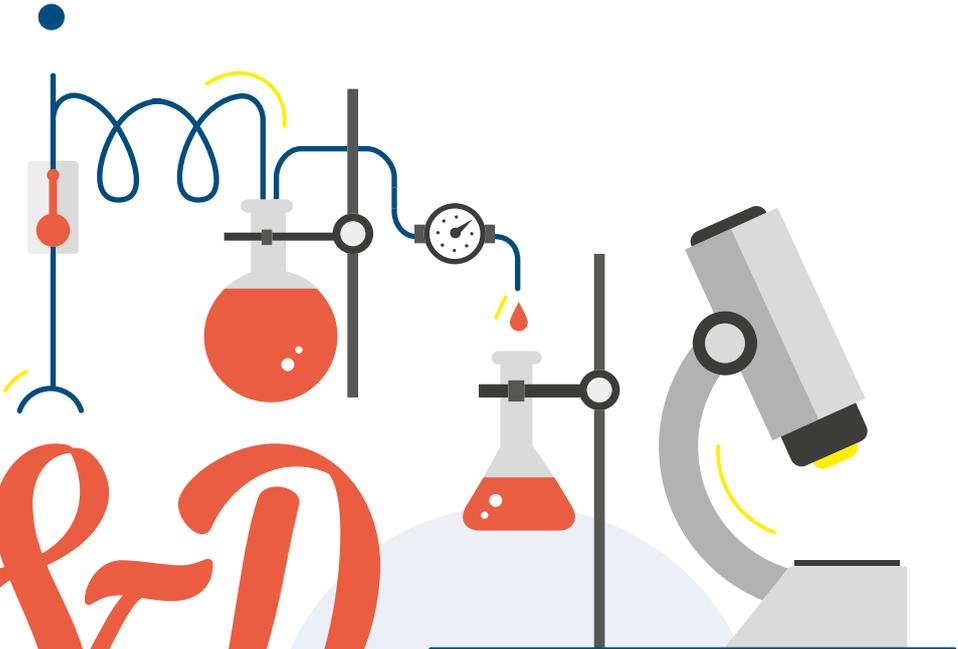
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Ayming is an international consulting group created from the merger of Alma Consulting Group and Lowendalmasaĭ, providing Business Performance Consulting services in 16 countries in Europe, Asia and North America. Ayming Polska helps businesses optimally carry out their operations, and record better financial results, offering professional strategic and operational consulting in three areas:

- **Finance & Innovation Performance**
(research and development tax relief, funding, real estate tax, VAT tax)
- **HR Performance**
(accident premiums, premiums for social insurance, the PFRON)
- **Operations Performance**
(non-strategic costs, energy products, energy audit)

Ayming Polska is the head of the Team in charge of the Innovation Reliefs of the Lewiatan Confederation's Tax Council. In 2016, 80% of the individual law interpretations regarding the R&D relief were developed at the request of Ayming Polska. The Ayming Group conducts over 15,000 projects globally regarding the acquisition of EU funds and R&D tax relief.



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Introduction



“ Attractive tax incentives and subventions help companies make the decision to increase their research and development investments ”

One of the objectives of the European Union as part of the Europa 2020 strategy is increasing the amount of spending on research and development to a level of 3% of the GDP in 2020. This target has been defined at a much lower level of 1.7% GDP for Poland. In the meantime, in 2016, the amount of internal spending on R&D in Poland has reached the level of 17.943 mln PLN and their share in the GDP equals 0.97%, which is by 0.03 pp. lower than in the past year¹. In 2016, over half of the R&D spending came from the business sector. Even though the share of this sector in R&D spending is gradually growing, it is still insufficient to achieve the target for Poland. How to encourage companies to intensify their R&D investments? Examples of innovative economies such as Ireland or the Netherlands², show that attractive tax incentives and funding make it easier for companies to make the decision to increase their R&D spend.

Ayming Polska has been involved in the process of developing the R&D tax relief in Poland since the very beginning, as we are heading the Team in charge of the Innovation Reliefs of the Lewiatan Confederation's Tax Council.

We are proud that our recommendations regarding continued development of this tax incentive have been implemented in the so called "large innovativeness bill"³ and have contributed to the attractiveness of this tax relief. The new R&D relief is more beneficial

for businesses, offers higher deduction levels and it is also easier to claim.

After over two years since the research and development relief has been functioning in Poland, we are giving you a report, in which we examine the R&D activities in businesses and we check to what extent they are claiming the R&D relief. In this publication, we share practical insight, which companies need to fully tap the potential of this tax incentive. We are hoping that the increased attractiveness of the tax relief in 2018 will motivate businesses to take advantage of it, which will result in the growth of research and development spending in the business sector.

Magdalena Burzyńska

Managing Director at Ayming Polska

1. Główny Urząd Statystyczny, Działalność badawcza i rozwojowa w Polsce w 2016, signal report, 27.11.2017, Warsaw

2. European Commission, R&D tax incentives. How to make them most effective?, Working Paper Series – September 2017, B-1049 Brussels.

3. Law from November 9th, 2017 on amendments to acts for improving the legal environment of innovative activity (Bill of laws, item 2201) which entered into life on January 1st, 2018



The research and development relief is the most accessible form of supporting research and development activity for businesses in Poland



Since the beginning of 2016, business that conduct R&D activity may benefit from the R&D tax relief that was introduced to increase R&D spending in the business sector in Poland. What is significant, the Polish legislator rewards companies for carrying out advanced activities, as well as very basic R&D work. The relief can be used not just by large organizations with their own, separate R&D departments or laboratories, but also smaller companies and start-ups willing to invest in research and development, but which cannot always acquire EU funding or other domestic funding programs.

The original shape of the R&D relief was far from perfect – the small deductible amount, the very limited catalogue of eligible costs and the above all preferential treatment of the SME sector may have contributed to the initially low interest for this solution. According to the data from the Finance Ministry, the total sum of the relief claimed by taxpayers in 2016 was over 323 mln PLN⁴. Making the relief more attractive through the so-called small innovativeness bill was intended to raise the taxpayers interest for the solution. Even though the Finance Ministry has not yet published data summing up the relief's usage in 2017, market research projects conducted for Ayming Polska by Kantar Millward Brown indicates that it is still not a very popular solution.

Since the beginning of 2018, the so-called big innovativeness bill has been in place, which significantly changed the shape of the tax relief. When settling the 2018 tax year, all companies conducting R&D activity will be eligible to writing off 100% of the eligible costs as part of the relief, whereas the entities with R&D center status were able to deduct even 150% of said costs. The third approach of businesses to claiming the R&D relief may turn out to be a breakthrough.

The research and development relief is the most accessible form of supporting research and development activity for businesses in Poland. The Finance Ministry has launched work on completing this mechanism with the so-called IP Box. It will most likely enable using a preferential 5% CIT rate on the revenue obtained by commercializing the results of R&D works. This is a significant difference compared to the basic 19% tax rate.

Businesses in Poland have more and more solutions at their disposal, which can be used for increasing their innovativeness. Therefore, are they raising their research and development spending? How are the companies using the tax relief and how are they viewing it?

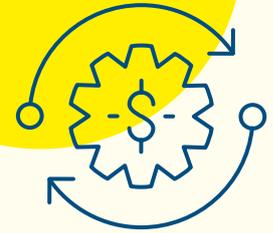
We are hoping that our publication will provide valuable insight to businesses that had already deducted their R&D relief, as well as those that are considering using this incentive. At the same time, we would like to thank all the businesses that dedicated their time to answer our questions and share their thoughts on conducting research and development activity and using the R&D relief.

Agnieszka Hrynkiewicz-Sudnik

Director, Finance & Innovation Performance

4. Data from Finance Ministry based on information on deductions of costs incurred on R&D activity (PIT-BR and CIT-BR), submitted by taxpayers, May 30th 2018

How does the R&D relief mechanism work?



The research and development tax relief is a simple fiscal instrument, that enables CIT and PIT taxpayers deduct the eligible costs of research and development activity from the tax base.

The types of costs that may be deducted have been listed in a closed catalogue. The tax preference is based on the fact that R&D costs have a dual impact on the income tax base for CIT/ PIT entities, specifically:

#1



firstly

taxpayers deduct their eligible R&D costs as regular deductible costs under regular accounting principles (100%)

#2



secondly

by deducting from the tax base the eligible R&D costs, which had already been deducted on general terms

As a result, the company may fiscally benefit from a given R&D expenses in 200% – that is first, by deducting it as a regular cost (100%) and then deducting 100% of the same cost from the already established tax base (which is usually the income of the taxpayer).

The tax relief is deducted within the year when the eligible costs were incurred. It is settled annually together with the CIT/ PIT declaration or a correction of the tax declaration. If the company incurred losses, or when the income is below the amount of the eligible write-off, the company

may deduct the tax relief from said fiscal year across a period of the subsequent 6 years.

The taxpayer with the shifted fiscal year settles the R&D tax relief deduction according to principles valid on the fiscal year for which they are deducting.

