Business breathing a sigh of relief

5 years of R&D relief in Poland

ayming

Report 2021

Ayming is an international advisory group operating in 15 countries in Europe, Asia and North America. Ayming Poland supports companies in running their business operations in an optimal way and achieving better financial results, by offering professional advice in three areas:

- Innovation funding (R&D relief, IP Box, subsidies)
- Taxes (real estate tax, new investments and cost segregation)
- Labour costs (work accident insurance contribution, PFRON)

Ayming Poland chairs the Innovation Relief Team in the Tax Council of the Polish Confederation Lewiatan. The Group globally implements more than 15,000 projects per year in the field of obtaining EU subsidies and relief for R&D activities. The quality of services provided by Ayming Poland is confirmed by the ISO 9001:2015 Certificate.

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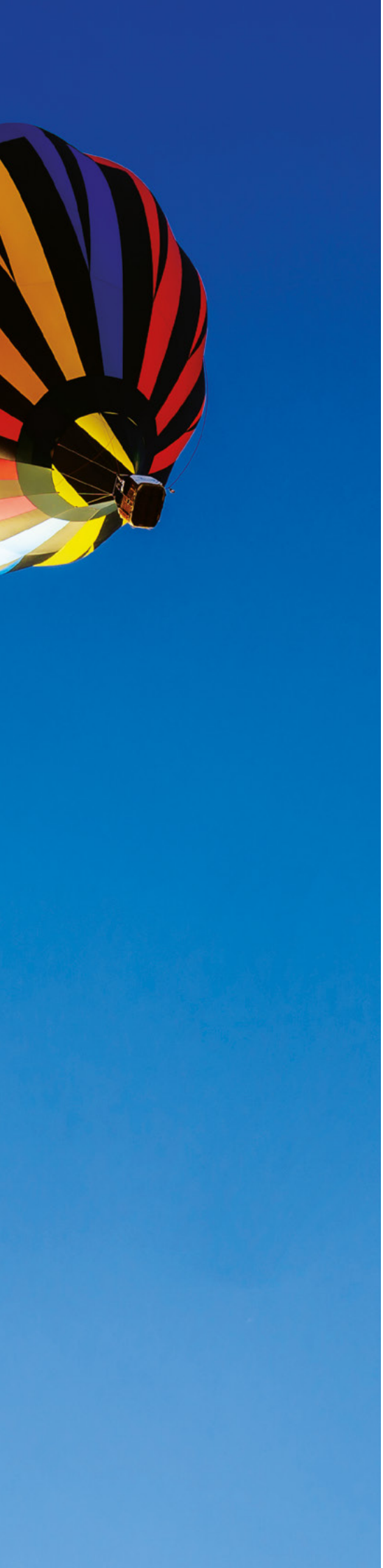

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Introduction

“In the five years that the relief has been in place, only a small number of R&D entrepreneurs paying income tax have taken advantage of this preference.”

In 2021, it is 5 years since the introduction of the research and development relief in Poland, which was supposed to encourage companies to increase R&D activities. This is therefore a good time for the first conclusions. Hopes for the new tax mechanism were high. The Ministry of Finance assumed hundreds of millions of zlotys of deductions (in 2019 it was supposed to be PLN 502 million) that would remain with entrepreneurs and enable them to increase their R&D expenditures. However, not once was the projected budget fully utilised. In the five years that the relief has been in place, only a small number of R&D companies paying income tax have taken advantage of this preference.

The beneficiaries of the R&D relief were to be everyone. First of all, entrepreneurs, because with new or improved products, processes or services they could increase their competitiveness and gain new contractors. Secondly, customers who could choose from increasingly modern solutions. These range from the totally mundane ones, such as an improved recipe for your favourite yoghurt, which will additionally be put in biodegradable packaging, to highly advanced IT technologies or medical products. And thirdly, Poland was to gain by becoming one of the world’s leading innovators and attracting further investors.

Next to national and EU subsidies, the R&D relief is the most frequently chosen tool to gain additional funding for R&D projects. However, it needs further promotion among entrepreneurs, as it remains an unfamiliar mechanism for many of them. Only half of our respondents carrying out R&D activities have heard of this preference, and of these, another half has used it at least once. The SME sector is the least likely to apply the R&D relief, and it is the sector that could benefit most from additional funds.

The past 5 years have shown that we are still at the beginning of building an innovation ecosystem in our country. The introduction of the R&D relief was an important step towards increasing the innovativeness of companies in Poland, but now changes are needed in the functioning of the relief itself. The aim is, for example, to minimise paperwork or to unify the line of interpretation of tax legislation so that taxpayers can settle the relief safely and without unnecessary difficulties. Changes are also needed in the whole system of innovation funding. Our respondents pointed out, among other things, the need for easier access to grants and for closer cooperation with scientific and research institutions or the reduction of formal procedures in applying for external financing.

I hope that our publication will be an impulse for a discussion on the direction of development of pro-innovation tax incentives in Poland and the expansion of support for domestic innovators.

Magdalena Burzyńska
Managing Director, Ayming Poland

5 facts about the innovation landscape in Poland

98%

of respondents regard innovation as an important factor supporting competitiveness

50%

of enterprises perceive their level of innovativeness as good as compared to international competition

29%

of companies are hampered from increasing their innovation by insufficient cooperation with scientific and research institutions

54%

of respondents would increase their R&D spending under the condition of easier access to grants

