Patent box and R&D incentives in selected European Countries

Newsletter on current information and developments

Japan External Trade Organisation

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Newsletter on current information and developments

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Preface

This newsletter provides information to governmental regulations on incentives for research & development in selected European OECD Countries with special focus on tax incentives for innovation/patent boxes and R&D tax credits.

As regulations change frequently, we strongly recommend seeking professional advice before making any decision.

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Introduction

Introduction to R&D tax incentives

Countries have different approaches how to apply R&D tax incentives. Every scheme has some particularities, but in principle there is a distinction between income based and expense-based R&D tax incentives.

R&D tax incentives based on the income from an innovation are the so-called Innovation/Patent Boxes. They apply a reduced corporate tax rate to profits from patents and similar intellectual property. It should be noted that as part of the OECD's Base Erosion and Profit Shifting Project 2015, countries have adopted the "Modified Nexus Approach for IP Regimes", because of this companies must have R&D activities in the same jurisdiction as where their IP is owned to benefit from Patent Box rates.[1]

Tax incentives for innovations that are based on the R&D expenses of a company are R&D tax credits and special R&D deduction e.g. accelerated depreciation on R&D assets and enhanced allowances. Accelerated depreciation and enhanced allowances reduce a company's income and subsequently its tax liability. R&D tax credits are deducted from the tax liability and might even result in a negative tax liability (tax refund). Tax refunds are effective for new firms in their start-up phase where they often generate losses.

In many countries governmental institutions provide financial support by direct payments on certain R&D assets or expenses as well. For EU Countries such financial support is generally subject to state aid regulations adopted by the European Commission.[2]

For the measurement of R&D activities many countries adopted the definitions of the Frascati Manual[3] measuring the expenditure and personnel resources devoted to R&D in the sectors performing it: business, private non-profit organizations, higher education and governments. For the measurement of Innovation activities, many countries adopted the definitions of the OECD's Oslo Manual.[4]

In October 2021, the international community agreed a landmark deal involving a two-pillar solution to address the tax challenges arising from the digitalization and the globalization of the economy. As part of this plan, Pillar Two introduces domestic rules that establish a global minimum effective corporate tax rate of 15% for large multinational enterprises (MNEs) with consolidated group revenue of at least EUR 750 million. Wherever tax incentives drive an MNE's effective tax rate in a jurisdiction below 15%, the MNE would potentially be subject to top-up taxes under the GloBE (Global Anti-Base Erosion) rules, a core component of Pillar Two. The OECD report "Tax Incentives and the Global Minimum Corporate Tax"[5] is a tool for jurisdictions in evaluating the potential impact of Pillar Two on different types of tax incentives and provides recommendations for jurisdictions to consider in reassessing their tax incentives environment considering GloBE implementation.

Due to the increased offering of R&D incentives and use of R&D incentives by businesses, a market for specialised consultants assisting companies in making claims for R&D incentives has developed.

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1 Action 5: Agreement on Modified Nexus Approach for IP Regimes," OECD/G20 Base Erosion and Profit Shifting Project, 2015, https://www.oecd. org/ctp/beps-action-5-agreement-on-modified-nexus-approach-for-ip-regimes.pdf. Update July 2022 https://www.oecd.org/tax/beps/harmful-tax-practices-peer-review-results-on-preferential-regimes.pdf.

2 European Commission adopts revised State aid Framework for research, development and innovation 19 October 2022; https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12777-State-aid-rules-for-research-development-innovation-framework-_en.

3 The Measurement of Scientific, Technological and Innovation Activities Frascati Manual 2015 https://ec.europa.eu/eurostat/cache/metadata/Annexes/isoc_se_esms_an2.pdf

4 https://www.oecd.org/science/oslo-manual-2018-9789264304604-en.htm

5 OECD (2022), Tax Incentives and the Global Minimum Corporate Tax: Reconsidering Tax Incentives after the GloBE Rules, OECD Publishing, Paris, https://doi.org/10.1787/25d30b96-en. https://www.oecd.org/tax/tax-incentives-and-the-global-minimum-corporate-tax-25d30b96-en.htm.

Belgium

Country introduction and overview

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Belgian tax law provides for specific incentives for R&D. Belgian taxpayers can benefit from an additional tax deduction or tax credit on their R&D expenditure. According to the Belgian patent box regime, taxpayers are entitled to an 85% deduction of their net innovation income from their tax base. Belgium also promotes investments in R&D through a reduction of the employment cost of researchers and through direct funding by means of cash grants.

Innovation/Patent Box

Entitlement

Qualifying taxpayers
Under the Belgian Innovation income deduction (IID), Belgian taxpayers (irrespective of their size) can deduct 85% of the net innovation income from the tax base. The IID is based on Action Point 5 of the OECD BEPS Action Plan (applying the so-called Modified nexus approach) and replaces the (previous) Belgian patent income deduction (PID) regime.

Qualifying IP
Qualifying intangibles include patents and supplementary protection certificates, breeders' rights, orphan drugs, data and market exclusivity and IP of copyrighted software resulting from a R&D project which has not yet generated income before 1 July 2016, regardless of the country where the intangible is protected. A temporary exemption applies for taxable periods during which the intangible is still under request.

Trademarks and other marketing related intangibles do not qualify under the IID regime.

Ownership conditions

The taxpayer should have the full ownership, co-ownership, usufruct or license of or right on a qualifying IP. "Any right" is sufficient.

Development and management conditions

In line with BEPS Action 5, net innovation income is considered only in proportion to the share of expenditure related to R&D activities performed in-house and outsourced to unrelated parties in the overall expenditure related to the R&D activities. To this end, innovation income is multiplied by a fraction, the so-called modified nexus ratio, which reflects the share of qualifying expenditure in the overall expenditure. As a result, the IID is granted only to companies to the extent that they also engage in effective R&D activities

Administrative guidance states that for acquired IP rights improvements could be eligible for IID without an effective IP right being granted. Expenses for the acquisition of IP are considered non-qualifying and are reflected only in the denominator of the modified nexus ratio.

The type of R&D activities (i.e. outsourcing to third/related parties, acquisition of IP, etc.) have an impact on the IID calculation through the modified nexus ratio. Where the R&D activities are performed, in Belgium or abroad, has as such no impact on the calculation of the benefit.

Qualifying income (eligible income)

Qualifying income includes license income, income embedded in sales income (i.e. the license fee that a third party would pay if that third party produced the goods (or services delivered) on the basis of a license granted by the company, which is included in the Belgian tax base of the company), income derived from process innovation and remunerations received on the base of a court/arbitral decision, amicable settlement or insurance contract. The income should be included in the Belgian tax base of the company of the taxable period.

Proceeds derived from the sale of an IP right qualify as innovation income to the extent that the IP right has the nature of a fixed asset, which was either created no later than during the previous taxable period or was acquired no later than in the course of the last 24 months. A reinvestment condition within 5 years of the sales price applies.