5. OECD (2017). Compendium of R&D tax incentive schemes: OECD countries and selected economies, 2017, <http://oe.cd/rdtax>, accessed 29.05.2018

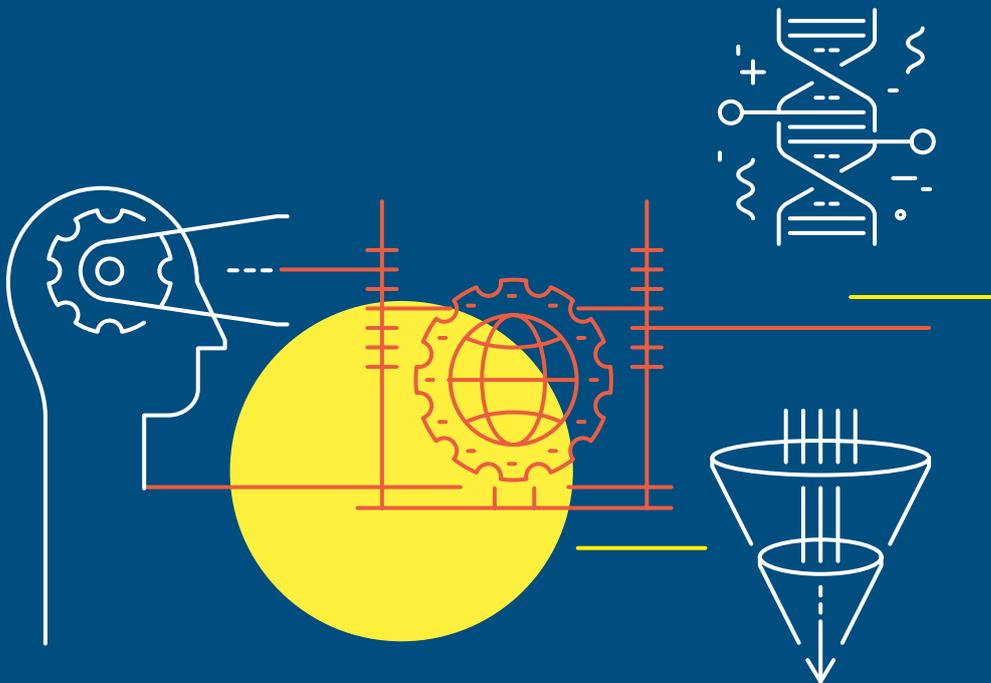
“ In order to take advantage of the R&D tax relief, the business that carried out R&D activity in a given fiscal year, must list the appropriate costs in the annual tax declaration.

What is significant is the moment when the cost is incurred, not the length of the project or the outcome of the R&D activity.

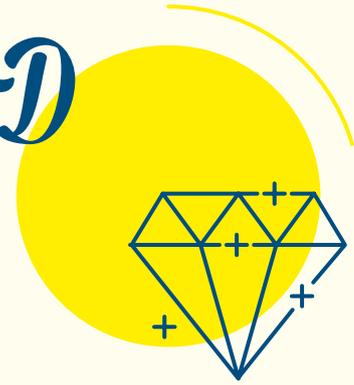
“

– Agnieszka Hrynkiewicz–Sudnik

Director, Finance & Innovation Performance, Ayming Polska.

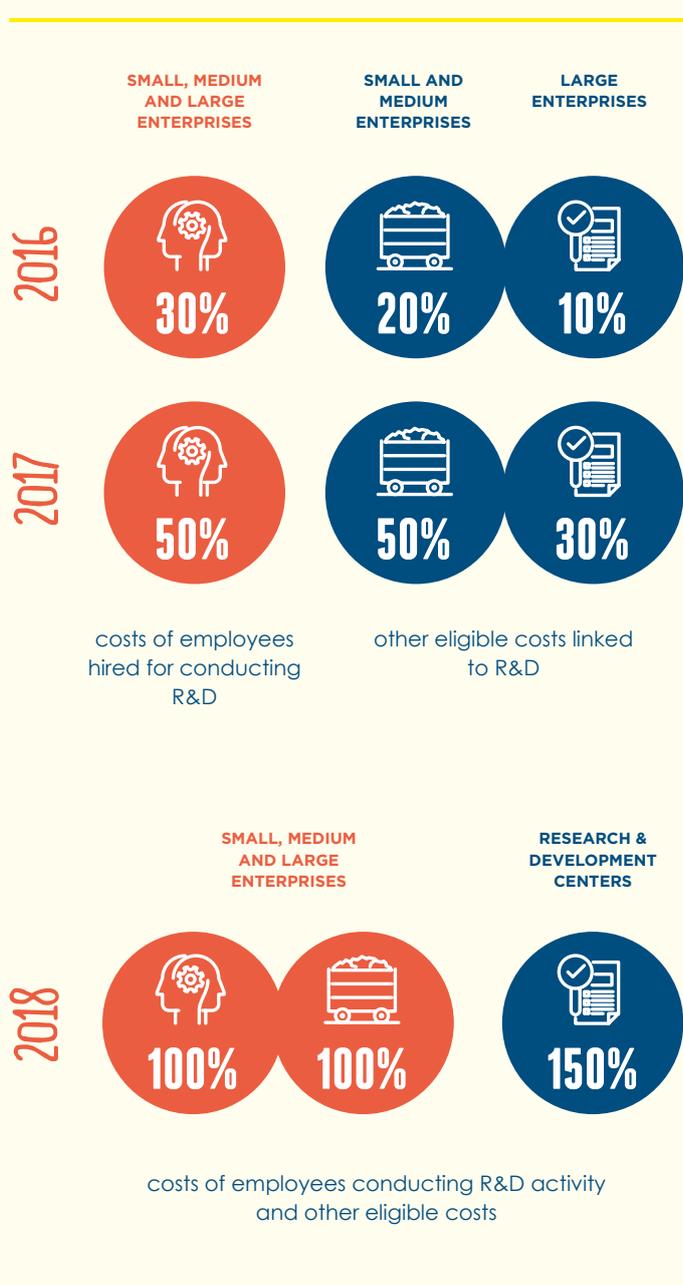


The updated R&D relief in 2018



Poland introduced the R&D tax relief in 2016. At that time, the size of the deduction was 30% of the eligible costs of employees hired for the purpose of conducting R&D activity and 20% (SME) or 10% (LE) of other eligible costs. Thanks to the modifications implemented at the end of 2016 by the so-called small innovativeness bill, companies settling the R&D relief for 2017 may deduct 50% of the eligible costs of employees hired for the purpose of conducting R&D activity and 50% (SME) or 30% (LE) of other eligible costs.

The "big" innovativeness bill introduced at the start of 2018 has increased the attractiveness of the tax relief to the level of 100% and has lifted the different sizes of the deduction depending on the category of costs and company size. Regardless of how many employees a given company hires, they may write-off 100% of all eligible costs. To give an example: a large company whose annual cost of employees hired for conducting R&D is 1 mln PLN and whose other eligible costs amount to 500 thousand PLN, with a CIT of 19%, was eligible to obtain savings of 66.5 thousand PLN in 2016. With the same R&D costs, the same company was able to save up 123.5 thousand PLN in 2017, whereas in 2018 the said company will be able to acquire savings of as much as 285 thousand PLN.





THE INCREASE IN THE VALUE OF THE DEDUCTION IN 2016-2018



Broader catalogue of eligible costs

The "big" innovativeness bill has expanded the catalogue of eligible costs that businesses may deduct from their tax base. When settling the tax relief for 2018, companies will be able to deduct the costs of specialized, non-fixed asset equipment, directly used for R&D activity. In practice, this will include above all the equipment of laboratories, laboratory utensils or measurement devices used directly in R&D.

The list of eligible costs now also includes the cost of purchasing the service of using tools to be used for analyses commissioned exclusively for purposes of R&D. Moreover, large enterprises may now deduct the costs of purchasing and maintaining patents and other intellectual property rights, previously available only for SMEs.



CATALOGUE OF R&D RELIEF ELIGIBLE COSTS IN 2016-2018

ELGIBLE COSTS	% VALUE OF THE ADDITIONAL DEDUCTION				
	2016		2017		2018
	SME	LE	SME	LE	SME AND LE
 Employment costs	30%	30%	50%	50%	100%
 Materials	20%	10%	50%	30%	100%
 Expert studies, consulting services, reviews, research purchased from scientific entity	20%	10%	50%	30%	100%
 Paid usage of research-science tools	20%	10%	50%	30%	100%
 Depreciation of fixed assets and non-tangible and legal assets	20%	10%	50%	30%	100%
 Costs of obtaining a patent, protecting a utility model or industrial design	-	-	50%	-	100%
 Specialized equipment used directly in R&D	-	-	-	-	100%
 Purchasing the service of using science-research tools/ devices	-	-	-	-	100%

Costs of cooperation based on civil contracts now eligible for the tax relief

When settling the R&D relief for 2016 and 2017, businesses were able to deduct only the costs of employees hired on employment contracts. Starting with 2018, companies may

also deduct the cost of cooperating with persons conducting R&D for said companies based on a single job, civil code contract. The business may deduct the monthly cost of the collaborator and the cost of their social insurance premiums to the level appropriate for the R&D service provided by the collaborator.

Even up to 150% deduction for R&D centers

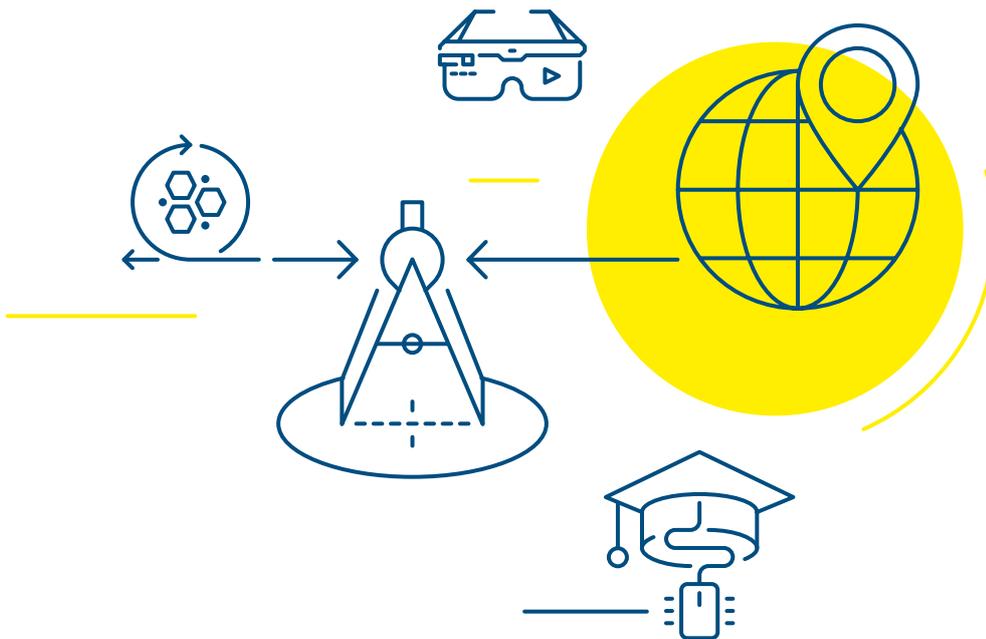
The "big" innovativeness bill has introduced preferential treatment for entities that hold the status of Research and Development Centers (R&DC). When settling their 2018 fiscal year, they will be eligible for deducting even up to 150% of their eligible costs, including: costs of personnel, materials, specialized, non-fixed asset equipment, cooperation with scientific entities and other companies, paid usage of science-research tools and equipment and the purchase of the service of using such equipment, depreciation

of buildings, structures and establishments that constitute a separate property and costs of fixed assets as well as intangible and legal assets used for R&D. What is significant, the deduction stemming from the depreciation of buildings, structures and establishments used for R&D and the costs of cooperation with entities other than scientific ones must not exceed 10% of the R&D center's revenue. A large enterprise with R&D center status may deduct 100% of the costs of protecting intellectual property, whereas SMEs as much as 150%.