51%

of entrepreneurs have heard of the R&D relief

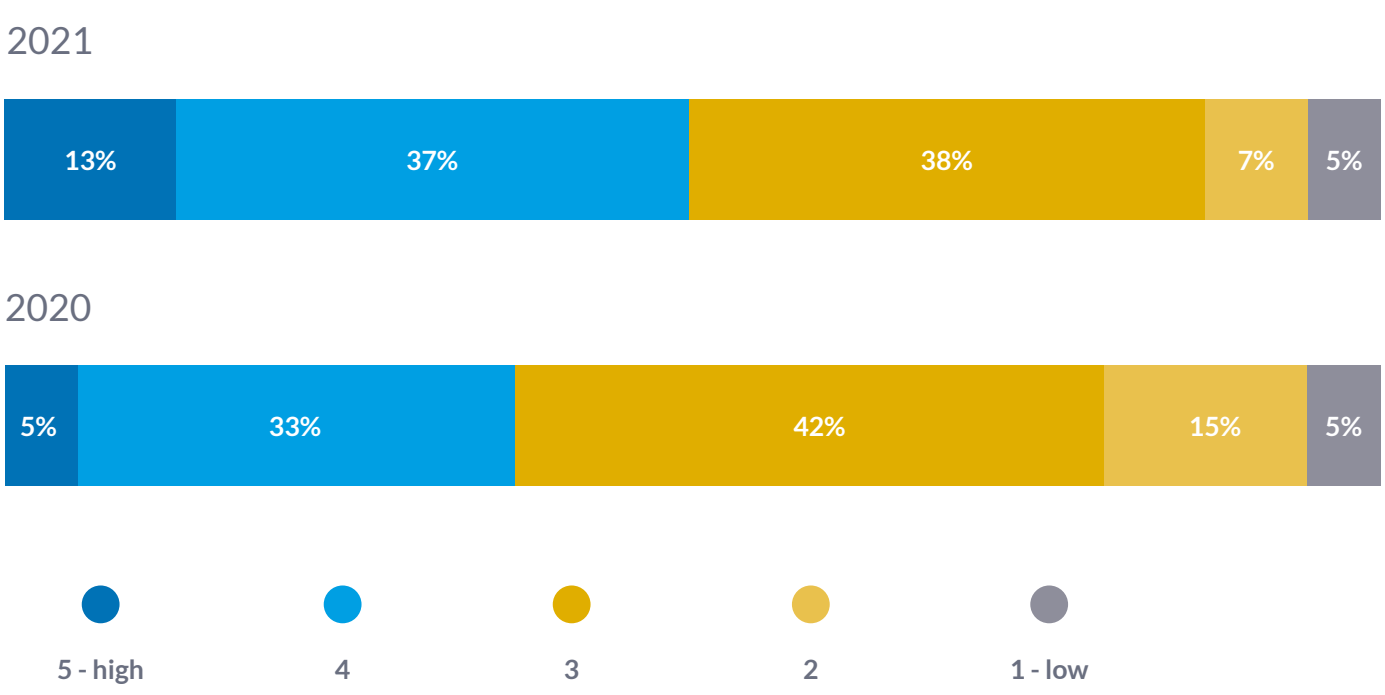
Strengths and weaknesses of Polish innovation

Almost all respondents (98%) believe, that innovation is important for a company's competitiveness, and for 48% it is even crucial. The highest percentage of respondents expressing this opinion comes from the following sectors: IT (83%), pharmaceuticals (80%), electronics (75%), aviation and food industry (67% each). These are highly competitive sectors in which innovation plays an important role.

Compared to international competition, half of the companies in Poland assess the level of their innovativeness as 4 and 5 on a scale from 1 to 5. This is a noticeable increase in comparison with the last year's survey, in which 38% of respondents considered their level of innovation to be good or high, of which only 5% gave themselves the highest score.

Slightly more than one in ten respondents rated the level of innovation of their company low (scores of 1 and 2), which is also a noticeable improvement. In 2020, one in five respondents felt this way. This year's results show that not only did the Covid-19 pandemic not affect the level of innovation of companies in Poland, but it may have encouraged them to intensify their pro-innovation activities, resulting in noticeably higher scores.

Self-assessment of the level of innovation of companies in Poland



2020 r., N=100 2021 r., N=101

Polish innovativeness as compared with Europe

Yet, positive individual assessments of entrepreneurs stand in contrast to the overall condition of domestic innovation. In the European Innovation Scoreboard 2020[1], Poland was ranked fourth from the bottom for the second time in a row. Although our country is ranked among moderate innovators together with Italy, Greece and Spain, it is only ahead of Romania, Bulgaria and Croatia by a hair (Poland's innovation index is 0.1 higher). Other countries in the region — the Czech Republic, Slovakia, Lithuania and Latvia — came before us. Sweden remains the most innovative EU country, followed by Finland, Denmark and the Netherlands.

According to the ranking, the Polish innovation system performs best in two categories:

- innovation-friendly environment (8th out of 27 countries) and
- the impact of innovation on employment (only 13th, behind the EU average).

In turn, the following categories are among the weakest:

- innovation in SMEs (last but one),
- links and cooperation (4th from last),
- attractiveness of the research system (3rd from last),
- financing and support (5th from last).

What causes the gap between entrepreneurs' self-assessment and their international performance? One answer may be the very narrow thinking about innovation, which is reduced to a finished product or service. In this area domestic innovators can do quite well. However, equally important are the other stages that lead to this innovation (e.g. access to qualified staff or cooperation with research centres) and then allow its appearance on the market (e.g. ease of commercialisation of technology, obtaining financing).

The PARP report states that in companies that are active in innovation, almost 3/4 of innovations are the responsibility of their owners or managers[2]. In the second position (63%) we have external environment in the form of customers, suppliers and entities form the sector, which are usually contacted by the managing staff. This means that innovation in Poland is based almost exclusively on decision-makers. In only one in four companies are creative employees outside the R&D team involved in the process, and in one in ten – those who work in it every day.