Quantifying the benefit

The IID is calculated on a net basis, meaning that the gross income for a given year is decreased by the deductible R&D expenditure with respect to the qualifying IP. That amount, being the net innovation income, is multiplied by the modified nexus ratio, i.e. a fraction reflecting the extent to which the taxpayer itself incurred qualifying R&D expenditure. The qualifying R&D expenditure is reflected in the numerator (i.e. R&D expenditure directly connected to the qualifying intangible incurred by the company itself or compensation for outsourced R&D activities to non-related companies), increased with an uplift of 30% (up to maximum the amount of the overall expenditure). The denominator includes the overall R&D expenditure, consisting of the qualifying R&D expenditure, R&D expenditure for related party outsourcing and acquisition costs for the qualifying intangibles. 85% of that amount can be deducted from the corporate income tax base.

The first year a taxpayer applies the IID after 1 July 2016, the gross innovation income should be reduced with the overall expenditure from the previous taxable years, ending after 30 June 2016 (some exceptions apply). At that point, the taxpayer can opt irrevocably to spread these costs during a period of maximum 7 consecutive taxable years.

Any unused IID can be carried forward without any limitation in time or amount.

Application process

The following formalities have to be complied with when applying the IID. At the time of the annual corporate income tax return, a special form has to be added to the corporate income tax return. Furthermore, in case the IID is applied with respect to copyrighted software, a certificate should be obtained from the Federal Public Service Science (Belspo) confirming the innovative character of the software (as long as the software is being further developed). The taxpayer is required to have certain supporting documentation available for its qualifying IP. Furthermore, a ruling can be requested.

Other aspects

As mentioned above, the former PID regime was replaced by the IID regime in order to be BEPS compliant.

Since more conditions apply in order for income derived from the sale of an IP right to qualify as innovation income compared to for example license fees, administrative guidance takes into account tax abuse in this respect. Guidance states that in case fees are obtained in the context of an agreement, other than an agreement of alienation, that actually leads to the exclusive assignment of the exploitation of the IP right for its entire duration are therefore a priori considered subject to the same conditions as the fees obtained following the sale of the IP right. The taxpayer can rebut the application of this anti-abuse measure by proving that the selection of its legal act is justified by motives other than the avoidance of income tax.

R&D tax credit

Entitlement

Belgian taxpayers (irrespective of their size) can benefit from an additional tax deduction or tax credit on their environmentally friendly R&D expenditure. Indeed, on top of the general tax deductibility of R&D expenditures, Belgian taxpayers may opt for capitalizing these R&D expenditures following which an investment deduction or tax credit can be claimed.

For a long time, no general definition of R&D was included in Belgian tax law. Reference was made to accounting law as well as to the Frascati Manual. Eventually the Belgian legislator introduced a tax definition of the terms research and development in Belgian tax law, based on the OECD definition in the Frascati Manual.

Ownership conditions

Based on current ruling practice, it is not required for the taxpayer carrying out R&D activities to own all IP resulting from the R&D activities as long as the taxpayer can demonstrate that the know-how created at the level of the R&D center will increase the future performance of the R&D center and will contribute to the taxpayer's future profitability. This implies that taxpayers carrying out contract R&D activities can also claim an R&D investment deduction/tax credit, notwithstanding the fact that the R&D costs concerned are typically charged on to the beneficiary of the R&D activities.

Please note that challenges by the tax authorities in this respect are increasing, so it should be further assessed to what extent the R&D investment deduction/tax credit can be applied in the particular case at hand. Furthermore, an advance ruling in this respect is highly recommended.

Development and management conditions

In order to qualify, both the tangible assets and the intangible assets have to be new. In this respect, it is irrelevant whether the assets concerned are acquired from third parties or are self-developed. Contrary to their position on tangible assets, the Belgian tax authorities accept the qualification as new for intangible assets as long as the assets have not been used in Belgium for business purposes.

As mentioned above, based on ruling practice, it is not required for the taxpayer carrying out R&D activities to own all IP resulting from the R&D activities. R&D can be performed abroad, but management and oversight need to take place in Belgium.

Quantifying the benefit

The R&D investment deduction/tax credit is aimed at capital expenditures, including both tangible and intangible fixed assets. Tangible assets in practice cover those assets that are used to carry out R&D activities. In principle, such tangible assets need to be used within a qualifying R&D center. Tangible assets are generally depreciated over their economic lifetime. Examples are: IT equipment, lab utilities, buildings, office furniture, and prototypes.

Intangible assets, on the other hand, are defined as R&D expenses, i.e. the costs of the research, manufacture and development of prototypes and products, inventions and know-how, which are useful for developing the taxpayer's future activities. Patents, licenses and know-how also qualify. Also in this case, such intangible assets need to be utilized within a qualifying R&D center, but again limited exceptions are available. Examples are: payroll costs of the researchers, self-developed patents, patents licensed from third parties, non-patented technologies, and R&D costs that are recharged.

Constituting an allowance, the investment deduction results in a decrease of the tax base. As they have no tax base, lossmaking taxpayers cannot actually benefit from this measure. As such, the Belgian tax legislator has opted to also provide for a tax credit, the amount of which equals the amount of the investment deduction multiplied by the statutory corporate income tax rate (25% as of tax year 2021). Hence, the tax credit is identical to the investment deduction, be it that the tax credit is a credit against the tax effectively due.

In the case where, however, no tax is due, the tax credit becomes refundable after a 5-year period (including the year to which the tax credit relates, i.e. the year during which the qualifying investments were made). This incentive can take the form of a one-shot deduction or credit or a spread deduction or credit. The one-shot deduction/credit is calculated as a percentage on the acquisition value of the qualifying assets. For tax year 2023, this percentage amounts to 13.5%. The spread deduction/credit, on the other hand, is calculated as a percentage on the yearly depreciation of the qualifying assets. For tax year 2023, this percentage amounts to 20.5%. Generally, the one-shot deduction/credit results in a net tax benefit of approximately 3.4%, whereas the spread deduction/credit results in a net tax benefit of approximately 5.1%.

Both the investment deduction and the tax credit can be carried forward, be it that, once the tax credit has been opted for, the investment deduction can no longer be applied (complex transitory measures exist in this respect). The investment deduction can be carried forward indefinitely whereas the tax credit, as mentioned, is repaid after a 5-year period. For both the investment deduction and the tax credit, the yearly amount that can be claimed is capped.

Application process

The following formalities have to be complied with when applying the (spread) R&D investment deduction/tax credit. At the time of the annual corporate income tax return, a special form has to be added to the corporate income tax return. Furthermore, a certificate should be obtained from the Flemish/Walloon/Brussels Region confirming the innovative and environmentally friendly character of the development (depending on where the R&D center is located). A separate and yearly updated “defense” file in relation to the application of the R&D investment deduction/tax credit should be kept at the disposal of the Belgian tax authorities. A ruling can be requested in this respect.

Other aspects

In order to avoid abuse of the R&D investment deduction/ tax credit incentive, the Belgian legislator has introduced a list of assets that are excluded from application of the investment deduction or tax credit, including amongst others fixed assets that cannot be depreciated and assets with a depreciation period of less than 3 years and fixed assets acquired or developed with a view to transferring the right to use the assets.