R&D relief for businesses in special economic zones

Companies operating in Special Economy Zones (SEZs), due to the tax exemptions available there, were previously unable to take advantage of the R&D relief. According to article 18d., par. 6 of the CIT law: "the taxpayer is eligible for the deduction, if they did not conduct activity in a special economic zone in a given fiscal year based on the appropriate permit". In practice, this meant that the R&D relief was also not available to

the part of the company located outside the SEZ, which was indeed not using the special economic zone exemptions anyway. Thanks to the "big" innovativeness bill of 2018, companies have acquired the possibility to deduct eligible costs which are not included in the calculation of income exempted from tax based on the permit. According to Ayming experts, this among others means the possibility to deduct eligible R&D costs which are not incurred in the area of the special economic zone.



Research findings:

research and development activity in businesses and claiming the R&D relief



On the study

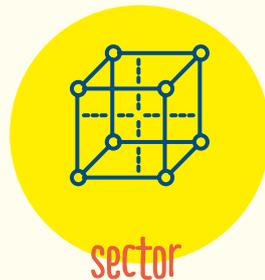
In April 2018, Ayming Polska commissioned Kantar Millward Brown and Opinia 24 to conduct quantitative research projects, with the aim of learning from entrepreneurs from chosen sectors about their research-development activities and the awareness and their plans regarding the usage of the R&D tax relief.

150 companies with over 50 employees participated in the study. The companies spanned

the following sectors: electronics, automotive, pharmaceutical, chemical, metal and non-metal processing, production of machinery and devices. In these sectors, R&D should constitute an integral part of their operations.

The interviews were conducted with the CATI method. Depending on the size of the company, questions were answered by: the CEO, the general director, the financial director, director/manager in charge of development, technical director, industrial director, chief accountant.

The data obtained was analyzed vs. total number of studied companies and in the following subgroups:



sector

electronics, automotive, pharmaceutical, chemical, metal and non-metal processing, production of machinery and devices



company size

medium companies: 50-249 employees, large companies: 250+ employees.

The findings were weighted according to the structure of businesses from given sectors in Poland with respect to the company size for the purpose of analysis.

Key research findings

Companies still display a low level of maturity regarding R&D activity



45%

companies where R&D should be an integral part of their operations, declare that they do not conduct R&D



1-3%

of the annual spending - this is how much companies most often invest in R&D



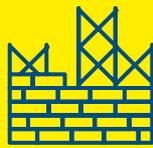
companies are not planning to significantly increase their R&D spending in 2018

Awareness of the R&D relief is still low and few businesses use it



35%

companies do not know that they may use a research & development relief



9%

companies participating in the study used the R&D relief in 2017



25%

companies declare that they will use the R&D relief when settling their 2018 fiscal year

Research-development activity in businesses

Are companies conducting research & development

A study conducted in 2016 by Kantar Millward Brown has revealed that only 40% of the companies conduct R&D activity⁶. On the other hand, in 2018, as many as 55% companies declared that they carry out R&D. Despite the visible increase, 45% business still believe that they are not conducting any R&D. The questions were answered by businesses from sectors where research and development is integral to their daily operations. Are these companies genuinely not conducting research and development, or are they unaware of what R&D really is?

The experience of Ayming Polska shows that companies in Poland have become used to seeing R&D as advanced projects, the goal of which is at least a whole country-level-scale innovation. Perhaps this perception has been caused by the high requirements of EU funding programs. According to the definition in the CIT/PIT law⁷, research and development is creative activity that encompasses scientific research or development works, undertaken systematically for increasing knowledge resources and the usage of these resources for developing new applications.

In fact, R&D activity is not only about developing technologically advanced solutions and global-scale innovations. R&D also includes changes that are implemented as part of the standard activity of the business, such as reducing the weight of a packaging or using new materials in production. It is also the integration of complex production processes in a single, automatized system, the development of software and interfacing in new technology or developing a new risk assessment model in financial services. These changes, albeit not always revolutionary, have real impact on developing and growing the innovativeness of businesses.

Understanding what R&D activity is has key importance for using the research and development relief. This tax incentive rewards businesses for advanced as well as simple R&D activities. In the meantime, Ayming Polska observations show that the identification of R&D activity is still a challenge to many companies. Companies that do not identify the simple R&D activities that they do, lose the chance for savings that could be used for advanced R&D, which can provide a major enhancement of the company's innovativeness

6. Ayming Polska, 2016 report. R&D relief. Challenges, opportunities solutions, November 2016, Warsaw

7. Law from February 15th, 1992 on income tax of legal persons (CIT), art. 4a, item 26-28. Law from 26 July 1991 on income tax on natural persons (PIT), art. 5a, items 38-40.



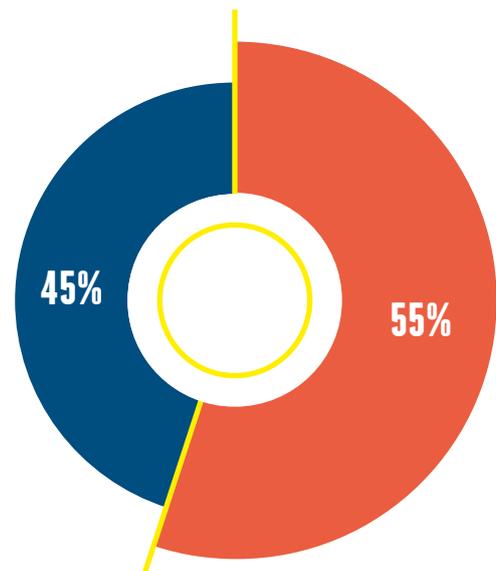
CONDUCTING R&D ACTIVITY IN BUSINESSES

Does your company conduct research and development activities

● yes

● no

Base: total sample N=15,
closed question, single choice



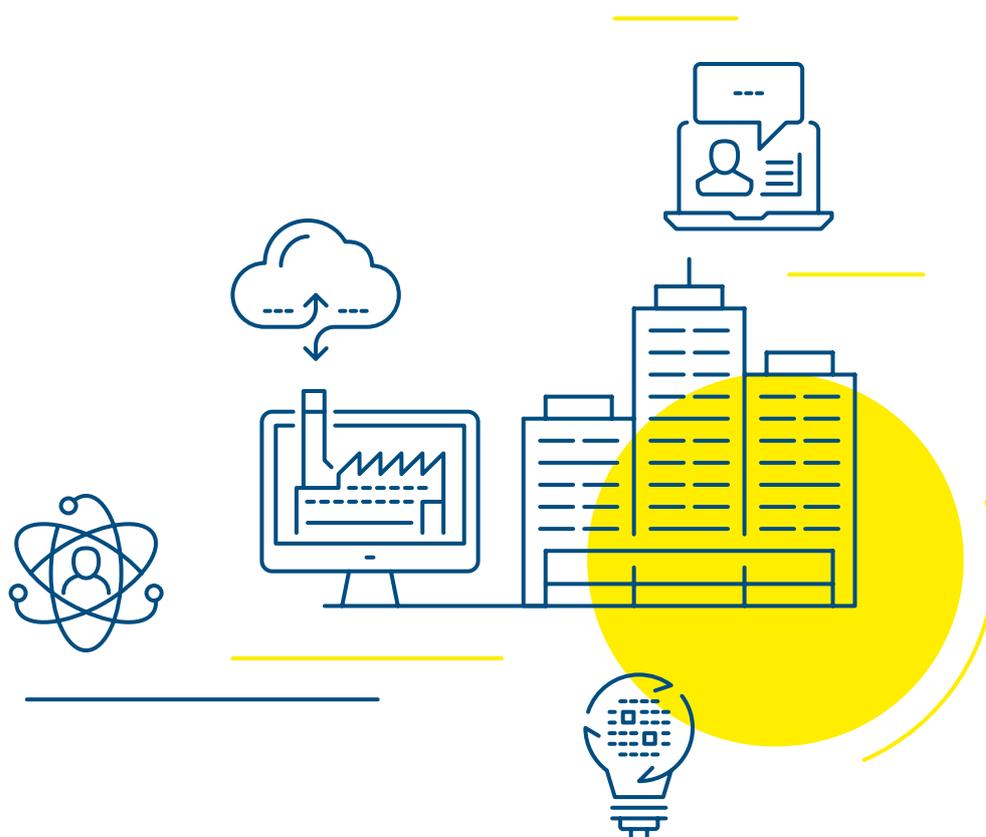
“Research and development activity may be understood very broadly.

It does not only include advanced research–development projects.

It may also be activity conducted as part of the regular operations of the business, which bears the semblance of innovativeness. This can for example be the implementation of an IT system, enhancing the recipe of a product or developing the prototype of a new machine.

– comment by M. Eng. Paweł Perzyński

Senior R&D consultant, Grants and R&D Reliefs Department, Ayming Polska.





