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Mr Brian Boyle
Principal Officer
Incentives and Financial Services Branch
Revenue Commissioners
Dublin Castle
Dublin 2

18 December 2014

Dear Mr. Boyle

Draft R&D guidelines

Thank you for the opportunity to provide comments on the draft updated R&D Guidelines (the Guidelines). Given the time allowed we have collated our comments and observations in the list below.

There are a number of positive changes in the Guidelines, for example greater clarity in relation to the treatment of R&D employee costs and expansion of the guidance in relation to the software development sector. There are elements of the Guidelines that appear substantially different to previous practice and guidance and would appear more restrictive in approach, for example in relation to eligible expenditure. It is important that companies can be clear on their entitlements to relief and that the approach adopted aligns with the policy objective of encouraging and supporting R&D activity.

We have outlined our specific comments on the Guidelines below.

Different industries have different "norms" in relation to documentation produced and retained that could support an R&D claim. This is also the case when comparing smaller businesses with larger businesses. As discussed with your colleagues at the November TALC Audit sub-committee meeting it would be helpful to engage in a round-table with the various stakeholders on the types of records to be maintained. We think this would be of benefit to all sides in providing greater certainty as to whether a claim will be accepted, and in facilitating the efficient operation of R&D audits.

As these Guidelines substantially revise the previous guidelines it is important that it is very clear to readers what has changed. We would welcome publication of an appendix to the Guidelines highlighting what paragraphs have changed, the nature of the change and the effective date of the changes.

Comments and observations

- We note the reference to "*The tax credit is an adjustment to tax and is calculated separately from the normal deduction of the R&D expenditure in computing the taxable profits of the company"* (paragraph 2.1, page 4). We presume that this has no implications for the "above the line" accounting treatment allowed for IFRS and Irish GAAP purposes. Perhaps the wording could be made clearer.
- It would be useful to provide clarity on the refund process (paragraph 2.4, page 6) where additional information is sought to substantiate an R&D claim.
- We note that Revenue is of the view that "Social Science Activities are excluded from the definition of qualifying activity" (paragraph 3.2, page 11). This is a growing area of activity within R&D and we would welcome the chance to discuss this area further.
- It would be useful if there was a page number reference included for the Frascati manual quote (referred to in paragraph 3.7, page 13).
- Paragraph 3.7 also refers to large scale developments using established project governance methodologies lending themselves to closer tracking of qualifying and non-qualifying costs. We think it would be useful to reference smaller scale projects here to recognise while appropriate deliverables and expenditure tracking procedures need to be in place, less formal governance methodologies may be in operation.
- We note the expansion in the guidelines in paragraph 3.7 on software development methodologies in the sector and this is a welcome development.
- Paragraph 4.1, page 16 includes a number of new elements and details additional areas of cost categories that Revenue considers do not qualify as relevant expenditure such as *"travel, recruitment fees, insurance, equipment repairs or maintenance, shipping, business entertainment, telephone…"* and a change in relation to the position for overheads. This differs from the position in the current guidance and as indicated in legislation which clarifies that administration and general support services which are not wholly and exclusively undertaken in connection with an R&D activity will not be qualifying R&D activities. We are unclear as to the rationale for change in the absence of change in legislation on this area.
- The exclusion in relation to overheads associated with the employment of an individual e.g. HR costs, etc. would seem quite a restrictive interpretation (paragraph 4.2, page 17). For example, a company may need to incur HR costs to recruit a targeted R&D specialist through a recruitment agency or through internal HR resources.
- We note a reference to the fact that proprietary directors must provide a higher level of proof as to costs incurred (page 16). It is not fully clear from the guidance what is expected from the taxpayer here.
- We understand from our discussions at Main TALC that the reference to *"substantial amount*" in the context of allowable pension costs (paragraph 4.2, page 17) is to be removed.
- We would like to see the concession agreed with Revenue in relation to costs related to individual consultants hired on a part-time or short-term basis to undertake sub-contracted activity reflected in paragraph 4.3, page 17.

- Paragraph 4.6, page 18 notes that the ‘cost’ value of the materials which remain after the R&D activity should be deducted from the expenditure claimed. We are unclear as to the legislative basis for this approach.
- It would be welcome if clarity could be provided on how relief for buildings used for R&D can be claimed in situations where a building may take a number of years to be constructed e.g. the aggregate expenditure treated as incurred when the building is first brought into use. It would be appropriate to also clarify here the position as regards building purchased and used for R&D activity (paragraph 5.1, page 19).
- Tax Briefing No. 59 of 2005 provides clarity on Revenue’s position where expenditure is incurred on machinery or plant over more than one accounting period before the asset is brought into use. It would be useful to include the relevant extract from the Tax Briefing in paragraph 5.3, (page 21).
- We note that the Department of Finance Review of the R&D Credit 2013 indicated that the Irish regime allows the outsourcing to take place “anywhere in the world”. The Guidelines in paragraph 6.1, page 24 seem to indicate that outsourcing is limited to Member States. Perhaps this matter could be clarified in the Guidelines.
- The clarification provided in paragraph 7.7 (page 28) in relation to change of ownership and the base year is welcome. It would appear that some text has been omitted from the first line of the second example (page 28).
- We note that extra emphasis is given in relation to maintaining records for the “base year” (paragraph 8, page 30). Given the provision in Finance Bill 2014 to abolish the base year the base year records will only be relevant in the context of historic audits and it may merit removal of this requirement as time passes.
- We note that extra emphasis has been added to “contemporaneous” records being available for inspection by Revenue to support a claim. As noted above, we think it would be worthwhile to have engagement between the various stakeholders to discuss appropriate records to be held given the different norms operated by different sectors.
- The wording in paragraph 8.2, page 31 in relation to *“The following records required to be maintained to satisfy the accounting test*” could imply that the list provided is an exhaustive list of what is required. It should not be the case that where a company is not in possession of all the records listed a claim would automatically be treated as invalid. As noted above, different records may be held depending on the sector and the size of the business, which would still satisfy Revenue that a claim is valid. Perhaps the Guidelines could note that the list is not an exhaustive list.
- If there is a general briefing document provided to external experts setting out what steps they are expected to take in coming to their conclusion it would be useful to include a link to this document in the Guidelines in paragraph 10, page 35.

Should you have any queries in relation to the above please do not hesitate to contact us.

Yours truly

Cora O'Brien

Cora O’ Brien
Director