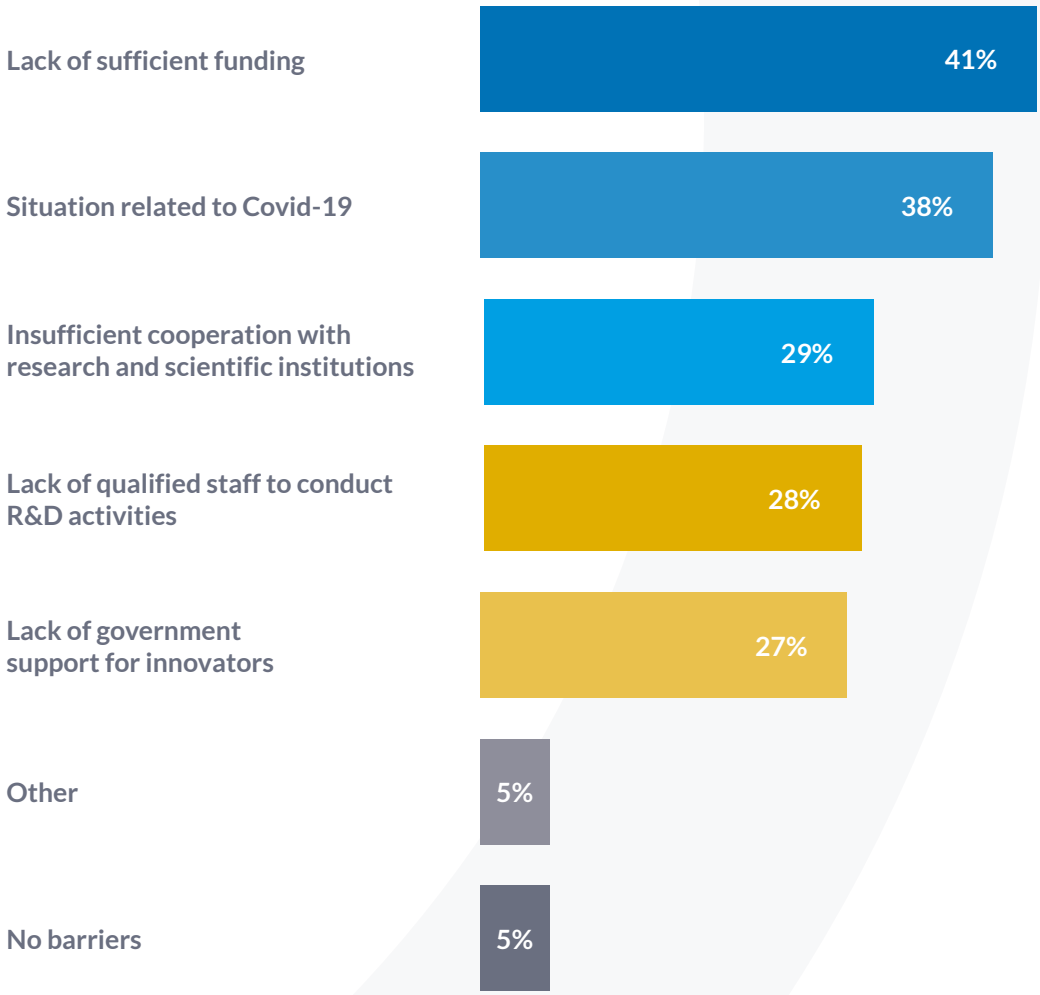
[1] *European Innovation Scoreboard*, available online: https://ec.europa.eu/docsroom/documents/42981 [30.03.2021].

[2] PARP, *Monitoring innowacyjności polskich przedsiębiorstw. Wyniki II edycji badania 2019*. Available online: https://www.parp.gov.pl/storage/publications/pdf/Raport-2019---II-edycja-Monitoring-innowacyjnoci-polskich-przedsibiorstw.pdf [30.03.2021].

Poor cooperation

As already mentioned, one of the weaknesses of Polish innovation is the lack of cooperation both between business & business and between business & science. 29% of enterprises surveyed stated that one of the barriers to increasing their level of innovation is insufficient cooperation with research and scientific institutions. Access to qualified staff capable of carrying out complex R&D projects also remains a problem for one in four respondents.

Barriers to innovation growth



N=101, multiple choice

The voice of science

In recent years, we have seen an increase in the interest and involvement of businesses in carrying out research and development activities. Companies have used the opportunities provided by tax reliefs for R&D and the support of research and development centres. This results in their dynamically increasing R&D expenditures. The reliefs are positively perceived by entrepreneurs. Business appreciates the real financial benefits and the motivational nature of the solution. This is a source of considerable satisfaction for me, as it is a good example of regulatory changes for innovation introduced by the government in which, as the minister in charge, I had the opportunity to work in the Ministry of Science and Higher Education under the leadership of Deputy Prime Minister Jarosław Gowin.

We have also observed an increased interest in cooperation between companies and research organisations such as the Łukasiewicz Research Network, which is best confirmed by the actively growing number of the so-called Łukasiewicz Challenges. In Q1 2021, the number of Challenges we undertook was comparable to the number for the whole year of 2020. We would like to involve Polish universities and other research organisations in these projects to a greater extent in 2021. We already have positive experiences of cooperation, mainly with technical universities, but we see very good opportunities in this area and we will want to make better use of them.

We have high hopes for strengthening cooperation between science and business under the National Recovery Programme, the European Funds Programme for Modern Economy and the Horizon Europe and Digital Europe programmes. From Łukasiewicz's perspective, it will be crucial to subsidise the Competence Centres, which aim to transfer knowledge and commercialise modern technologies and to support the development of small and medium-sized enterprises. We would like to create 7-8 such Centres in different regions of Poland in the next few years.

In 2021, we are also implementing a pilot project, the Łukasiewicz Accelerator, which will aim to support the development of start-ups based on the results of scientific research and development work created at Łukasiewicz. In this way, we want to create stable and highly skilled jobs for doctoral students and graduates. We have a lot to boast about in this respect, as we have currently over 100 ongoing implementation-based doctoral works at Łukasiewicz.

We want to strengthen the cooperation of Łukasiewicz and our partner universities with business by using e.g. Digital Technology Hubs to support the digital transformation of small and medium-sized enterprises. Łukasiewicz took part in the competition for Digital Technology Hubs, submitting 8 applications, and we hope that as many as possible will be selected. This will open up additional possibilities for us to offer modern services to companies, in particular to test their products, provide specialised training and consultancy services.

We are also pleased to have made many valuable contacts with other research organisations during the 2 years of Łukasiewicz Centre's operation. We are a member of EARTO and AIOTI and we are actively involved in the activities of the European Institute of Innovation and Technology. In 2020, our institutes became partners in EIT Urban Mobility, EIT Health and Climate-KIC. In addition, we continued cooperation with EIT Raw Materials and we obtained the status of a Polish Hub in EIT Manufacturing.

Our cooperation with foreign research organisations shows that we all have very similar challenges when it comes to cooperation between science and business. An additional challenge in the countries of Central and Eastern Europe is to strengthen the culture of innovation and trust in relations between science and business, as well as to demonstrate to the public that spending on R&D is an investment in the future, which in the long run determines the competitiveness of cities, regions and countries.

Piotr Dardziński, Ph.D.
President of the Łukasiewicz Research Network

Funding of innovative activities

Data from the Central Statistical Office (Polish: GUS) show that in 2019 gross domestic expenditure on R&D activities amounted to PLN 30.3 billion and reached 1.32% of GDP. A year earlier it was 1.21%, while the government's target presented in the Responsible Growth Plan was to reach 1.7% in 2020. Although the final figures have not yet been published, there are many indications that the target level could not be met, and the outbreak of the Covid-19 pandemic in early 2020 was just one of the factors that made this impossible.