RESEARCH AND DEVELOPMENT IN THEORY AND PRACTICE

SCIENTIFIC RESEARCH		EXAMPLES OF ACTIONS
 <p>basic research</p>	<ul style="list-style-type: none">• aiming to acquire new knowledge• only in cooperation with scientific entity	<ul style="list-style-type: none">• identifying the composition of the amino acid chain in antibody molecules• modulating tubulence in liquid-liquid emulsions, with consideration of the impact of mixing and transportation of the mass on the course of complex chemical reactions• low energy nuclera processes within the fimedependent energy density functional theory
 <p>applied research</p>	<ul style="list-style-type: none">• acquiring and applying new theoretical knowledge in practice	<ul style="list-style-type: none">• identification of antibodies for specific diseases• developing methods for building blue lasers on a Gallium Nitride foundation
 <p>industrial research</p>	<ul style="list-style-type: none">• new products, processes, services• introduction of significant enhancements to products, processes and services	<ul style="list-style-type: none">• developing new materials for meeting mechanical property requirements (i.e. stretch-resistance) with respect to design criteria or regulations• developing new design procedures and complex, automatic scripts to enhance functionality, i.e. precisely planning out the layout, defining the signal routes and verification of a circuit project on nearly 100% coverage
DEVELOPMENT WORKS		EXAMPLES OF ACTIONS
<ul style="list-style-type: none">• acquiring and applying the available knowledge from science, technology, economic activity to plan production and develep new, changed or enhanced products, processes or services• prototypes, pilot projects, demos, testing, validation		<ul style="list-style-type: none">• introducing a new type of welding machine for production• significantly enhancing a device's longevity and sustainable functioning in severe environmental conditions• introducing a new IT system influencing the production planning process

The most often seen type of R&D activity in businesses are industrial research and development-oriented works.

The R&D department in the company's structure

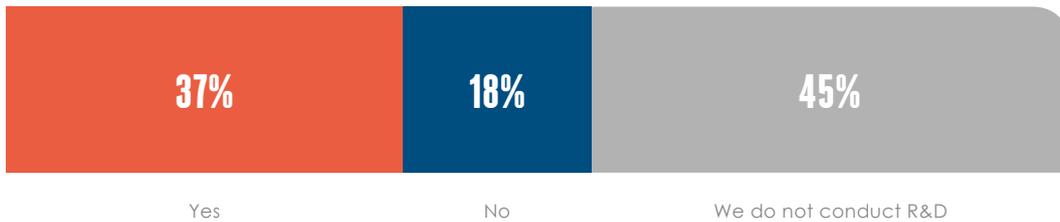
According to the study, 37% companies have their own, separate cell handling R&D activity. This is most often true in the case of pharmaceutical and chemical sector companies

(42%). Several years ago, R&D teams were only maintained in very few companies and their existence signified high innovativeness. According to the information obtained from the businesses participating in the study, the median size of the research cell is 5 people.



PRESENCE OF R&D CELL IN COMPANY STRUCTURE

Does your company's structure have a research and development cell?



Base: total sample N=150, closed question, single choice

According to Ayming's experience, the actual number of people really involved in conducting R&D activity is much higher, because R&D works are scattered across the organization. First and foremost, the R&D departments involve employees from various areas of the company in R&D projects. For example, production employees handle such key R&D activities as developing prototypes, developing pilot projects, testing and validating new or enhanced products, processes or services. Secondly, it happens very often that the company, despite not having an

R&D department, has employees conducting R&D "by-the-way" of conducting the company's basic operations.

This is worth keeping in mind in the context of benefiting from the research and development relief. At present, the Polish legislator enables taxpayers to deduct the costs of employees and collaborators that perform R&D activities in the organization, not just the employees hired for conducting R&D as stipulated in their employment contract.

When considering the R&D relief, many companies include only the costs of employees from R&D departments, laboratories or construction departments in the eligible costs. Whereas in reality, they have employees from various departments conducting R&D projects, i.e. employees working for production quality control or IT. It is typical for businesses to declare that 1-3% of their employees conduct R&D activities, whereas in reality about 15% of the employees participate in such projects.

- comment by M. Eng., Paweł Perzyński

Senior R&D consultant, Grants and R&D Reliefs Department R&D, Ayming Polska.



EMPLOYEES CONDUCTING R&D IN COMPANIES - PERCEPTION AND REALITY

SECTOR	COMPANY SIZE	HOW MANY PEOPLE IN R&D CELL	ACTUAL NUMBER OF PEOPLE CONDUCTING R&D PROJECTS
 Production of construction materials from plastics	320	4	43
 Production of household chemicals	401	5	22
 Pharmacy	635	68	114

Source: established by Ayming Polska based on own data.

“Alongside research and development cells, companies increasingly often create research and development centers. This may be due to their attractive benefits. A company with an R&D center status obtains higher property tax deductions thanks to the higher R&D relief, but also has broader possibilities for obtaining funding for increasing innovativeness. At present, there are only 36 entities operating in Poland with an R&D center status⁸”

– comment by Wojciech Popardowski

Project Manager, Grants and R&D Reliefs Department, Ayming Polska.

8. Data from: Ministry of Investment and Development, Research-Development Centers in Poland, accessed March 6th, 2018 <https://miir.bip.gov.pl/centra-badawczo-rozwojowe/wykaz-przedsiębiorców-posiadających-status-cbr.html>

Research and development spending

In recent years in Poland, there has been a decline in the government sector's share in internal spending on research and development and an increase of the share of businesses. According to the data of the GUS Central Statistical Office, in 2010, 24.4% of all spending on R&D was made by businesses, whereas in

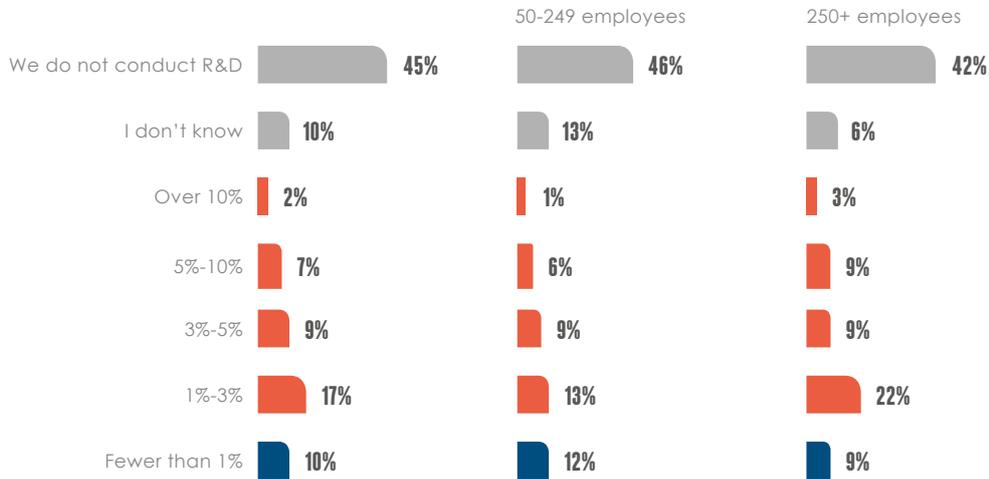
2015 the figure was 39%⁹. In 2016, the share of businesses was 53.1%, meaning that it grew by as many as 14.1 p.p. within one year.

9. Główny Urząd Statystyczny (Central Statistical Office), Działalność badawcza i rozwojowa w Polsce w 2015 (Research and development activity in Poland in 2015), signal report, 25.10.2016., Warsaw



SPENDING LEVEL FOR RESEARCH AND DEVELOPMENT IN 2017

How much did your company send on research and development in 2017?
Please estimate the percentage of the total annual spend.

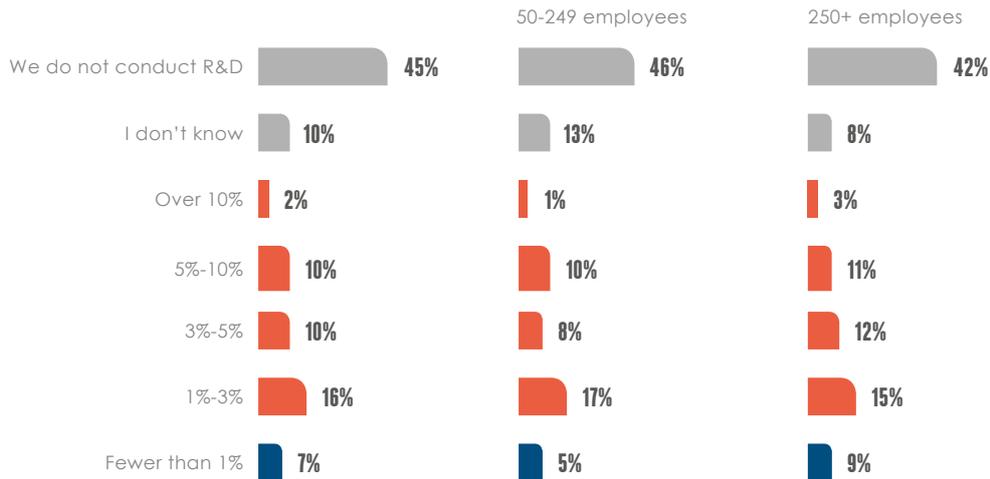


Base: total sample, N=150, closed question, single choice



PLANNED RESEARCH AND DEVELOPMENT SPEND IN 2018

How much is you company planning to spend on R&D in 2018?
Please estimate the percentage of the value of the total annual spending.



Base: total sample, N=150, closed question, single choice

In 2017, the R&D spending of the businesses participating in the study ranged from 1-3% of the total annual spend, although such a range was indicated by only 17% respondents. In this respect, large companies are not significantly different from the medium-size enterprises. Spending on the level of 5-10% of the annual expenses was declared by 7% respondents, whereas over 10% - was declared only by 2% respondents. The largest R&D spending is recorded in companies from the automotive and electronics' sectors. Despite a sizeable increase in the value of the R&D relief and the planned IP Box incentive, companies are not planning to spend more in 2018 than they did in 2017.