In addition, Belgian tax law requires that the tangible and intangible assets acquired from third parties (other than patents) are used to carry out qualifying R&D activities during the entire depreciation period. If this condition is no longer met and the assets are for example allocated to another purpose during the depreciation period, an investment deduction/tax credit recapture rule will apply. This recapture rule does not apply in the case where the tangible and intangible assets concerned are sold or put out of use. Indeed, in this case, Belgian tax law explicitly provides for an additional investment deduction/tax credit in the case where one applies the spread investment deduction/tax credit. Finally, note that upon a change of control of a Belgian taxpayer having a carry-forward investment deduction or tax credit, the deduction and credit are in principle forfeited, unless the change of control meets legitimate financial or economic needs.

For the Belgian R&D tax credit to be considered a qualified refundable tax credit for Pillar Two purposes, it is very likely that Belgian tax law will be amended, and that the remaining R&D tax credit will become repayable after four years instead of five.

Other R&D related incentives

Cash grants

Cash grants for R&D activities in Belgium are administered by the respective governments (Flanders - *VLAIO*, Brussels Capital Region - *Innoviris* and Wallonia - *SPW*). Each have their specific grant programs but in general they are categorized into:

- R&D grants focusing on development of new products, services, or processes. Both individuals as well as consortia of companies can apply for this funding.
- Investment grants linked to the implementation of innovative production processes.
- Investment grants for ecology and sustainability.

Most grants are non-repayable and fund costs such as wages, investments, overhead/consumables, subcontracting, etc. It’s important (often mandatory) that project proposals must be submitted before the actual start of the project.

More information on these grants can be found on the following websites:

- https://www.vlaio.be/nl
- https://innoviris.brussels/get-funded
- https://recherche.wallonie.be/home.html

Reduced payroll tax for qualifying researchers

A partial withholding tax exemption for research and development is available in Belgium. This exemption can be applied by companies if the following (cumulative) conditions are met: the applicant must execute R&D activities, the R&D projects should be notified with Belspo prior to starting their execution, the employees need to perform R&D activities and the employees need to be in the possession of a qualifying degree (PhD, master’s, or bachelor’s degree in (applied) sciences, engineering…).

A maximum of 80% of the Belgian payroll tax can be exempted on behalf of the employees for whom the aforementioned conditions are met, with a cap for exemption claimed for employees holding a bachelor's degree of 25% of the total exemption claimed for the employees holding a Master's or a PhD. It should be considered that the time spent on R&D activities (indicated by a percentage of the total working time of the employee) should be considered when determining the maximum of 80%. The exemption can only be applied for those employees that are included on the Belgian payroll. One should note that, contrary to the past, the benefit obtained from the application of the partial wage withholding tax exemption cannot be applied in combination with the R&D tax credit for the same expenses.

A project or program can be considered as an R&D project if it falls within the scope of the definition of scientific research as foreseen by the Belgian legislator. A binding advice with regards to the R&D activities can be obtained with Belspo.

France

Country introduction and overview

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The two main R&D incentives available in France are:

- the IP box regime, which provides for a reduced 10% CIT rate on eligible IP income
- the R&D tax credit provides for a tax credit based on the R&D expenses incurred by French taxpayers

It is possible for an enterprise to cumulate the advantages provided by both regimes.

Innovation/Patent Box

Entitlement

Qualifying taxpayer
The French IP box regime applies to businesses of all sizes (large, small, medium-sized enterprises) subject to either personal income tax or corporate tax in France.

Where an enterprise is subject to income tax, it can avail of the IP box regime only if it is placed under a standard regime (i.e., a regime whereby the expenses deducted are the expenses actually incurred, as opposed to expenses computed on a lump sum basis).

Qualifying IP
The qualifying IP rights are set out as follows:

- Patents
- Industrial manufacturing processes, provided that they cumulatively meet three conditions, namely: (i) they are the result of research activity, (ii) they are necessary to the exploitation of a patent, (iii) they are sold or licensed with the patent they are attached to pursuant to the same contract
- Plant variety rights
- Software, on condition it is protected by a copyright (in French law, a copyright protection can only be delivered to a software that meets an originality condition)

In contrast to the above items, trademarks, know-how and industrial designs are not covered by the French IP box regime.

French law states that the IP box regime applies to eligible IP assets that bear "the character of fixed assets". Nevertheless, in light of parliamentary preparatory works, this wording is to be interpreted broadly. As such, one should rather consider the IP box regime also covers IP assets that have been fully amortized and assets whose acquisition fees have been completely deducted as operating expenses, notwithstanding the fact they are not registered in the balance sheet of the enterprise.

The IP box regime is also applicable in the event the qualifying IP asset is obtained through licensing. In this case, the royalties paid by the enterprise to the licensor are taken into account to compute the net income derived from the IP asset. In this case, the eligible income corresponds to income derived from the sublicensing of the eligible asset.

How is the regime applied to the qualifying IP rights?
The French IP box regime is optional. The enterprise is free to choose for which qualifying assets it will opt for the IP box regime.

The election for the IP box regime is made for:

- Each qualifying IP asset (in principle)
- Each good or service including IP assets
- Each set of goods or services including IP assets

Where the applicant enterprise chooses to opt for the second or the third choice, it must provide justifications as to the fact that the election on an asset-by-asset basis is not feasible based on the accounting data available.

For instance, in the event multiple assets are required to develop a given good or service (*e.g*., a formula for a medicine), or a set of goods or services (the different versions of a software), it may be difficult to single out R&D expenses as well as the income raised by each intangible asset.

The French IP box regime has been rehauled precisely to comply with the new OECD standards and is therefore in line with the nexus approach.

Ownership conditions

The IP box regime applies where the applicant has legal ownership of IP assets or where it holds contractual rights on those assets (e.g., case of the licensee).

Development and management conditions

The regime may apply to acquired IP if the buying enterprise incurs R&D expenditures to further develop the IP. Since the acquisition costs are only taken into account at the denominator of the nexus ratio, it may trigger a decrease of that ratio. The IP box regime is also applicable to existing IP.

R&D activities can be subcontracted to a third-party located abroad but not to a related party. Nonetheless, subcontracting to a foreign PE of the taxpayer is considered subcontracting to a related entity.

Qualifying income (eligible income)

The scope of the regime encompasses licensing and sublicensing fees, as well as the proceeds from the sale of IP. For this purpose, the concept of license is understood broadly and refers to any agreement granting a right of use on the qualifying IP (e.g., franchise agreement).

Regarding the sale of IP, the IP box regime is applicable on condition that, (i) the IP asset is not sold to a related party and that (ii) the said IP asset was acquired, for a consideration, at least two years prior to the sale.

Some expenses must be deducted from those income, namely: R&D expenditures or acquisition fees which share a direct connection with the development or the acquisition of the intangible asset. For this purpose, the concept of R&D expenditures is given the same meaning as for the R&D tax credit.

According to the guidelines of the French tax authorities, the following expenses must be deducted:

- Research personnel fees
- Raw materials expenses, as long as they are used to create or develop the intangible asset.
- Acquisition of technical installation fees
- Machinery and equipment expenses, provided they are used to do research
- Costs incurred for the acquisition of a qualifying asset
- Expenses related to the outsourcing of the R&D activities

Those expenses must be deducted whether they have been engaged directly or indirectly by the enterprise.