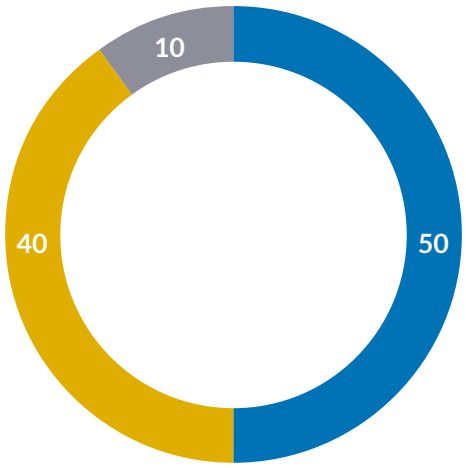
Despite the fact that Polish economy has not achieved its goal, year after year the expenses of enterprises on R&D activities have been systematically increasing. However, finding a budget for innovative projects still remains a big challenge. The results of our survey show that for 41% of those surveyed, lack of sufficient financial resources is the biggest barrier preventing innovation growth. 88% of them finance R&D projects from their own funds. In second place (43%) there are EU subsidies, with national subsidies ranking third (24%). The research and development relief is used by 16% of respondents.

R&D budget

It should be noted that in order to introduce innovation effectively, it is necessary to rely on one's own budget and supplement it with available instruments. It is very difficult to develop R&D activities effectively only on the basis of acquired funds, e.g. cash loans, credits or pro-innovation reliefs. In the case of such instruments as national or EU subsidies, the rules for participation assume that entrepreneurs must provide their own contribution.

How, then, does the problem of ownership and the amount of R&D budgets in companies in Poland look like? Half of the respondents admitted to having a dedicated budget for R&D projects. For 76% of the respondents it is sufficient and 18% admitted that it does not satisfy their needs related to R&D activities. It is worth noting that companies which have a separate R&D budget have a better perception of their innovativeness. As many as two out of three respondents without separate funds place their level of innovation at the lowest end of the scale (scores 1 and 2). In contrast, more than half of the companies with a separate R&D budget rate this level as high (scores of 4 and 5).

Having a dedicated budget for R&D



50% I have a separate R&D budget

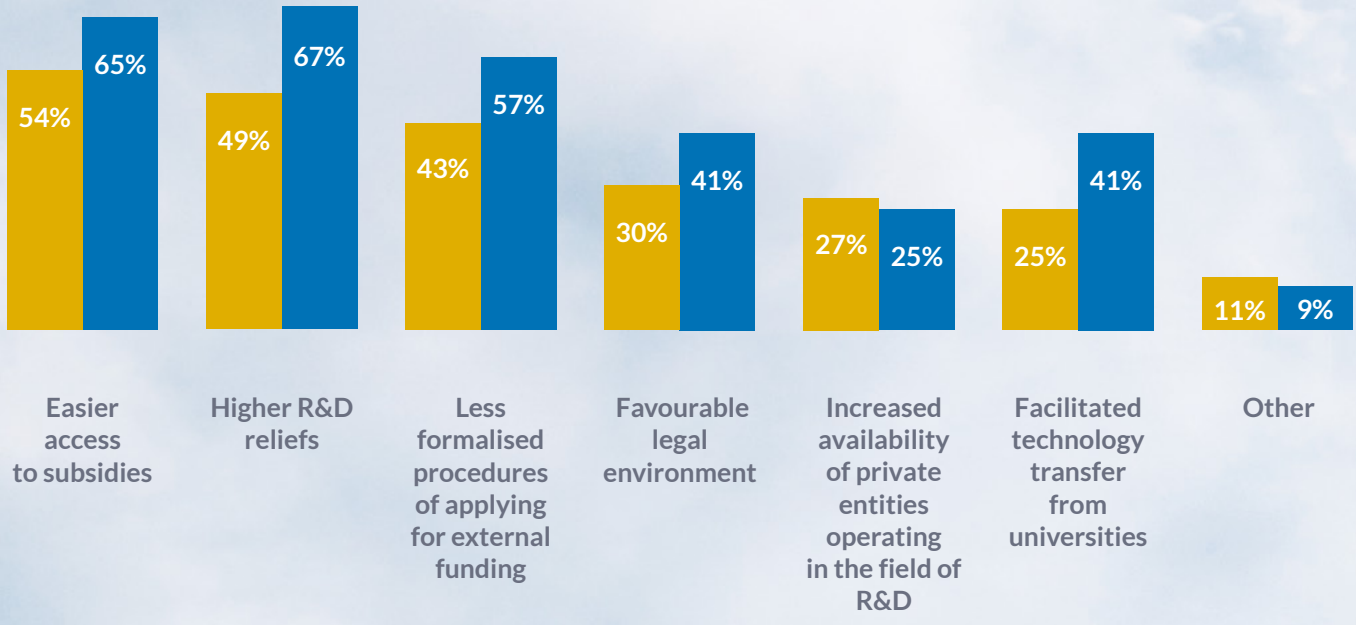
40% I do not have a separate R&D budget

10% don't know

N=101

Compared to the 2020 survey conducted prior to the Covid-19 pandemic outbreak, we see significant declines in responses regarding factors that could contribute to increased R&D investment. This might mean that in the current situation, still that of crisis, it is difficult for entrepreneurs to clearly assess what would be the most beneficial change for them. Nevertheless, the top three look similar to those of last year. In this year's edition of the survey, easier access to grants (54%) ranked first, ahead of the increase in R&D tax reliefs (49%) and less formal procedures in applying for external funding (43%).

Factors conducive to increasing expenditure on R&D activities



Multiple choice

Tools for innovators

Although the most popular source of R&D financing remains the company's own resources, entrepreneurs can use a wide range of pro-innovation tools and with their help supplement their own budget with external funding. The choice of the appropriate form of support should correspond to the time when the company wants to use it and the type of R&D activities in the company.

Below are the characteristics of the currently available tax mechanisms (as of April 2021).

National and EU subsidies

Time to use: action planning
Type of R&D activity: breakthrough innovations

Innovative projects that a company is planning to carry out can be financed with national or EU subsidies. It is then necessary to follow a pre-defined plan, and the results of the R&D activities carried out are important for the subsequent settlement of the subsidy.

Relief for Authors

Time to use: creation of a new product, service or process
Type of R&D activity: creative work of the employees

The relief for authors allows you to apply 50% of tax deductible costs to creative activity being original, unique, non-trivial, non-routine and with elements which individualise the author. The royalty should be clearly distinguished from other components of remuneration of an employee being an author.