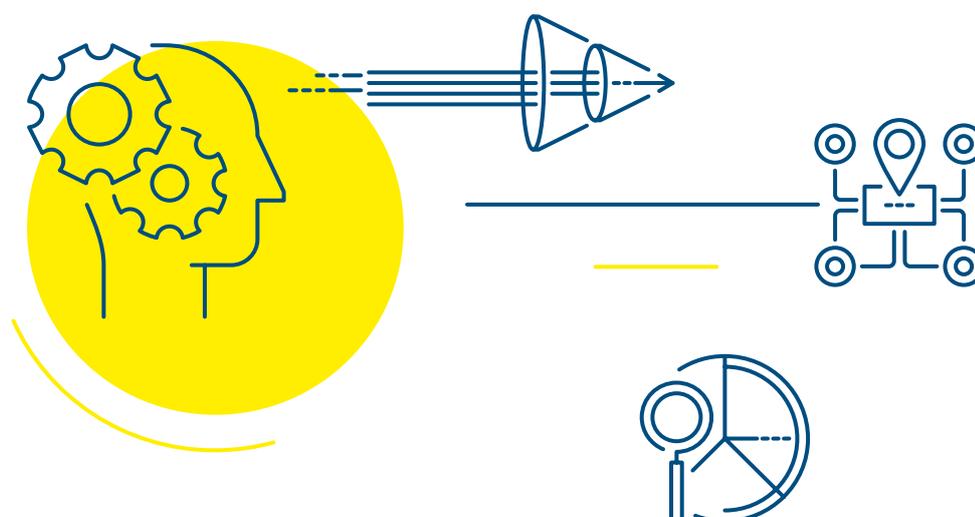
These findings are in line with the research findings provided by international institutions. Most of the private businesses are focused on providing their basic operational activity. Investments in advanced researchdevelopment activities are imbued with a risk. According to Investopedia, global companies doing R&D on average spend 1.3% percent of their revenues on it⁹, which may mean that Polish businesses are indeed slightly above the average.

However, one has to acknowledge that this value is much below the results for businesses from highly developed countries. The chemical industry scores above average, with a result ranging from 2-3%. In 2017, the largest global pharmaceutical companies spent on average 19% of their costs on R&D (Biogen – 32%., Eli Lilly – 23%, Roche and Merck – 21%., Pfizer and Astra-Zeneca – 14%, GlaxoSmithKline – 13% and Abbott Laboratories – 8%).¹⁰.

9. <https://www.investopedia.com/ask/answers/060115/how-much-drug-companys-spending-allocated-research-and-development-average.asp> dostępn 29.05.2018 r.
10. Data commonly accessible in financial reports.

Categories of R&D spending

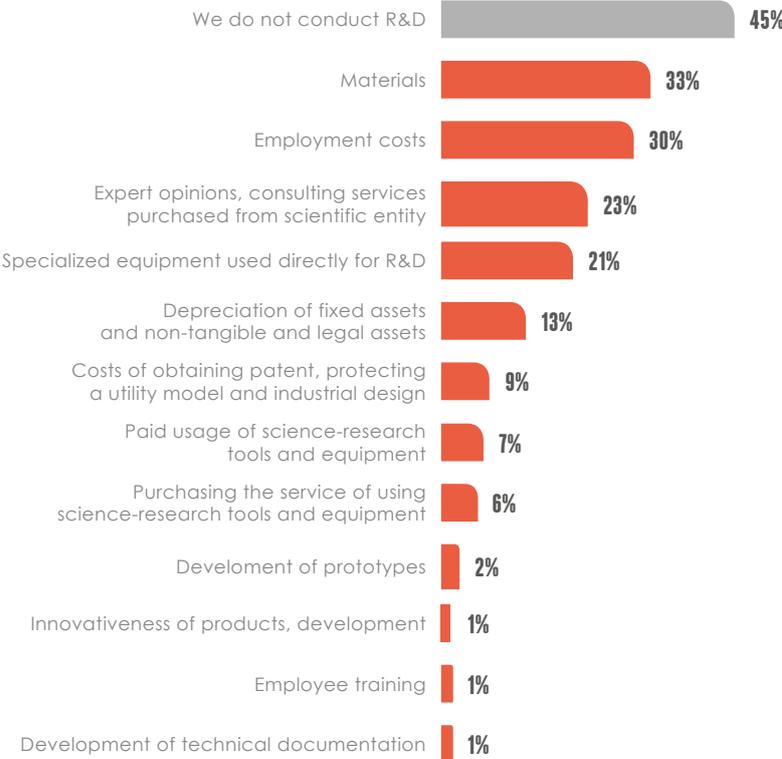
The main spending on R&D incurred by companies are costs of materials (33%) and employment costs (30%). For nearly one in four companies, buying expert opinions and consulting services from scientific institutions is also a significant expense.





CATEGORIES OF R&D SPENDING IN COMPANIES

What categories of R&D spending are present in your company?



Base: total sample, N=150, closed question, multiple choice

In 2018, a wide range of eligible costs can be deducted as part of the R&D relief, these are listed in a closed catalogue. For comparison, in the Czech Republic, which is our direct competitor for foreign investments, the tax incentive system was already enacted in 2005. The model that functions there is similar to the Polish one: a company may deduct from tax 100% of eligible costs incurred for R&D, moreover they can also use that sum to lower their tax base. The total tax benefit is 200% of the expenses incurred. There are no significant differences between the Polish and Czech catalogue of eligible costs, although the latter also includes operational expenses, such as the cost of buying books or magazines or energy costs. Another interesting solution is also

including eligible costs incurred by foreign branches of resident companies registered in Czech Republic as R&D activity costs. This is an effective mechanism that supports the development of Czech businesses in foreign markets.

According to the experience of Ayming Polska, a significant expense to many businesses is the purchase of expert opinions and consulting services. At present, these costs may be deducted via the R&D relief only when they had been purchased from a scientific entity. In the meantime, companies turn to professionals with the required experience for these services. Such cooperation between businesses should also be covered by the R&D relief.

Factors contributing to growing R&D spending

What factors motivate companies to increase their R&D spending? Respondents most often mention easier access to research development funding (51%). Respondents had a similar opinion in 2016, considering this factor the most

important (61%). In 2016, 56% of the companies indicated the necessity to increase the company's competitiveness in the market - now, this is a significant factor to only 21% companies. Interestingly, in 2016 as many as 52% companies mentioned the enlarged scope of the R&D relief, whereas at the moment this was mentioned by only 26% respondents.



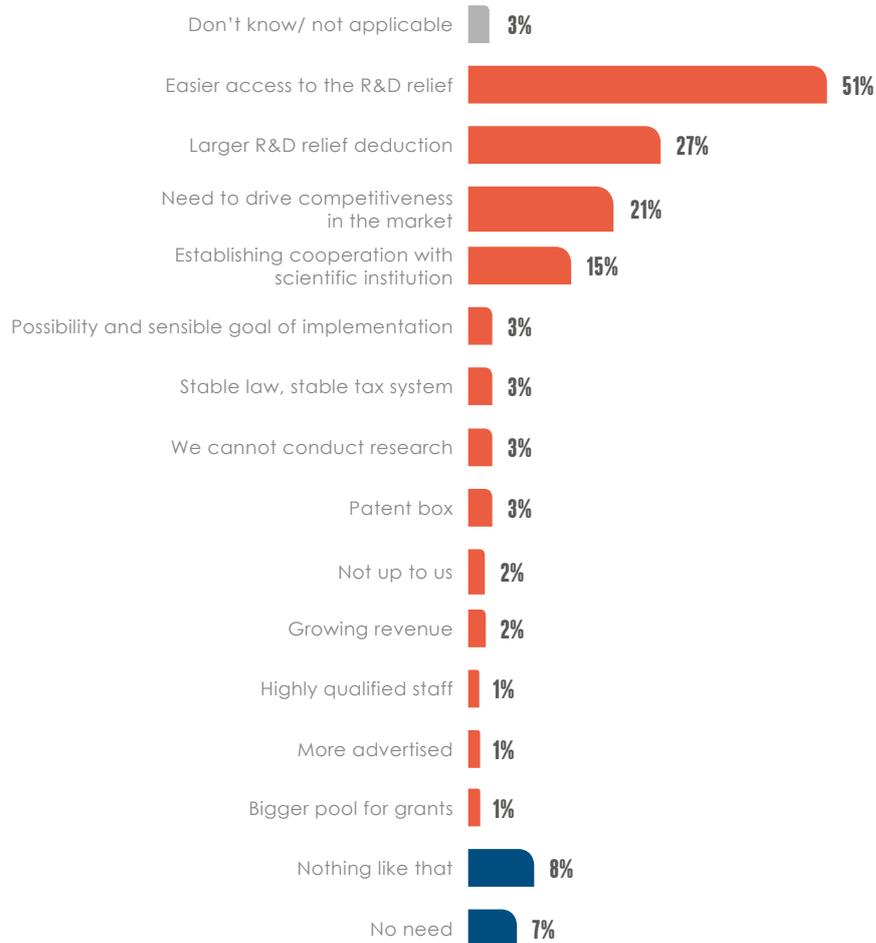
COMPARISON OF RESEARCH RESULTS

	2016	2018
 Easier access to the R&D relief	61%	51%
 Need to drive competitiveness in the market	56%	21%
 Larger R&D relief deduction	52%	27%



FACTORS CONTRIBUTING TO INCREASING RESEARCH AND DEVELOPMENT SPENDING

What could encourage your company to increase its research and development spending?



Base: total sample N=150, closed question, multiple choice

Ayming Polska experts observe that R&D activity is still above all associated with subventions and cooperation with academic/ scientific institutions. EU funding is granted to the developing companies that need support to accelerate their growth. Companies applying for funding need to provide that they can finance the part of the

project that is not covered by EU funding. In the meantime, the R&D relief is accessible to every company that conducts simple R&D activity as well as advanced innovation projects. What are the principal differences between these solutions? Let us see.