Income derived from the sale of goods and services including IP cannot benefit from the IP box regime. Only the income derived from the sale or the licensing of the qualifying IP themselves can benefit from the said regime.

Quantifying the benefit

Computation of the gross income
For each financial year, the gross income equals to all the qualifying income deriving from the same IP asset, good or service or set of goods or services.

In practice, where the same agreement covers both eligible and non-eligible assets, two situations may occur:

- The contract allocates the price between eligible and non-eligible assets; in which case, the gross income corresponds to the income allocated to the eligible assets
- The contract does not provide such an allocation, but only indicates an overall price. In this situation, the enterprise must allocate the said price between eligible and non-eligible assets. That allocation must rely on objective criteria. It can be based on comparable transactions that were realized within the same timeframe and related to comparable IP assets. Other data, such **as the**

intrinsic value of the qualifying IP rights, the price paid for the acquisition of those rights or a cost-based approach can also be taken into account.

Computation of the net income
For each financial year, the net income equals to the gross income from the IP asset minus the R&D expenses related to that same asset, as mentioned above.

Depending on the choices made by the enterprise, the computation of the net income will be made on an asset-by-asset basis, for each good or service including IP or for each set of goods or services including IP, or a combination thereof.

In the event, the first years following the election give rise to a net loss (R&D expenses incurred for the IP asset exceeding the eligible income), that net loss must be offset against the first net profit derived from that same IP asset (claw-back rule).

Application of the nexus ratio
The nexus ratio is computed as follows:

$$\frac{\boldsymbol{Qualifying\ expenditures\ incurred} \times \mathbf{130}\%}{\boldsymbol{Overall\ expenditures\ incurred}}$$

Where:

- Numerator: The qualifying expenditures incurred are the R&D expenditures directly incurred by the enterprise or the R&D expenditures it has outsourced to a non-related party in order to develop the IP asset. The law provides that they are to be multiplied by 130%.
- Denominator: The overall expenditures incurred are all the R&D expenditures directly or indirectly incurred by the enterprise, i.e. the R&D expenditures included at the numerator plus those outsourced to related parties and the acquisition costs incurred with regard to eligible IP assets

The ratio cannot exceed 100%.

Additionally, the ratio must be applied to the net income generated by the IP asset for which the enterprise intends to benefit from the IP box regime.

In the event the enterprise is part of an integrated group, the outsourcing of R&D operations to related parties pertaining to the group no longer reduces the tax advantage of the IP box regime.

In case of exceptional circumstances beyond the enterprise's control, the enterprise may, under particular conditions, request to swap the nexus ratio for a substitute ratio. Nevertheless, that exchange of ratio is subject to obtaining ministerial approval.

Standard tax rate / tax rate under the regime
Standard French corporate tax rate is 25%. Concerning personal income tax, it relies on progressive rates, with a maximum rate of 45%, for the fraction exceeding circa EUR 168,000. Under the French IP box regime, income generated by using qualifying IP is taxed at a 10% rate.

Carry forward to later assessment years
Losses incurred for the IP Box regime in relation to an asset, good or service or set of goods or services must be carried forward. However, they must only be set off against the net income generated by the same asset, good or service or set of goods or services on the following tax years.

Instead of applying the 10% rate, it is also possible to set off the net income derived from qualifying IP assets against the tax loss incurred by the enterprise for the tax year.

Application process

In order to apply for the French IP box regime, taxpayers are to attach an additional form to their income / corporate tax return. As a reminder, the option is to be made separately for each intangible asset, good or service and set of goods or services, depending on the accounting data available.

Other aspects

Following the election, the enterprise must provide, for each fiscal year, additional forms to its tax returns. In order to comply with those reporting obligations, the enterprise must keep track of the income derived from those said asset, good or service and set of goods or services as well as the eligible expenses incurred therefrom. In case of non-compliance with those reporting rules, a 5% fine is to be applied on the income derived from the IP assets for which the reporting obligations have not been respected. Should an IP asset that has been placed under the IP box regime not be mentioned within the reporting form of a following tax year, then the benefit of the IP box is lost regarding that asset.

Additionally, the enterprise shall keep specific documentation (consisting in (i) a general description of its R&D activities, (ii) a list of the eligible assets, goods or services, sets of goods or services for which an election has been made, (iii) details concerning the nexus ratio applied to each of those items and (iv) indications as to the way the deductible expenditures have been allocated to each of them) at the disposal of the tax authorities.

The upcoming Pillar Two regulations ensure that a minimum effective tax rate of 15% is met per jurisdiction. The patent box regime provides for a 10% statutory tax rate on net eligible income. It will therefore impact the effective tax rate of the French entity/ies, although the jurisdictional blending may lower its impact.

There is no special measure to avoid misuse of the R&D tax incentive schemes in French law. Be that as it may, anti-abuse measures such as GAAR (general anti-avoidance rules) or transfer pricing rules may help avoid misuse of the IP box regime.

R&D tax credit

Entitlement

The R&D tax credit applies to enterprises whose activity consists in business, manufacturing or agriculture. The applicant enterprise may either be subject to corporate tax or personal income tax. In the latter case, it must be either placed under a standard taxation regime or be placed under a qualifying tax exemption regime, notably but not limited to free zones or the innovative new enterprises regime. The size of the enterprise is not a criterion taken into account by French law. As far as R&D is concerned, there is no specific sector which benefits from a better tax treatment in comparison to others.

R&D activities qualifying for a tax credit encompass:

- Basic research
- Applied research
- Experimental development

The definitions of the above items in French law are in line with the Frascati Manual, even though they are not a word-for-word translation of the definitions provided by this document.

In addition to these definitions, the R&D tax credit Guide published by the French Ministry of Research uses the 5 criteria for evaluating the reality of scientific research of the Frascati Manual, namely

- Novelty
- Creativity
- Technical uncertainty/ Technological lock to solve
- Reproducibility / contribution of new scientific knowledge
- Systematic character / an R&D organization must be in place

Ownership conditions

The ownership of the IP resulting from the R&D is not a condition to benefit from the R&D tax credit.

Development and management conditions

R&D operations can be performed (i) in France or (ii) in another EU member State or (iii) in a State that has partaken to the Agreement on the European Economic Area and has entered into a mutual administrative assistance for tax matter treaty with France (EU, Norway and Iceland). As the ownership of the IP resulting from the R&D is not a condition, it can reside abroad. The staff must be hired under a French employment agreement.

The exception to this general rule is the taking into account of costs related to IPs in the computation of the R&D tax credit, which is not possible if there is no ownership of the IP concerned.

R&D activities subcontracted to external service providers are eligible for the R&D tax credit, under certain conditions. Service providers may be established in France, in an EU member State or the European Economic Area (EU, Norway and Iceland) and must be approved by the Ministry of Research.

To be eligible for the R&D tax credit, outsourced R&D activities must in principle be carried out directly by the organizations to which they have been entrusted and by its direct subcontractors, but exceptions exist. subcontracts of rank 3 and above are not eligible. This condition obliges the taxpayer to ensure the traceability of the cascade of subcontractors.