R&D relief

Time to use: research, implementation work
Type of R&D activity: new or improved products, processes and services

Research and development costs that have already been incurred can be settled as part of the R&D relief. An entrepreneur may deduct 100% of eligible costs (150% for Research and Development Centres) from the tax base. The duration and effects of the actions carried out are irrelevant. The taxpayer is required to keep records of eligible costs and maintain documentation of R&D projects.

IP Box relief

Time to use: commercialisation of results
Type of R&D activity: creation, development or improvement of eligible IP

Companies that generate income by commercialising the results of their own R&D work can benefit from the preferential income tax rate of 5%. The IP Box relief covers a closed list of eligible intellectual property rights, including a patent, utility model, industrial design or copyright in a computer programme.

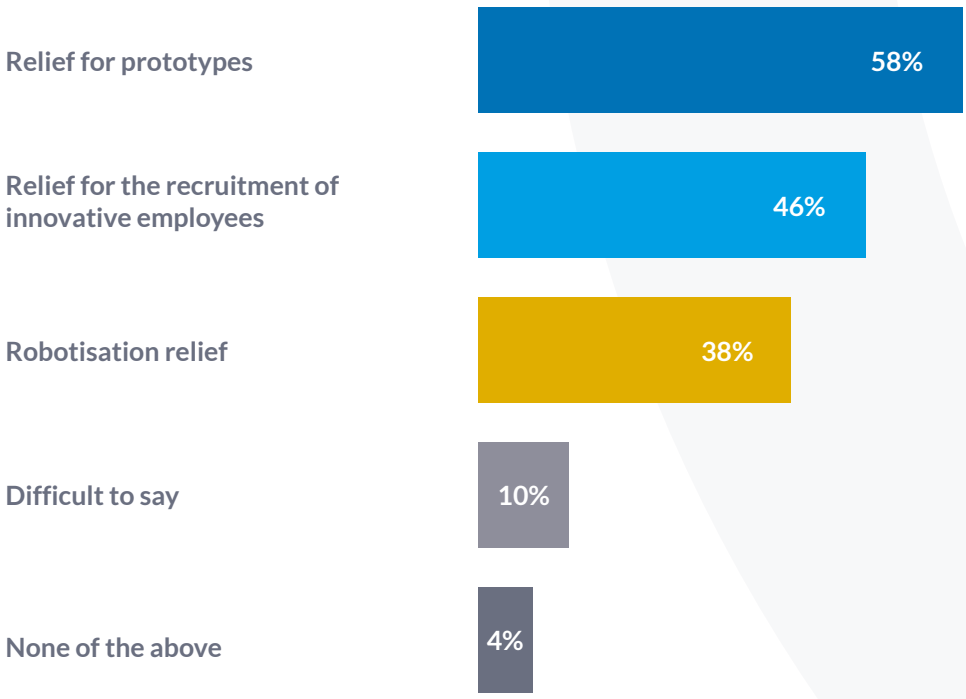
New relief proposals for innovators

For 2021, the Ministry of Development announced the introduction of new pro-innovation reliefs:

- **robotisation relief** - applies to a 50% deduction of costs of e.g. the purchase of new robots for industrial production and the training of employees. It is intended to be in force for a period of five years;
- **innovative employees relief** - it will enable a reduction in the value of the advance income tax payment and the value of the flat-rate income tax on the income from the employment relationship of employees engaged exclusively in research and development work;
- **relief for prototypes** - provides for a deduction of costs of trial production of a new product or of launching such a product on the market. The value of the deduction cannot exceed 30% of the costs incurred.

The most broadly discussed proposal to date has been the robotisation relief which was to be introduced as early as January 2021. The aim of this mechanism will be to increase production efficiency and reduce its costs. Interestingly, our survey shows that it is not among the solutions that are most awaited by entrepreneurs. There is much more interest in the relief for prototypes and the relief for employees working in R&D departments.

Willingness to use the planned pro-innovation reliefs



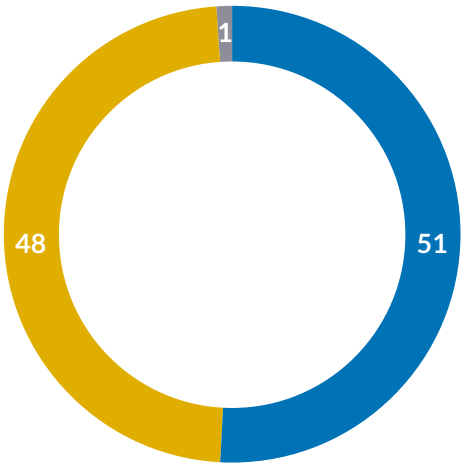
N=101, multiple choice

5 years of R&D relief

In the report of the Tax Council of the Polish Confederation Lewiatan[3] concerning recently introduced tax changes, the R&D relief was among the solutions which were perceived positively by 457 respondents. On the one hand, this is good news as it shows that both management and accountants appreciate this mechanism. However, on the other hand, the R&D relief was indicated by only 14% of respondents, which could mean that it is not a commonly used solution.

This is due to two reasons. First of all, the relief brings a tangible benefit only to entrepreneurs paying income tax (PIT or CIT) and conducting research and development activities, which reduces the number of beneficiaries significantly. Secondly, it appears that despite five years of the relief being in place, it is still not a widely known mechanism.

Our survey found that 51% of respondents heard of the R&D relief. The most common source from which they found out about it was the Internet (44%), then the press (19%) and their own finance or accounting department (13%). Government sources such as journals of laws, Ministry of Finance or National Centre for Research and Development websites, informed one in ten respondents. 60% of companies declaring a high level of their own innovativeness and 38% of those with a lower self-assessment have heard of the R&D relief.



Awareness of the existence of R&D relief

- 51% heard of it
- 48% have not heard of it
- 1% difficult to say

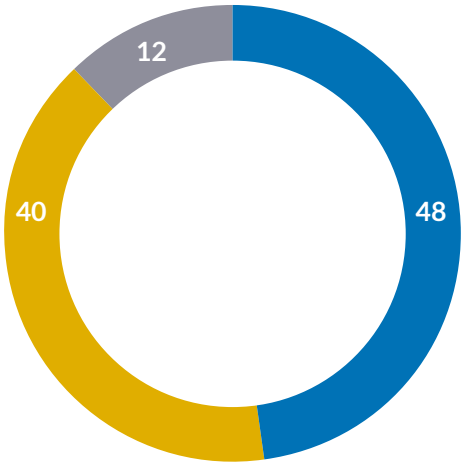
N=101

[3] Tax Council of the Polish Confederation Lewiatan, *Co wiesz o ostatnich zmianach podatkowych?*, 2020.