EU FUNDS AND R&D RELIEF. BENEFITS AND LIMITATIONS

EU FUNDING	R&D RELIEF
<p>Benefits</p> <ul style="list-style-type: none"> • Funding growth or modernization of the company and increasing its competitiveness • Access to external capital • Non-returnable aid • Supporting a high risk actions stimulating faster growth 	<ul style="list-style-type: none"> • Savings that can be used for continued R&D activities • R&D defined broadly - company-scale innovation is sufficient • The outcome of projects in the company is irrelevant • No need to participate in contest-related programs • Small requirement for formalities
<p>Limitations</p> <ul style="list-style-type: none"> • Strict definitions of R&D works and innovations • Conducting works in accordance with the funding application • Amount of support dependent on the size of the company and project location • Additional administrative-accounting requirements 	<ul style="list-style-type: none"> • Need to map R&D processes • Separating R&D spending in the accounting records • Tax laws have unprecise definitions • Difficult access to knowledge and trainings on the R&D relief

At this point one has to emphasize the complementary character of both of these forms of support. The legislator has excluded from the list of eligible costs anything that had been refunded to the taxpayer in the form of any grant. Nevertheless, the exclusion does not apply to the so-called own contribution, which is eligible to being covered by the R&D relief. Businesses may presently choose both forms of support, which definitely needs to be seen as positive.

– Przemysław Gabrysiak

Project Manager, Grants and R&D Reliefs Department Ayming Polska.

R&D relief and EU funding as complementary benefits



MINING

Sector



2_k

Employees



ŚLĄSKIE

Where



2_{MLN PLN}

Annual R&D spend
(as part of regular
operations)



R&D CENTER

Planned
construction

Deduction for 2018

EU FUNDING		R&D RELIEF	
Investment value	Size of grant	Costs eligible for R&D relief	Amount saved by R&D relief
Regular R&D activity			
not applicable	not applicable	2 mln PLN	300 k PLN
PO IR 2.1. Investments in R&D infrastructure of business: building an R&D center (main cost is purchasing equipment necessary for R&D works including machines and devices for providing R&D)			
3 mln PLN	750 k PLN (25%)	1,5 mln PLN	285 k PLN
PO IR 1.1.1 Industrial research and development works conducted by businesses: so-called „faster path” (main cost is employee wages, subcontracting)			
5 mln PLN	2,5 mln PLN (50%)	1,25 mln PLN	237,5 k PLN
SAVINGS	3,25 MLN PLN	KORZYŚCI	0,90 MLN PLN

40%
savings

Company's spending on R&D – 10 mln PLN, savings obtained thanks to available support forms – 4.15 mln PLN (3.25 mln PLN from EU funding + 0.90 mln PLN from relief), which is over 40% of the investment.

Usage of the R&D relief by companies

Are companies aware of the R&D relief?

The awareness of the R&D relief equals 65%. This means that one in three companies is still unaware of the R&D relief. The awareness level has grown compared to the end of the 2016, when only 16% declared good and very good awareness of the R&D relief mechanism, whereas 40% had never heard of it¹¹. The lowest awareness of the R&D relief is visible in the electronics' and automotive sectors (60%), which surprisingly declare the highest spending on such activity.

Both studies included companies from sectors that conduct R&D as part of their regular operations. The findings indicate that actions promoting the R&D relief are required to raise the awareness of businesses about the available forms of supporting innovativeness. One must add that the R&D relief and the IP Box are solutions that have been enjoying popularity for many years in the countries that chose to implement them. Both of these instruments should contribute to boosting the competitiveness of Poland when it comes to acquiring new investments and sustaining and growing business in the Polish market.

11. Ayming Polska, 2016 report. R&D relief. Challenges, opportunities, solutions, November 2016, Warsaw

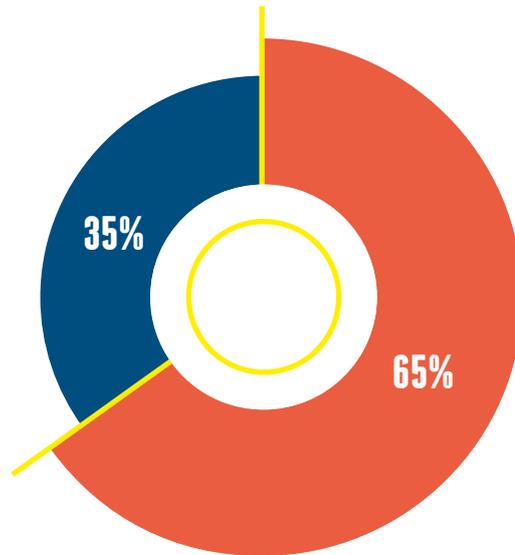


AWARENESS OF THE R&D RELIEF

Starting January the 1st, 2016, businesses investing in innovations can use a CIT tax relief. Every company can deduct the costs separated in their accounting records incurred for R&D activity.

Are you aware that your business can use such a tax incentive for research-development activity?

- yes
- no

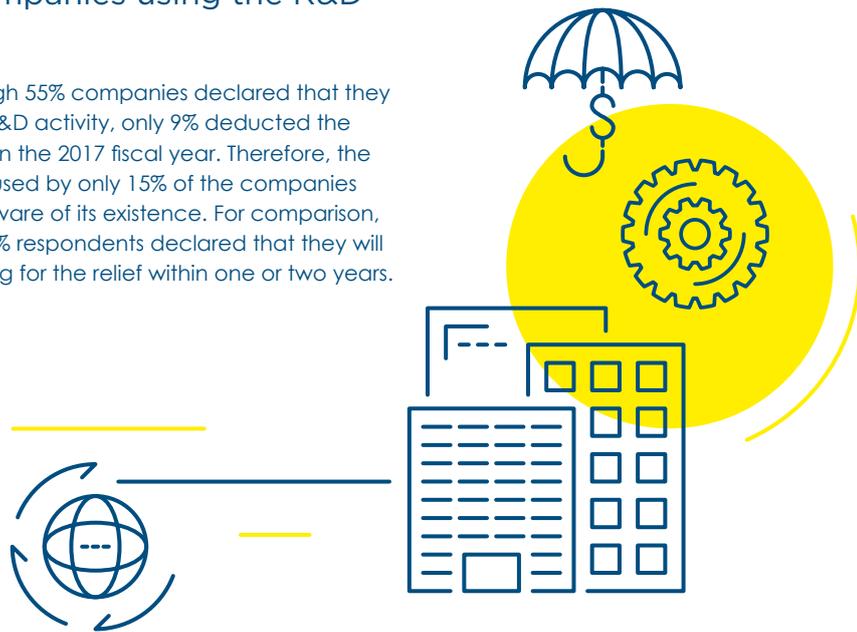


Base: whole sample, N=150, closed question, single choice



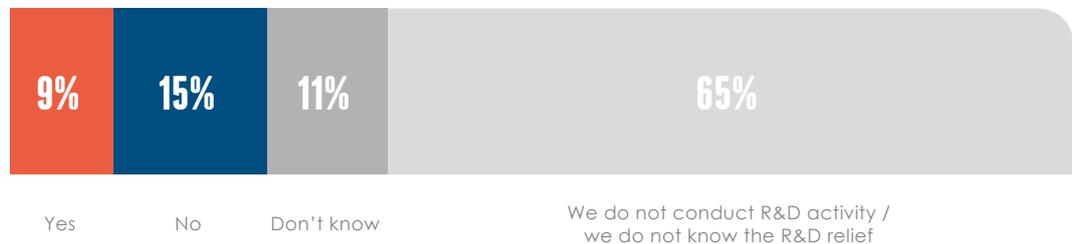
Are companies using the R&D relief?

Even though 55% companies declared that they conduct R&D activity, only 9% deducted the R&D relief in the 2017 fiscal year. Therefore, the relief was used by only 15% of the companies that are aware of its existence. For comparison, in 2016, 19% respondents declared that they will be applying for the relief within one or two years.



USAGE OF THE R&D RELIEF

Has your company claimed the R&D relief for 2017?



Base: whole sample N=150, closed question, single choice

According to the data from the Finance Ministry, 323 mln PLN was deducted via the research and development relief in 2016. According to the government's forecasts, the sum of the deductions for 2016 was intended to reach 1668 mln PLN, whereas in the end it constituted only 19% of this sum. For comparison, in the Czech Republic, which implemented the R&D relief in 2005, taxpayers deducted 516 mln PLN¹² in the first year, providing savings of 141 mln PLN. A year later 680 mln PLN was written off (163 mln PLN savings), whereas in 2016 the deducted sum was 2,071 mln PLN, with 392 mln savings¹³. The example of the Czech Republic shows that taxpayers

need time to familiarize themselves with the new tax incentive. What needs to be stressed is that in Czech Republic, the deduction size was 100% already since 2005, whereas in Poland it was on a much lower level at first. Raising awareness of the companies about the R&D relief and higher value of the deduction should translate into better usage of the R&D relief in the coming years.

12. Currency exchange rate according to the NBP 04.06.2018 r.

13. Český statistický úřad, Nepřímá veřejná podpora výzkumu a vývoje, <https://www.czso.cz/csu/czso/nepriama-verejna-podpora-vyzkumu-a-vyvoje> dostup w dniu 04.06.2018 r.

Evaluation of the R&D relief

The value of the deduction has been increased twofold in Poland since 2016, whereas the catalogue of eligible costs has been expanded. Still, the level of usage of the tax relief is still very low. Very few companies have used it, whereas all that did have a positive opinion on it.

The main reason for being satisfied that respondents mentioned was the possibility to acquire savings that could be used on continued growth and investments in R&D. This is positive information for the legislator, whose intention was to introduce a mechanism for intensifying R&D activities of companies.



EVALUATION OF THE R&D RELIEF - QUOTES

Why are you positive about the R&D relief? Please provide the key reasons.