The conditions for subcontracting are strengthened to limit multi-tier subcontracting which would result in the same research expense being taken into account several times for the computation of the R&D tax credit.

Subcontracting eligible for the R&D tax credit must meet a need for specific skills and resources to carry out an R&D operation. The subcontractor must be responsible for the scientific coordination of the research service. The enterprise must clearly justify the individualization of tasks and the identification of identification of the deliverables.

Quantifying the benefit

Eligible expenditures are as follows:

Depreciation of fixed assets used exclusively to perform research activities
Assets under leasing are considered fixed assets and can be depreciated as such.

Personnel expenses
They concern researchers, research assistants and technical staff involved in R&D project, e.g. to carry out tests. The expenses included in this category are as follows:

- Salaries (for the fraction which effectively corresponds to R&D activities where the employee also carries out other activities)
- Employment taxes, in as much as they are computed on the salary taken into account for the computation of the R&D tax credit and paid by the employer
- Sums accrued to the employee profit-sharing regime (*i.e.,* a plan required by French law for all entities with more than fifty salaried employees)

Additionally, French law contains an incentive for enterprises to hire young PhDs. Under it, upon first hiring of a PhD, the salaries paid by the employer are taken into account for twice their amount during the first two years of employment. The benefit of this measure is conditional on the PhD to be granted a permanent contract and on whether the number of salaried research personnel of the company is not less than that of the previous year.

Other operating expenses
Those expenses correspond to a lump sum amount which is equal to:

- 75% of R&D depreciation costs
- 43% of R&D personnel expenses
- and 200% of "young PhD" wages

Further expenses
- Expenses incurred for IP protection (registration, maintenance and defense of patents and plants variety rights, under the condition of ownership of the related IP in France
- Costs related to standardization
- Expenses incurred for technological watch, up to EUR 60,000
- Subcontracted R&D activities to a public or private subcontractor, approved by the Ministry of Higher Education and Research.

Whether they are entrusted to public or private organisms, R&D expenditures are capped to three times the cost of R&D activities directly carried over by the applicant enterprise for the purpose of determining the Research Tax Credit (CIR: Le crédit d'impôt recherche). Consequently, should an enterprise not perform any R&D activities, then it cannot avail of the CIR for any of its outsourced R&D operations.

In addition, for the computation of the CIR, subcontracted R&D activities are capped to

- EUR 2 million, if the applicant enterprise and its subcontractors, be they public or private organisms, are related entities.
- EUR 10 million, in the other case.

Subsidies
Public subsidies received by companies for operations that give rise to the tax credit are deducted from the basis for calculating the tax credit, whether they are definitively acquired by the company or reimbursable. When these subsidies are refundable, they are added to the basis for calculating the tax credit for the year in which they are refunded to the organization that paid them.

The tax credit equals to:

- 30% of the eligible expenses incurred below EUR 100 million.
- 5% of the eligible expenses incurred beyond EUR 100 million.

In French overseas departments (Guadeloupe, Guyana, Martinique, Mayotte and Reunion) a 50% rate applies instead of the 30% rate. The 5% rate, however, remains unchanged.

There is no cap on benefit. The tax credit is to be set of against the income tax or corporate tax of the tax year in which the eligible R&D expenses have been incurred. Should there be a remaining amount of tax credit, it can be carried forward to the three following tax years. Should there still be a remaining amount at the end of that period, it will be refunded to the enterprise. An immediate refund of the tax credit is applicable to SME as well as to innovative new enterprises. There is no possibility to carry the tax credit backward.

Application process

To benefit from the R&D tax credit, businesses must file a special tax return, in electronic format, so as. In the event an enterprise has spent more than EUR 100 million of R&D expenditures, it is required to fulfill additional reporting obligations. Namely, to provide a description of ongoing R&D activities' nature, status, dedicated assets and personnel etc.

In the event an enterprise has spent between EUR 10 million and EUR 100 million of R&D expenditures, it is required to provide information concerning the number of PhDs funded or hired because of those very expenditures, the global number of full-time research employees and their respective average salary.

Other aspects

In order to control whether the expenses taken into account in the computation of the R&D tax credit have been effectively allocated to actual research activities, experts of the ministry of higher education, research and innovation are entitled to ask the enterprise for justification. In this case, the company must reply within a 30-day timeframe, which can be prolonged under certain conditions.

The audit can also be performed on site upon request from the agent, notably but not limited to access accounting documents, proceed to fact-finding, or lead technical inspection.

Where the enterprise (i) has not answered the questions addressed to it, (ii) has not transferred any pieces of justification, or (iii) has obstructed the agents' control in case of an on-site inspection, the agents conclude the correlation between the expenses incurred and the research activities is not established.

In case of a tax audit, should a disagreement between the enterprise and the Tax Authorities arise as to the correlation between expenses used for the computation of the tax credit and research activities, an advisory committee can be summoned. It does only provide an opinion on the facts, not on law. It is also possible to refer to a mediator that can suggest, for instance, the intervention of another expert.

The upcoming Pillar Two regulations ensure that a minimum effective tax rate of 15% is met per jurisdiction. The R&D tax credit meets the characteristics of a qualified refundable tax credit within the meaning of Article 3 (38) of the EU Model rules[1]. However, the tax credit being a non-taxable item under French law, it will impact the effective tax rate.

There is no special measure to avoid misuse of the R&D tax incentive schemes in French law. Be that as it may, anti-abuse measures such as GAAR (general anti-avoidance rules) or transfer pricing rules may help avoid misuse of the IP box regime.

Other R&D related incentives

Apart from the above, it is worthwhile to mention that:

(i) There are two other tax credits related to R&D activities, namely:

- The Innovation Tax Credit (Crédit d'impôt innovation), which is 30% of the expenses incurred for the design of new products, without implementing R&D work generating new scientific knowledge (which is eligible for the R&D tax credit). This Innovation Tax Credit is capped at EUR 120,000 of tax credit (EUR 400,000 of expenses), it is calculated as the R&D tax credit with a few exceptions but above all it is limited to SMEs.
- The tax credit for collaborative research. This is a 40% tax credit, which exists since 2022 and is limited to new research partnerships between a private company and one of the research and knowledge diffusion organizations listed by the Ministry of Higher Education, Research and

[1] COUNCIL DIRECTIVE (EU) 2022/2523 of 14 December 2022 on ensuring a global minimum level of taxation for multinational enterprise groups and large-scale domestic groups in the Union.

Innovation. These partnerships must provide for a sharing of the fruits of the research, particularly with regard to PIs.

(ii) There are also other tax credits whose scope is limited to more specific activities, namely the production of:

- Films
- audiovisual works
- video games

(iii) Finally, there is a multitude of subsidy schemes for R&D projects to finance projects. There are in France mainly 3 organizations managing subsidies:

- ADEME, the energy and environment agency, which offers grants dedicated to research projects whose vocation is energy saving or environmental performance. For example, grants are offered for projects to design tools that improve the recycling of plastics.
- BPI France, the public investment bank, offers grants mainly to SMEs as well as calls for projects for collaborative projects between at least one large group, an SME and a public research organization.
- The 13 French regions have ERDF funds, some of which are dedicated to R&D on targeted themes such as health, energy and the environment, and digital technology.