Settlement of the relief

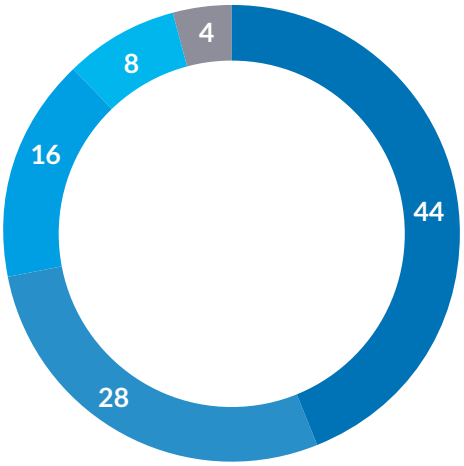
Of the companies that have heard of the research and development relief, 48% have used this mechanism. For almost half of them it was a one-off experience, and less than one in three applied the relief twice. Taking into account the size of a company, as much as 70% of enterprises with 250 or more employees have used this tax preference at least once. In the case of the smallest companies (30-49 employees), half applied the R&D relief, while among those with 50-249 employees it was only 32%. It is worth mentioning that as many as 14% of respondents from this segment did not know whether their company used the relief or not.

Has the company used the R&D relief at least once?



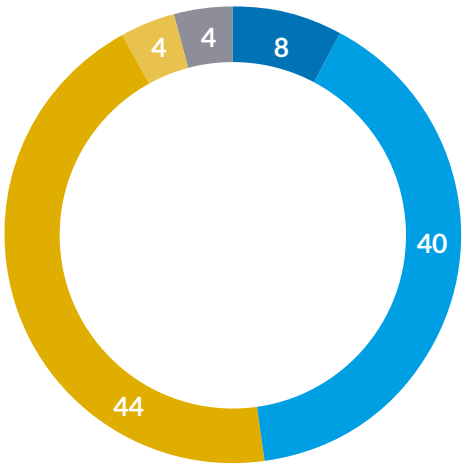
48% yes
12% don't know
40% no
N=52

How many times have you applied the R&D relief?



44% once
8% more than 3 times
28% twice
4% don't know
16% 3 times
N=25

The R&D relief is primarily settled by the company's employees. Almost always (92% of responses), the accounting, finance or legal departments are involved. For one in four respondents, it is also handled by the management board and the R&D department. The assistance of a consulting company is used by 12% of respondents, while cooperation with an external accounting office or law firm is declared by 8%. The funds coming from the settlement of the research and development relief primarily fund further R&D activities (80% of indications) and are invested in company development (68%). To a lesser extent, they are spent on improving the competences of employees (36%) or the current activities of the company (20%). The question of how significant the funds obtained from R&D relief settlement are for a company's budget is a very interesting one. The same percentage of respondents (48% each) declare that they are an important source of additional financing as well as that they do not play a significant role in the budget.



Importance of the R&D relief for a company's budget

- 8% very important
- 40% rather important
- 44% rather unimportant
- 4% definitely not important
- 4% difficult to say

N=25

Increase in the value of deductions

The reason why taxpayers have so rarely applied the R&D relief in the five years of its functioning may be due to the low value of the deductions and the limited catalogue of eligible costs in the first two years of the relief's applicability. It was only in 2018, as part of the so-called Big Law on Innovation, that the attractiveness of the deduction was increased to 100% (150% for Research and Development Centres), the differentiation of the size of the deduction depending on the category of eligible costs and the size of the company was abolished and the catalogue of costs was expanded.

In June 2021, the Ministry of Finance announced further changes to make the R&D relief more attractive. From 2022, the amount of deductions for Research and Development Centres will increase from 150% to 200% Moreover, all taxpayers conducting R&D activities will be able to deduct as much as 200% of personnel costs instead of the previous 100%.

CHANGES IN THE AMOUNT OF DEDUCTIONS OF THE RESEARCH AND DEVELOPMENT RELIEF IN POLAND	PERSONNEL COSTS	OTHER ELIGIBLE COSTS	
	SMEs and large companies	SMEs	Large companies
2016	30%	20%	10%
2017	50%	50%	30%
2018-2021	100%	100%	100%
from 2022*	200%	100%	100%

*According to the draft amendment to the CIT and PIT Act of 15 June 2021.

Potential problems

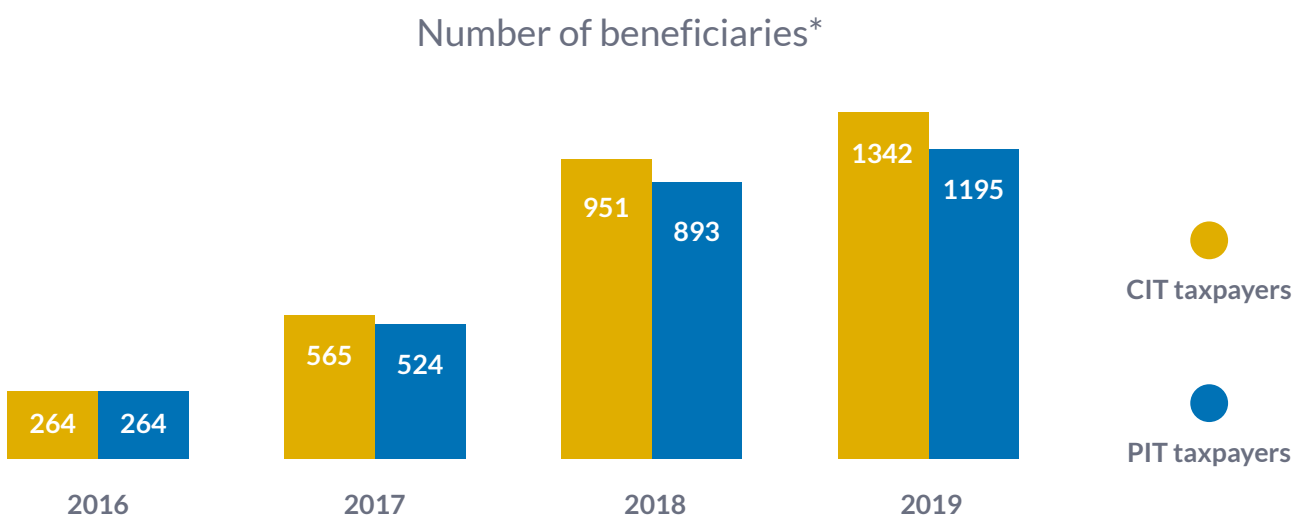
Although the R&D relief has already become established in the Polish tax system, it is still a big challenge to unify the line of interpretation of the Director of the National Fiscal Information Centre and to eliminate interpretation discrepancies of some regulations. A good example of such discrepancies is the possibility to deduct a part of remuneration relating to the time of excused absence of employees (annual leave or sick leave) as personnel costs.