- This always leaves some money in the company for continued growth
- The tax relief can be used as a deduction
- Reduces the financial burden on companies that wish to grow and increase their R&D spend
- Savings for the company. We can motivate our new hires better
- It is a kind of help and a state incentive for companies



The R&D relief? We're positive about it

The R&D relief helped us save money, which is why we are positive about it. The deduction process was not complicated and did not require excessive work from us. The amount that we deducted wasn't perhaps very large, but it was surely felt. The savings obtained will be used for investments, i.e. in hiring more R&D staff. What is important is that we have blazed the trails, so the next year's deduction will be even simpler. Moreover, the 2018 deduction will be higher. Promar is a tech company where R&D is seen as a priority and an investment. What could motivate us more to increase our spending on research and development is the possibility to deduct all the actual R&D costs and less bureaucracy when settling the relief. Last year, we were not able to deduct all the costs due to problems acquiring the proper accounting documentation.

– comment by Robert Śmiałek

Director of the Development Department, Promar Przedsiębiorstwo Produkcyjno-Handlowe Sp. z o.o.





The money from the tax relief enables us to finance more R&D

Our organizational culture is based on an innovative approach to work, projects and processes. In such a large organization as Budimex, we are simultaneously conducting many R&D tasks, whereas the R&D relief is a factor that may contribute to launching more, innovative projects.

However, to effectively deduct the costs, you need to educate the teams participating in research–development activities and you need to properly attribute the tasks with regards to the settling process itself – the process is labor–intensive, but pays off.

Budimex is turning 50 this year. We are a market leader and that sets the bar high. We don't need to be motivated to support innovativeness in the industry or to conduct R&D. What is also important is that it is possible to lower the costs of the R&D projects carried out and that the money saved from the tax relief may be used to finance future, innovative actions.

– comment by Przemysław Kuśmierczyk

Head of Innovation Team, Budimex S.A.



As the research shows, companies rarely use the R&D relief. But when they do, their biggest challenge is the record-keeping of the costs. The respondents' answers confirm the experiences of Ayming Polska from cooperating with companies of various sizes and from various sectors. The lack of clear guidelines and situations when tax authorities avoid answering how to keep records of the costs should encourage the legislator to provide more precise regulations or to publish applicable guidelines.

The research and development relief is a new mechanism, something that businesses and tax authorities are still learning to use. The first approach of the taxpayers to settling the tax relief for 2016 showed how challenging it is for the companies and authorities to estimate the basis on which the employees' worktime spent on R&D can be submitted to the R&D relief. Some tax offices are refusing to provide a tax interpretation or require a formal inclusion of R&D activities within the list of responsibilities of a

given employee. By assumption, the R&D relief was intended to motivate companies to increase their R&D spending, which is why the Finance Ministry sided with the taxpayers and published guidelines that were beneficial for the businesses with respect to qualifying personnel costs to the tax relief.

Another obstacle for the companies that settled their R&D relief was identifying R&D activity. The proper identification of R&D activity is a key element of settling the tax relief, which is why it is required to dedicate sufficient time to it and to involve employees doing R&D (i.e. the development department) to map the R&D processes in the organization. Moreover, businesses have access to a range of individual tax interpretations, that may be used as their point of reference for identifying R&D. If there are doubts, a company may submit a request for an individual interpretation to obtain clear guidelines regarding the course of action.

What is stopping businesses from using the R&D relief

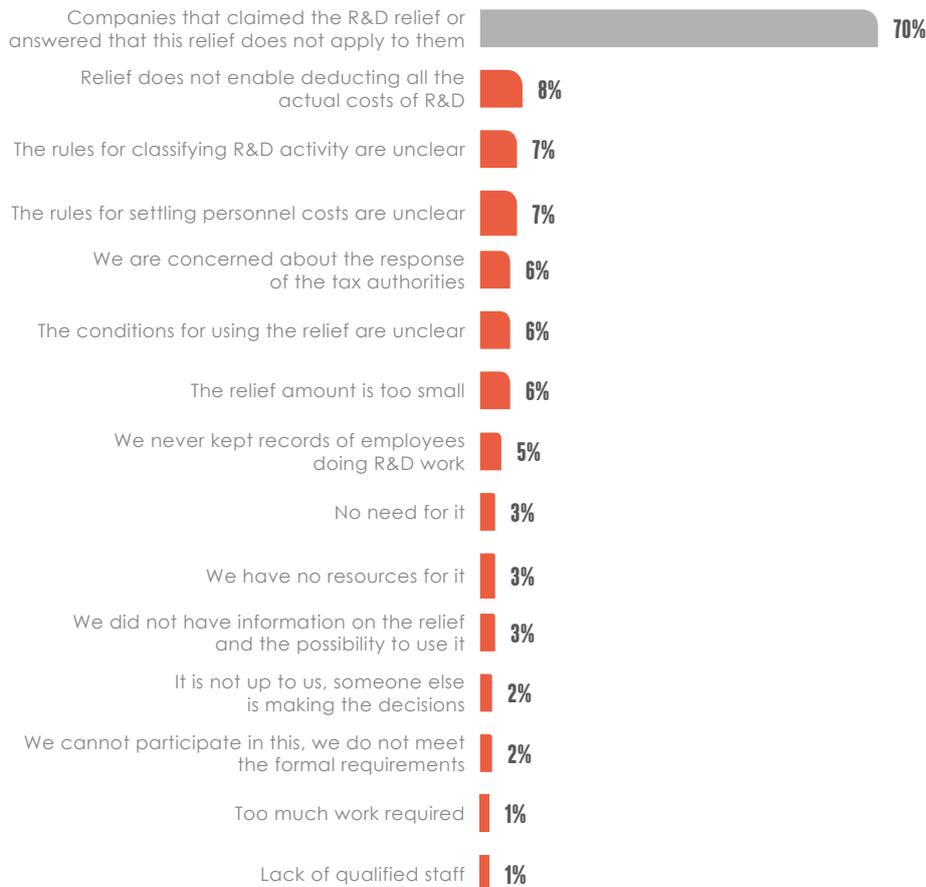
What are the reasons why companies have not used the R&D relief? Three key reasons indicated

by the respondents were: inability to deduct all the actual R&D costs, unclear rules for classifying R&D activity and unclear rules regarding the deduction of personnel costs.



BARRIERS TO USING THE R&D RELIEF

What are the reasons that stopped your company from using the R&D relief?



Base: total sample N=150, closed question, multiple choice

For contrast, at the end of 2016, the potential limitations and concerns related to using the R&D relief for businesses were: unclear rules for classifying R&D activity, inability to deduct all the actual costs of R&D, no information on the tax relief and inability to use it, but also too small value of the tax relief relative to the risk of investing into R&D.

In the meantime, the legislator has doubled the size of the deduction, expanded on the scope of eligible costs and made the rules regarding personnel cost deductions more precise. However, the development of the R&D relief should also be accompanied by the growth of awareness in businesses about this form of support that is available. Two years after the relief's implementation, 35% companies are still unaware of its existence. What is needed at the moment is educating businesses on the possibility to use this tax incentive.

Are businesses planning to claim the R&D relief for 2018?

Even though the R&D relief was claimed in 2017 by only 9% of the companies participating in the study, 25% respondents declare that they intend to use the tax relief in the next year. The growth of the interest for the tax relief is most likely due to the growing awareness of companies about

available forms of aid and beneficial changes to the mechanism itself put in place by the so-called "big" innovativeness bill.

All the companies that claimed the R&D relief in 2017 are planning to use it next year, which confirms that they assess the tax relief positively.



PLANNED CLAIMING OF RELIEF FOR 2018

Is your company planning to claim the R&D relief for 2018?



Base: whole sample N=150, closed question, single choice

According to the companies participating in the study, the main factor that could drive them to more frequently use the tax relief is the harmonization of legal regulations. According to the experience of Ayming Polska, the issue is not the provisions of the specific laws, but their interpretations issued by the Director of the State Treasury Information Center. Unfortunately, despite the harmonization of the number of institutions

that issue interpretations, these interpretations are indeed still contradictory and the rulings change over time. It needs to be noted that in Western Europe countries, such as in France, tax authorities are perceived much more positively. What may provide a positive change in how the authorities are viewed in Poland is the recently announced constitution for business.



R&D RELIEF - EXPECTED CHANGES

What do you think would have to change in the tax relief for your company to start using it?

- Clear and stable legal regulations, simple and clear criteria
- Harmonization of the law, easier to deduct, fewer inspections and fines
- We'd like to have a guarantee that the tax system is stable
- More information on the possibilities for using the tax relief
- Easier access to and more clearly specified criteria for granting the relief
- We do not know what the tax relief is about, if we had known, we would have used it
- Larger sums for deductions
- Everything should be much easier to process
- Easier and more single-minded way for qualifying the deductions

66

The higher deductible amount is a step in the right direction

The R&D relief is a solution that may bring real savings to businesses. Increasing the value of the deduction which had been done recently is a step in the right direction. This tax relief enables saving money, but there is still too much red tape if we look at the executive regulations. This creates doubts regarding the qualification of R&D project costs. In consequence, the company does not write off all the costs that it should. The relief does not yet allow deducting all the costs necessary for effective project execution. This applies among others to the cost of purchasing services from an entity that is not academic in nature. The purpose of buying such a service should be of primary concern, not the actual entity that it is purchased from. The deductible amount is definitely the biggest incentive to using the tax relief, but changing the rules regarding the qualification of costs would surely be positive as well. Replacing the rule of “what is allowed” with the rule of “what purpose was this done for” would motivate companies to conduct R&D and using the tax relief would make such projects more cost-efficient.

– Krzysztof Lonca

Economic director, Gedeon Richter Polska Sp. z o.o.

66



R&D relief in practice



Basis for obtaining the relief

Laws and documents regulating the R&D relief



CIT AND PIT TAX LAWS



OTHER LAWS*



INDIVIDUAL INTERPRETATIONS



PUBLICATIONS OF THE OECD, PARP, NCBR

The legal acts regulating the tax relief for research-development activity are laws about income taxes – CIT and PIT – and transitional regulations from laws changing the above, such as:

- ✓ The law from September 25th 2015, about amendments to some laws in relation to supporting innovativeness,
- ✓ The law from November 4th, 2017 about amendments to some laws specifying the conditions for carrying out innovative activity.