Germany

Country introduction and overview

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Germany is one of the world's leading countries in research and development. Germany offers innovative companies financial support for research and development. The comprehensive and efficient funding landscape consists of a large number of funding instruments and programs at federal and state level.

Direct project funding for research and development is one of the most significant forms of R&D funding in terms of amount and is provided at the national level by both the federal government and the states. Direct project funding at the federal and state level is generally accessible to large and small and medium-sized companies. Depending on the funding program, project funding can be provided to individual companies as stand-alone projects but there might also be a requirement that the project is carried out jointly with other partners e.g. other companies, universities, research institutes (joint or cooperative projects).

The introduction of the R&D tax credit ("Forschungszulage") in 2020 by the Forschungszulagengesetz (FZulG)[1] added an additional funding instrument to the German funding landscape.

Innovation/Patent Box

Germany tax law does not provide any kind of such a tax incentive.

R&D tax credit

Entitlement

trade business, agriculture and forestry or self-employment are principally entitled to apply for the R&D tax credit. In case of a partnership, the tax credit can be applied by the partnership but not at the level of the partners. Because the General Block Exemption regulation (GBER)[2] is applicable to the German R&D tax credit companies in difficulties and companies under the obligation to repay state aids are not eligible to apply for the tax credit.

R&D projects are eligible if they started after 1 January 2020 (commencement date of the Research Allowance Act).

The R&D projects have to be classified within one of the beneficiary R&D categories which are:

- Basic research
- Industrial research
- Experimental development

Activities aimed at market research and development and activities to be considered part of the market launch as well as activities regarding the mass production without generating additional innovations or knowledge are excluded of the beneficiary categories and therefore not eligible.

Ownership conditions

The registration and ownership of the intellectual property is not of relevance for claiming the R&D tax credit. However, see below the comments to contract research.

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[1] Gesetz zur steuerlichen Förderung von Forschung und Entwicklung dated 14 December 2019 Federal Gazette BGBl. I p. 2763.
[2] Commission Regulation (EU) No 651/2014 of 17 June 2014 with several amendments.

Development and management conditions

Projects can be carried out as:

- in-house projects;
- contract research projects;
- cooperative projects;
- or in combination of the three alternatives above.

In case of contract research, the principal subject to income tax in Germany is entitled to apply for the R&D tax credit but not the contractor. If the contractor is a foreign company its place of management has to be in the European Union (EU) or in another state to which the Agreement on the European Economic Area (EEA Agreement) applies. In addition, the other state must provide administrative assistance on the basis of a contractual obligation in accordance with the EU Administrative Assistance Act to the extent necessary to verify the eligibility requirements.

Contract research can be agreed between third parties and related parties[1]. Contract research will be identified by indications (between third parties) or by specific criteria to be met (among affiliated companies). Especially for cross border R&D arrangements between related parties the German tax authorities review whether the German party might be qualified as contractor under a contract research arrangement thus with the consequence that the German party would not be eligible for claiming the R&D tax credit. Ownership of the IP might become of relevance for this judgement.

If in a cooperation project a cooperative partner is a tax-exempt university or research institutions the expenses incurred by the taxpaying cooperative partner are considered only.

As the R&D tax credit application is subject to tax audit appropriate documentation have to be provided to project plans, calculation of the assessment basis, hourly documentations, service agreements and reports on the progress of the projects at the end of each financial year.

Quantifying the benefit

The assessment basis for the German R&D tax credit is capped at EUR 4 million[2] per financial year and consist of the company's eligible R&D expenditure which are:

- For in-house R&D: The personnel costs (wages subject to German wage tax and social security contributions) of the eligible entity`s own R&D employees that are performing the relevant R&D activities.
- For contract research: 60% of the remuneration paid to the contractor.

The allowance rate is 25% of the assessment basis which results in a maximum tax credit of EUR 1 million[3] per financial year. In the case of affiliated companies, the maximum assessment basis of EUR 4 million per financial year must be shared among all affiliated companies. The affiliated companies split the assessment base amongst themselves by making a corresponding declaration in the application for the tax credit.

The tax credit assessed for a year will be treated as an "income tax prepayment" of the fiscal year in which the assessment is issued. This "income tax prepayment" will be offset against income tax assessments issued for the first time in the same fiscal year. An exceeding amount will be refunded to the taxpayer. Companies in a loss situation will therefore benefit from the tax credit.

The R&D tax credit may in principle be provided in addition to other funding or state aid for the beneficiary research and development project. But eligible expenses may not be included in the assessment basis if they have been or will be funded under other grants or state aid. This exclusion of cumulation shall also apply if the other funding comes from European Union funds. Additionally, the corresponding regulations of the General Block Exemption regulation (GBER) must be respected. The maximum total amount of all subsidies for one project must therefore not exceed EUR 15 million.

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[1] Affiliated companies with domination influence according to Sec. 290 (2) to (4) HGB (German Commercial Code).

[2] Cap of EUR 2 million after 1 July 2026.

[3] EUR 0.5 million after 1 July 2026.

Application process

The application process consists of two steps that are closely linked:

- Application for a R&D certificate for each project at the certification authority "Bescheinigungsstelle Forschungszulage (BSFZ)"
- Application for the tax credit at the tax office at the end of each financial year

The BSFZ approves the basic eligibility of the R&D project by examining whether the project is to be considered within the beneficiary R&D categories (basic research, industrial research, experimental development). At this stage aside from the project description only preliminary data is needed.

The application at the tax office consists of the determination of personal and material eligibility and distinction between in-house R&D and contract R&D, the declaration on "companies in difficulty", SME classification and consideration of any cumulation with other funding sources and the determination of the assessment basis for the financial year.

Finally, not the certification authority but the tax office only analysis the personal and factual eligibility. Therefore, it is crucial to always pursue the application process for research allowance holistically and not only sequentially.

Other R&D related incentives

There is a large variety of funding programs offered by federal and regional institutions. Direct project funding is used to support specific research, innovation and technology projects of private companies for a limited period of time. Funding is provided primarily in technology fields or for innovation topics of particular importance to the economy. The focus of support for private companies is on projects in the R&D categories of industrial research and experimental development. For this purpose, the state grants companies primarily non-repayable subsidies, but also loans, state guarantees and equity-strengthening funds. The subsidy or financing of the R&D project is provided on a pro rata basis in accordance with the subsidy or financing rates specified in each case in compliance with European state aid law, and with the inclusion of a corresponding contribution by the company to the financing.

In the case of funding programs at the federal level (rarely also at the state level), direct project funding often takes place within the framework of time-limited calls for projects on specific content-related topics or technologies within larger topic and technology fields (top-down approach, since in this case the R&D topics are de facto specified to the applicants by the funding provider).

The Federal Government and the States often involve project management agencies (Federal Government) or development banks (States) in the implementation of direct project funding. These are public or private service providers that work for the respective federal and/or state ministries on the basis of a corresponding mandate (with or without entrustment).