The Supreme Administrative Court, in a judgment of 5 February 2021, held that if an employee devotes 100% of his or her time to R&D activities, the remuneration associated with his or her excused absence may be considered an eligible cost for the R&D relief. So far, the Director of the National Fiscal Information Centre, in individual interpretations issued, has treated absences as the performance of professional duties which are not related to research and development activities. Therefore, these components are not deductible under the R&D relief.

Another example of discrepancies concerns the incidental nature of R&D projects. In individual interpretations issued in 2018, the Director of the National Fiscal Information Centre indicated that research and development work cannot be incidental. The interpretation line adopted by the authorities was that incidental activities, although they fall under the statutory definition of R&D activity, cannot be settled under the relief because they do not meet the requirement of regularity.

The above position was also adopted by Voivodship Administrative Courts, which examined complaints against individual interpretations issued by the National Fiscal Information Centre. It was not until the Tax Clarification on IP Box - PIT of 15 July 2019 that the Ministry of Finance indicated that any activity that meets the statutory definition of R&D activity is eligible for the relief, and the argument of incidental nature is artificial.

R&D relief in numbers



	2016	2017	2018	2019
	Amount of deductions - 19% or 17% of the indicated amount* [PLN]			
CIT	198 million	543 million	1 675 million	2 248 million
PIT	8 million	41 million	179 million	293 million
	Financial impact on the budget** [PLN]			
AMOUNT OF DEDUCTIONS	206 million	584 million	1 854,8 million	2 541,7 million
PROJECTED EFFECT	none	200 million	361 million	502 million
OBSERVED EFFECT	39,1 million	111 million	352,4 million	482,9 million

Source: * Data obtained from the Ministry of Finance in April 2021, ** Own elaboration based on data obtained from the Ministry of Finance in 2018 and 2019.

R&D relief in Poland as compared with the Czech Republic and Germany

The R&D relief is a fiscal mechanism promoting R&D activities which has been known in Europe for several decades. In the world, it was first introduced as early as 1944 in Canada. As for European countries, the earliest definition of R&D relief appeared in Spain in 1978. In contrast, German taxpayers had to wait the longest for this mechanism - they have only been using it since 2020.

Below we present the scope of the R&D relief applicable in Poland as compared with our two neighbours – the Czech Republic and Germany. It is worth noting that, compared to other European countries, the application of the relief itself is relatively simple in Poland. All you need to do is submit a tax return with the CIT-BR or PIT-BR attachment. It is not subject to evaluation by any committee and the taxpayer does not need to have additional certificates, such as a document certifying the conduct of R&D activities (such a requirement is in place e.g. in Italy).

However, it is important to prepare appropriate internal documentation, including descriptions of R&D projects and to create accounting records of eligible costs. Taxpayers may also be asked by the tax office for their own justification for applying the relief or undergo a tax audit for the last five fiscal years.

	POLAND	CZECH REPUBLIC	GERMANY
YEAR OF INTRODUCTION OF THE RELIEF	2016	2005	2020
RATE OF DEDUCTION FROM TAX	19% CIT 17% PIT	19.3%	25%
% OF ELIGIBLE DEDUCTIBLE COSTS	100% for entrepreneurs up to 150% for R&D Centres	100% 110% for each increase in R&D expenditure as compared to the previous year	25% (or a cash loan of up to €1 million per year)
NUMBER OF YEARS BACKWARDS TO BE ACCOUNTED FOR	5	1	4
ELIGIBLE COSTS	• personnel costs • materials, including raw materials • expert opinions, other opinions, advisory services, research purchased from a scientific entity • special equipment used directly for R&D activities • depreciation of fixed assets and intangible assets • purchase of the service of using scientific and research equipment • the costs of obtaining a patent, utility model and industrial design protection costs • the use of scientific and research equipment for consideration	• personnel costs • materials, including raw materials • depreciation of fixed assets • operating costs (electricity, water, heat, gas, etc.) and low-value assets • travel costs directly related to R&D projects • financial lease • purchase of services and know-how from R&D companies • certification of the results of research and development work (e.g. homologation)	• personnel costs • 60% of external research costs
MAIN DIFFICULTIES	• identification and scope of activities regarded as R&D work • separation of eligible costs • the taxpayer must keep the necessary documentation for 5 years	• the formal part of projects is as important to the tax authorities as meeting the criteria of R&D activities • even minor irregularities may result in a refusal to apply the R&D relief	• using the relief requires a technical certificate proving the eligibility of projects

Source: own elaboration based on „The Benchmark 2021" published by Ayming. Available online: https://www.ayming.pl/the- benchmark/ [30.03.2021].

Comment by Ayming Germany

Marcus Arens
Director of Sales and Marketing

The research and development relief in Germany is the first mechanism allowing entrepreneurs to recover costs they have previously incurred on research and development activities. In this respect, it is an attractive alternative to grants, which are the primary form of innovation funding. In total, up to 3,000 different subsidies can be applied for in Germany at EU, national, regional or local level. Their allocation is based on competitions with quite strict requirements, so companies are never sure if they will receive funding for their innovation projects.

A major challenge for taxpayers wishing to use the R&D relief in Germany is the requirement to obtain a technical certificate confirming the R&D activity. Such a certificate is issued by a special institution appointed by the Ministry of Development, and the waiting time for obtaining it varies from 8 to 12 weeks. As the R&D relief is a newly launched mechanism, it is difficult to tell how popular it will become with taxpayers in Germany. The Ministry of Finance predicts a tax refund of €2.5 billion for the first year of the relief's applicability.

Comment by Ayming Czech Republic

Kristína Šumichrastová
Managing Director

In the Czech Republic, the R&D relief has been in place for a relatively long time, since 2005. The application procedure itself is quite simple, which makes the relief a more favourable option for obtaining funding for innovative activities compared to subsidies. Unfortunately, the number of R&D projects in the private sector is steadily declining, as indicated by the total number of companies applying for R&D relief in recent years. In 2015, it was used by 1,306 entrepreneurs, while in 2019 only by 940.