*Analysis of the research-development activity of companies in the context of the possibility to claim the R&D relief is also based on many additional legal regulations, which include:

- ✓ Law from October 1998 on the social insurance system,
- ✓ Law from April 30th 2010, on the rules for funding science,
- ✓ Law from July 2nd 2004 on economic freedom,
- ✓ Law from September 29th 1994, on accounting,
- ✓ Law from November 9th, 2017, on amending some laws to improve the legal environment for innovative activities.

“

When considering various matters related to the R&D relief, it is advisable to consult the guidelines of the state administration published on the websites of the respective institutions, especially the Finance Ministry.

– Wojciech Popardowski

Project Manager, Grants and R&D Reliefs Department, Ayming Polska.

”

When identifying the R&D activity of businesses, one has to keep in mind that the basis for them are legal acts with legal power. Another element that explains such acts are general and individual interpretations. The documents below can also be used for additional supplementation. However, one has to keep in mind that they do not have legal power.

-  Frascati Manual 2015, The Measurement of Scientific, Technological and Innovation Activities. Guidelines for collecting and reporting data on research and experimental development,
-  The Oslo handbook. Rules for accumulating and interpreting data on innovations. Measurement of scientific and technical activity,
-  Processes for managing R&D projects. Report from a study conducted for the National Center for Research and Development,
-  R&D commercialization projects. Prepare-Evaluate-Implement,
-  Accounting policy as part of R&D commercialization,
-  Innovativeness of Polish companies. R&D activity and cooperation between science and business,
-  Research-development-innovations. Chosen problems.

According to the experience of Ayming Polska, companies often have an issue identifying which of the jobs they do constitute research and development.

This is one of the most frequent reasons why they apply for individual interpretations issued by the Director of the National Treasury Information Center.

By analyzing the interpretations published on the websites of the Finance Ministry in 2016-2017, Ayiming Polska experts chose examples of R&D

actions that were present in the sectors that participated in the study.



EXAMPLES OF R&D ACTIVITY FROM INDIVIDUAL INTERPRETATIONS FROM 2016-2017



MACHINE AND DEVICE PRODUCTION

Designing a transporter for powder goods and implementing the device for usage.



METAL AND NONMETAL PROCESSING

Designing and producing elements, tools, including special tools and elements necessary for building a prototype or pilot service in the process of building steel structures.



AUTOMOTIVE

Interior finishing – designing among others center consoles, dashboards with consideration of their ergonomics.



ELECTRONICS

Developing innovative products in the form of digital TV sets enabling distributing the television signal inside the home. Preparing prototypes of devices, including their verification and validation, possible improvements to idea plans and preparation for mass production.



PHARMACY

Producing more modern, advanced drugs and other healthcare products with increased efficacy, meeting the requirements of pharma safety regulations with respect to the most severe diseases of civilization (among others: autoimmune diseases, neurological, oncologic), steroid ointments and ointments for short-lasting, topical treatment of skin conditions.



CHEMICAL

Developing construction chemistry products based on existing recipes, but also developing recipes for new products, then checking their parameters, finding possible improvements and conducting all the procedures necessary to market the product.

It needs to be kept in mind that an individual interpretation protects only a particular applicant.

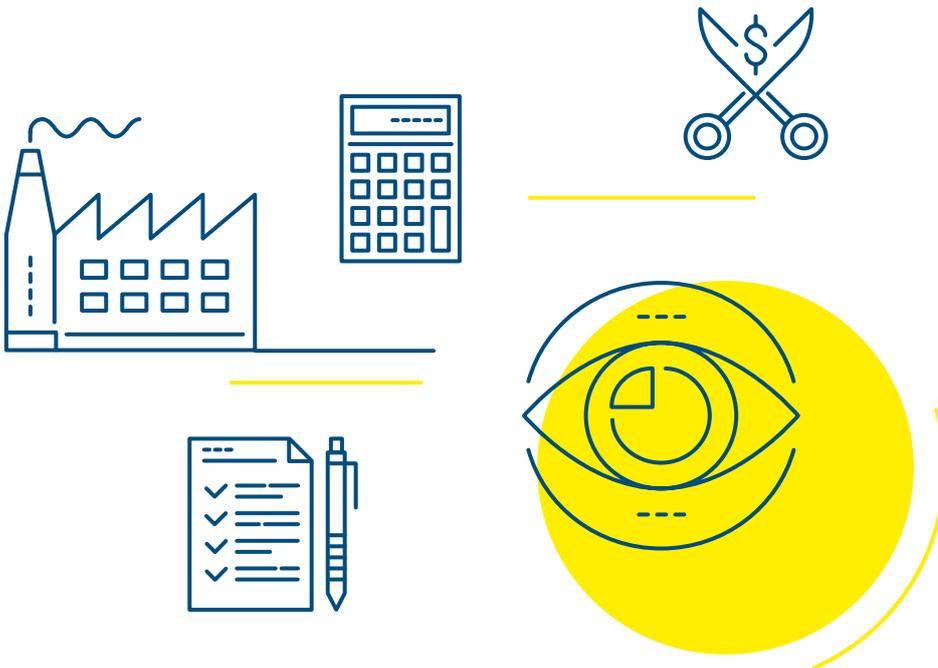
Source: own data from Ayiming Polska

Key conditions for claiming the R&D relief

A taxpayer intending to benefit from the R&D relief has to meet the following conditions:



- ✓ conducted R&D activity according to the legal definitions,
- ✓ incurred R&D costs that fit the catalogue of eligible costs,
- ✓ separated the costs eligible for deduction in the accounting records,
- ✓ presented the costs to be deducted in the tax declaration,
- ✓ has not received a refund of the eligible costs in any other form (i.e. grant).



How to obtain the R&D relief

To obtain the research and development relief, the following is needed:

- ✓ indicating the actions and the scope to which they constitute R&D activity,
- ✓ identifying the eligible costs according to the catalogue indicated in the legal acts,
- ✓ sharing eligible costs into categories indicated in the catalogue,
- ✓ showing them in the tax records this way,
- ✓ preparing documentation of R&D projects and staff documentation, if required, applying for individual tax interpretation,
- ✓ displaying the eligible costs in the form for an annual tax deduction - CIT-BR or PIT-BR,
- ✓ additionally deducting the eligible costs displayed in the CIT-BR or PIT-BR forms from the tax base to the amount corresponding to specific categories of costs.

“Acquiring the R&D relief requires using technical, staff and wage competences that dwell in various places in the organization. The key aspect is to properly diagnose research development activity, to deduct the relief optimally and safely. This requires cooperation of many departments in the organization.”

– comment by MA Eng. Karolina Łukasik

R&D consultant, Grants and R&D Relief Department, Ayming Polska.



INVOLVEMENT OF DEPARTMENTS IN THE BUSINESS IN THE PROCESS OF CLAIMING THE R&D RELIEF



R&D DEPARTMENT

- mapping R&D processes
- identification of R&D activities



ACCOUNTING

- identifying the eligible costs linked to R&D and matching them to the relief
- preparing the tax declaration
- applying for tax law interpretation
- direct contact with tax authorities



HR AND PAYROLL

- keeping worktime records
- calculating wages
- preparing hr documentation, such as agreements and job descriptions



BOARD

- making the decision to implement solutions
- possibly accepting the risk-relate

Savings made in fiscal year 2018

Case study



	TYPE OF ELIGIBLE COST	ELIGIBLE COSTS SIZE	% DEDUCTION	AMOUNT SAVED
	R&D personnel costs	1 000 000 PLN	100%	190 000 PLN
	Costs of materials	500 000 PLN	100%	95 000 PLN
	Costs of cooperation with academic entities	300 000 PLN	100%	57 000 PLN
	Depreciation costs	200 000 PLN	100%	38 000 PLN
	Total sum saved as part of R&D			380 000 PLN savings

Case study



CHEMICAL

Sector



500+

Employees



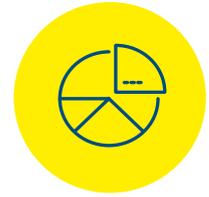
7,5 MLN PLN

Annual R&D
personnel cost



6 MLN PLN

Annual other
eligible costs



19%

CIT

	TYPE OF ELIGIBLE COST	ELIGIBLE COSTS SIZE	% DEDUCTION	AMOUNT SAVED
	R&D personnel costs	7 500 000 PLN	100%	1 425 000 PLN
	Cost of using research equipment	1 000 000 PLN	100%	190 000 PLN
	Patenting cost	100 000 PLN	100%	19 000 PLN
	Cost of materials	4 000 000 PLN	100%	760 000 PLN
	Cost of cooperating with academic institutions	500 000 PLN	100%	95 000 PLN
	Depreciation costs	400 000 PLN	100%	76 000 PLN
	Total amount saved as part of R&D relief			

2 565 000 PLN
saved

Myths about the R&D relief



Myth



Fact

#1

Claiming the R&D relief requires submitting a special application and undergoing a process of evaluating the project conducted.

Contrary to receiving EU funding, claiming the R&D relief does not require participation in any contest, and the results of the conducted R&D activity are not evaluated.

#2

The research-development activity needs to conclude with a successful outcome.

The outcome of the conducted R&D activity is irrelevant - one can also deduct the costs of projects that did not bring a positive outcome.

#3

The R&D project needs to be concluded.

Neither the beginning, nor the conclusion of the R&D project matters. The taxpayer may qualify costs of projects as they are taking place.

#4

It is required to display the level of innovativeness of the conducted R&D activity.

The level of innovativeness is irrelevant.

#5

Only commercialized results of R&D works can be written off.

Projects whose findings are used in own operations and the ones to be commercialized in the market can be written off.

#6

It is necessary to keep records of the eligible costs separated into projects.

The only requirement is keeping records of costs as divided according to their types, as listed in a legally indicated catalogue of eligible costs.

#7

The relief can be used only in reference to Polish projects.

The company may qualify costs of an international project as part of the relief, but this applies exclusively to costs incurred by the Polish company.

#8

Only companies that are cooperating with an academic entity are eligible to claiming the R&D relief.

This requirement is in place only when declaring the execution of basic research. The rest of the R&D activity does not require cooperation with an academic entity.

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