In addition, direct project funding at federal and state level also includes funding programs that are primarily or exclusively aimed at small and medium-sized enterprises e.g. ZIM Central Innovation Program for SMEs as well as individual funding programs of the federal states for individual company project funding). SME exclusive funding programs also fund individual projects, but with a more ready or less narrow technological focus or, in some cases, with no technological restrictions (bottom-up principle or broad-based funding since the topics for funding can be determined by the applicants themselves within certain limits.

In principle, there is no legal entitlement to funding under direct project funding. However, to receive funding from direct project funding, the implementation of the project must not yet have begun. Since direct project rules for direct project funding must also be observed and the and that the funding must have an incentive effect, the application and approval is always required before the start of the project (in the case of certain funding programs, the funding provider may agree to an early start of the project after the application has been submitted, even before approval has been granted).

Sources for researching these programs are:

- Bundesministerium für Wirtschaft und Klimaschutz / Federal Ministry for Economic Affairs and Climate Action. Funding database Federal, State and EU (in German only) https://www.foerderdatenbank.de/FDB/DE/Foerderprogramme/foerderprogramme.html

- GTAI German Trade & Invest GmbH supported by Federal Ministry for Economic Affairs and Climate Action
  https://www.gtai.de/en/invest
  https://www.gtai.de/en/invest/investment-guide/incentive-programs
- Ministerium für Bildung und Forschung / Federal Ministry of Education and Research
  https://www.datenportal.bmbf.de/portal/en/research.html
- ZIM (Zentrales Innovationsprogramm Mittelstand) department of the Federal Ministry for Economic Affairs and Climate Action. Germany’s largest innovation program for small and medium – sized enterprises.
  https://www.zim.de/ZIM/Navigation/DE/Meta/Englisch/englisch.html

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Italy

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Country introduction and overview

The two main R&D incentives available in Italy are the following:

- the IP box regime, which provides for a super-deduction of 110% for CIT and Regional Tax purposes of the expenses incurred to create, develop, maintain, and protect eligible IPs.
- the R&D, Innovation and Design tax credit, ranging between 5% and 10% of the eligible expenses, to be used to offset tax payments due for CIT, Regional tax, VAT, WHT and Social and Security Contributions (SSC).

It is possible for an enterprise to cumulate the advantages provided by both regimes, however the cost base eligible for the purposes of the tax credit must be netted of the tax benefit arising from the patent box.

In case of merger/demerger, under certain conditions, the tax benefits remain in the hands of the resulting entity.

Innovation/Patent Box

With effect from 2021 Italy revised the previous Patent Box regime by shifting from a profit-based incentive to a cost-based incentive.

Entitlement

Qualifying taxpayers
The patent box is for the benefit of all enterprises and Italian PE of foreign companies producing business income in Italy, regardless of the operating sector and the size of the enterprise / company.

Qualifying IP
For the purposes of the patent box qualifying IPs are patents, software protected by copyrights, drawings, and models legally protected.

The patent box is implemented in compliance with the nexus approach and the OECD standards.

Ownership conditions

To apply the patent box the enterprises must qualify as “investor”. The status of investor is meet when the taxpayer complies with the four conditions below:

- Sustains the cost to create, develop, maintain, and protect the IP
- Assumes the technical and financial risks
- Owns the results of the eligible activities
- Owns the economic rights for the exploitation of the IP

Therefore, enterprises carrying out R&D, Innovation and Design activities for the benefit of other entities that are tax resident in Italy or abroad, are excluded from the tax credits, as they cannot qualify as investor.

Development and management conditions

Expenses incurred to create, develop, maintain, and protect IPs that were purchased from third parties are eligible for the patent box.

Patent box can be applicable in case of existing IPs. If the IP was already existent at the beginning of the subsidized year, it is possible to apply the extra-deduction only on the expenses of the period, otherwise in the year of the IP creation / registration it is possible to apply the so-called “recapture mechanism”, applying the extra-deduction on the eligible expenses of the period and the ones incurred in the eight tax periods before, provided that the expenses are strictly connected with the creation of the IP.

The recapture is applicable:

- For patents, in the year of release of the grant certificate.
- For software, in the year of the registration at the Italian public register (SIAE).
- For drawings and models, in the year of the registration at public registers or the year of the disclosure to the public for the first time.

The Italian taxpayers can commission the execution of the R&D, Innovation and Design activities to third parties based outside of Italy, provided the supplier is tax resident in a country that implemented with Italy an agreement for the exchange of information between tax authorities and provided that the Italian taxpayer meets the requirements to be considered investor.

Qualifying cost (eligible cost)

The old patent box regime in force until 2020 was based on an income exemption mechanism. For the new patent box regime implemented from 2021 income arising from the IPs is not yet relevant.

Qualifying expenses are the followings:

- expenses for personnel with an employment or self-employment relationship or other relationship other than subordinate work, directly employed in the performance of the relevant activities. For personnel expenses relating to persons with subordinate employment contracts, the remuneration, gross of withholdings, is relevant and social security and welfare contributions, including accruals for severance indemnities, additional monthly salaries, holidays and leave, relating to the hours or days spent in relevant activities carried out during the tax period, including any travel allowances paid to worker in the case of eligible activities carried out off site;
- depreciation rates, principal amount of finance lease fees, operating lease fees and other expenses relating to movable capital assets and intangible assets used in carrying out the eligible activities;
- expenses for consultancy services and equivalent services relating exclusively to the eligible activities;
- expenses for materials, supplies and other similar products used in the eligible activities;
- expenses related to the maintenance of rights on subsidized intangible assets, their renewal upon expiry, their protection, also in associated form, and those relating to counterfeiting prevention activities and the management of disputes aimed at protecting the same rights.

Quantifying the benefit

The costs for the R&D activities (incurred either directly by the Italian resident companies and PEs of non-resident entities or by outsourcing the R&D activities to universities or other research institutes or equivalent institutes) in relation to copyrighted software, patents, designs, and models can be recognized for tax purposes for an amount equal to 210% of the relevant expenditure for both corporate income tax (IRES *imposta sul reddito sulle società*) and regional production tax (IRAP i*mposta regionale sulle attività produttive)*. R&D costs incurred with related parties are not eligible. The election for the new Patent Box procedure lasts for five fiscal years, is irrevocable, and is renewable.

Standard rates are 24% for CIT (IRES) purposes and 3,9% for regional tax purposes (IRAP). Considered the 110% extra-deduction of the eligible costs, the patent box benefit is equal to 30.69% of the relevant cost base. The cost base must be calculated net of the tax credits and other subsidies.

The extra-deduction is utilized year by year. If after the extra-deduction the taxpayer is in a tax loss position, the tax loss can be carried forward in the following tax periods.

Application process

The patent box extra-deduction must be report in the tax returns for CIT and regional tax purposes to decrease to taxable base. To benefit from the penalty protection in case of tax audit / assessment, the taxpayer must prepare patent box supporting documentation compliant with the guidelines issued by the Revenue Agency.

Other aspects

The patent box regime is compliant with the state aid regulation.