The reason for this may be the increased number of obligations imposed on taxpayers. These include e.g. the need for prior notification of the intention to use the relief, the creation of project documentation and keeping a detailed register of changes. No less important is the attitude of tax authorities, which are increasingly stringent in the process of justifying the right to apply the R&D relief. This results in lengthy and tedious financial audits.

“High five” for innovation

The following are 5 demands for the next 5 years of the R&D relief. In them, we indicate the directions of change we propose in order to make the relief an even more attractive mechanism, applicable by a larger group of taxpayers.

#1
Higher deductions for all

The first demand is to increase deductible costs for all businesses. Our observations show that some taxpayers are interested in using the R&D relief, but its amount is too small in relation to the effort required.

It should be noted that a similar solution, albeit on more preferential terms, is offered by Slovakia. Our southern neighbours can deduct up to 200% of costs incurred on R&D activities regardless of the status of the enterprise. More favourable conditions also apply in other countries offering a mechanism similar to the Polish R&D relief. In the UK this is a deduction of 230% of eligible costs, while in South Africa it is 150%.

#2
Settling the depreciation of fixed assets

A significant improvement would be the clarification of the provisions of the Act regarding the possibility of settling the depreciation of fixed assets produced or improved as a result of research and development activities. In its current form, the mechanism of the relief allows the costs of depreciation write-offs on fixed assets or intangible assets that were used in R&D activities to qualify. However, what if the fixed assets are the result of R&D work, their creation required incurring costs (e.g. for materials or wages) and depreciation starts only after the completion of the R&D project? The current provisions of the Act do not clarify this issue, and the line of interpretation of the National Fiscal Information Centre does not point to a specific solution either. As a result, this creates uncertainty for taxpayers.

Not being able to settle this type of cost would be unfair to some companies carrying out R&D projects. As an example, let us consider the process of creating a prototype resulting from R&D activities. If this prototype becomes a fixed asset at the end of the project and remains in the company's stock, the taxpayer cannot settle the costs related to its creation under the R&D relief. At the same time, if the entrepreneur decides to consider the prototype as an intangible assets and not as a fixed asset, the relief mechanism allows to settle depreciation write-offs on such a prototype.

#3
Settling employment costs under B2B contracts

Pursuant to Article 18d(2) and (3) of the CIT Act, eligible costs incurred by the taxpayer are costs resulting from employment contracts, contracts of mandate and contracts for a specific task. Due to the trend observed in the economy of an increasing number of one-person businesses, it is worth considering the inclusion of the costs of hiring employees under B2B contracts in the R&D relief. This form of activity is very often chosen by representatives of the IT industry, who are the beneficiaries of the relief.

In our opinion, the key criterion for the eligibility of personnel costs should be the nature of cooperation between the taxpayer and its employees, rather than the legal form of the contract signed. Creating the possibility of deducting the costs of R&D work provided under B2B contracts, if they are one-person businesses, will increase the attractiveness of the relief and will encourage entities conducting R&D activities to use such services.

#4
Settling the costs of technical/technological consultancy

It is worth considering extending the catalogue of eligible costs to include costs relating to expenditure on services such as technical consultancy or professional technological advice. In their current form, they are eligible to be settled under the R&D relief if they are provided by scientific entities. These should also include companies and firms specialising in technical or technological consultancy.

Such a solution will allow taxpayers to deduct from the tax base costs related to the use of experience and expertise of external specialists who can increase the effectiveness of R&D works conducted by the company. This will also make it possible to significantly reduce the risks that are generally associated with research and development projects. A similar preference is already used in Italy. Taxpayers there can settle the cost of procuring technical consultancy from external companies.

#5
Settling costs related to the certification of new products

An important phase of R&D work is bringing a new product to the stage of implementing it into serial production. Before this happens, a final verification of the parameters of the developed solution should be carried out, e.g. through certification by an external entity authorised to issue relevant documents. This is still a risky moment, as the product may not meet the parameters necessary to complete the certification process. The stage of final validation is an indispensable element of R&D work, as it makes it possible to determine whether the developed product still requires work or whether it has met all the required conditions allowing for its production and sale.

Therefore, we propose extending the catalogue of eligible costs to include costs related to the stage of final product verification and certification. In particular, services related to: preparation of documentation necessary to obtain a certificate, homologation, CE marking, safety mark, obtaining or maintaining a marketing authorisation or other compulsory documents or markings related to marketing or use permit of a product. Such a solution is already implemented e.g. in Portugal (part of audits and certification in R&D activities are eligible costs) and in the Czech Republic (certification of R&D results is an eligible cost).

Expert comment

The R&D relief is a mechanism that is gaining in popularity year on year. This happens for several reasons. First of all, there is a growing awareness among entrepreneurs of the existence of such a tax preference and the savings that can be made. The second important aspect concerns the increasingly stable legal environment related to R&D relief. Issues that initially raised many doubts and uncertainties have been largely clarified both in the field of individual tax interpretations and in the decision of Voivodeship Administrative Courts or the Supreme Administrative Court.

Third, the rules for using the relief have evolved over the five years of its functioning, adapting to market realities and business needs. The changes introduced responded well to the needs of companies and have made the relief more and more business-friendly, while the savings generated by it have become more and more tempting.

Nevertheless, there are still some issues that need to be modified. They constitute a barrier to the use of the relief by many entrepreneurs and often understate the deductible costs. The changes we are proposing are part of the national policy of supporting innovation, but above all they are a response to the expectations of entrepreneurs themselves. The need for additional fiscal incentives related to R&D activities is also recognised by the legislator.

The announced proposals (including the robotisation relief) will enable the innovation ecosystem to adapt to the dynamically changing business environment. Moreover, further preferences can help to maintain the continued growth in R&D expenditure, which is crucial for business development. Policies that promote innovation provide the foundation for the country's future economic growth and increase its international competitiveness.

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Methodology

The report was prepared based on Ayming Poland analyses and a CATI survey carried out by Opinia24 among 101 companies. The survey was conducted from 11 February to 9 March 2021. The companies that qualified for it were those with 30 or more employees, that are active in the sectors involving R&D. These included: machinery and equipment manufacturing (24% of respondents), metal and non-metal processing (21%), chemicals and automotive (8% each), IT and food (6% each), pharmaceuticals and construction (5% each), and electronics and energy (4% each). Depending on the size of a company, the questions were answered by the owner, CEO, general manager, CFO or development manager.

Preparation of the report

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