The upcoming Pillar Two regulations ensure that a minimum effective tax rate of 15% is met per jurisdiction. Therefore, there might be a Pillar Two impact on taxpayers. This has to be further analyzed after the implementation of Pillar Two.

R&D tax credit

Entitlement

The tax credit is for the benefit of all enterprises and Italian PE of foreign companies producing business income in Italy, regardless of the operating sector and the size of the enterprise / company.

The tax credit is available for:

- Investments in R&D activities, compliant with the definitions of the OECD's Frascati Manual and the Communication of the EU Commission n. 198/2014, letters m), q) and j) of point 15 of
- paragraph 1.3.
- Investments in Innovation activities, compliant with the definitions of the OECD's Oslo Manual, aimed at the creation or the significant development of products, production processes and services.
- Investments in Design and Aesthetic ideation activities aimed at innovating in a way significant the company's products in terms of form and other non-technical or functional elements, such as, for example, the characteristics of the lines, of the outlines, of the colours, of the surface structure, ornaments. To these effects, for product means any industrial or handicraft object, including components of complex products, packaging, le presentations, graphic symbols and typographic characters**.**

Ownership conditions

To apply the tax credit the enterprises must qualify as "investor". For details see the section above in the patent box.

Development and management conditions

Italian taxpayers can commission the execution of the R&D, Innovation and Design activities to third parties based outside of Italy, provided the supplier is tax resident in a country that implemented with Italy an agreement for the exchange of information between tax authorities and provided that the Italian taxpayer meets the requirements to be considered investor.

As the Italian taxpayer must be considered the investor, the resulting IP must necessarily reside in Italy.

Quantifying the benefit

Qualifying expenses are the same eligible for the patent box (see section above). Only for the R&D activities, it is possible to include also the cost of acquisition of license and patent to further develop the existing knowledge.

The R&D tax credit is calculated as follows:

- R&D tax credit is equal to 10% of the eligible cost base, net of other contributions and the patent box tax benefit. The annual maximum amount, available until FY 2031, is EUR 5 million for each enterprise.
- Innovation and Design tax credit is equal to 10% for FY203 and 5% for FYs 2024 and 2025. Also in this case the eligible cost base must be net of other contributions and the patent box tax benefit. The annual maximum amount is EUR 2 million for each enterprise, increased to 4 million in case the activities are aimed at digital solution 4.0 or the ecological transition/ circular economy.

The tax credit must be split in three equal amount installments, to be used from the tax period following the one in which the eligible expenses were incurred. It may be carried forward.

Application process

To access the tax credits, taxpayer must prepare supporting documentation compliant with the guidelines issued by the competent Minister and the Revenue Agency. The accounting expenses must be certified by the accounting auditor in charge of the certification of the financial statement.

Other aspects

The tax credits are compliant with the state aid regulation and with the Commission Regulation (EU) 651/2014[1].

As for patent box, these implications will be further analyzed after the implementation of Pillar Two.

Other R&D related incentives

Tax credit for the pharma sector

To face the adverse effects of the pandemic, from 2021 to 2030, it is available also a specific R&D tax credit for pharma sector aimed at boosting the creation of new drugs and vaccines or at the development of the existing ones.

Such tax credit is equal to 20% of the relevant expenses, with a maximum of EUR 20 million per year for each enterprise.

Differently form the R&D tax credit available for the generality of the taxpayers, this credit is available also for enterprises that perform in Italy R&D activities commissioned by group companies, or third parties based outside of Italy.

Government funding cash grant

Further to the tax credits, there also other national measures (development contracts and innovation agreements) to be negotiated with the Minister or equivalent bodies, aimed at supporting R&D or Innovation programs, that provide cash grants for significant amounts.

To access these programs, taxpayers must file with the competent authority proposals and candidatures to access the regulated schemes and they have to report the eligible expenses incurred.

[1] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32014R0651&from=HR.

The Netherlands

Country introduction and overview

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The Netherlands has the following tax incentives to stimulate research and development:

- the Innovation Box; and
- the R&D tax credit called "WBSO".

The Innovation Box relates to the R&D tax credit. The R&D activities that qualify for the R&D tax credit form the basis to opt for the Innovation Box.

Innovation/Patent Box

Entitlement

Qualifying taxpayers
A distinction is made between "smaller taxpayers" (consolidated group turnover of less than EUR 50 million and R&D gross income from intangible assets of less than EUR 7.5 million per year) and "larger taxpayers" (consolidated group turnover of at least EUR 50 million or a gross income from intangible assets of at least EUR 7.5 million per year). For smaller taxpayers, a self-developed IP for which an R&D declaration has been granted to the taxpayer is sufficient.[1]

For larger taxpayers, in addition to the R&D declaration on the time and costs spent to develop the IP, one of the following requirements should be met (this is an exhaustive list):

- Their IP can be classified as software (as developed in WBSO ICT projects).
- A patent or a plant variety right has been granted to the taxpayer.
- An application for a patent or a plant variety right has been filed by the taxpayer.
- A license to trade and use certain non-chemical methods for crops protection has been granted to the taxpayer.
- A license to distribute medication for human or animal application within the EU has been issued to the taxpayer.
- A Supplementary Protection Certificate has been issued to the taxpayer by the Netherlands Patent Office.
- A registered utility model has been granted for the purpose of the protection of the innovation.[2]
- An exclusive license has been granted to the taxpayer for the use of one of the abovementioned IPs, in either a certain way, during a certain term or certain geographical area.[3]

In addition, certain innovations which by itself do not qualify as software or are not protected by a patent or a comparable right can, in some situations, still qualify for the innovation box provided they are connected to a self-developed intangible asset for which this does apply ('group of related intangible assets').

Qualifying IP
Only self-developed innovations, e.g. innovations developed by personnel at the payroll of the Dutch taxpayer and for whose work an R&D declaration has been obtained – designated with a more technical term as 'intangible assets' - can qualify for the innovation box. Purchased intangible assets therefore do not qualify for use of the innovation box. However, a purchased intangible asset that is developed further may well qualify if the continued development has resulted in a 'new' intangible asset.[4]

[1] Article 12ba, paragraph 1, sub a, Dutch CITA.
[2] Article 12ba, paragraph 1, sub b, Dutch CITA.
[3] Article 12ba, paragraph 4 Dutch CITA.
[4] https://taxsummaries.pwc.com/netherlands/corporate/taxes-on-corporate-income.

R&D tax credit (WBSO) as a key entry ticket
The R&D tax credit (WBSO) is the key entry ticket to the Innovation Box. Under the R&D tax credit (see next paragraph) certain R&D activities are performed. These R&D activities qualify for R&D that falls within the scope of the Innovation Box (so called 'S&O-verklaringen' or 'WBSO-beschikkingen'). In that way, the application of the R&D tax credit also facilitates applicability of the Innovation Box. It is even required to have a R&D-declaration (in Dutch: 'S&O-verklaring') which a taxpayer obtains for applying the R&D tax credit (WBSO). In addition to that, the R&D tax credit and the Innovation Box are yearly applicable alongside each other. Meaning that taxpayers can apply for both tax incentives, the R&D tax credit for wage tax benefits and the Innovation Box for corporate income tax benefits.

Ownership conditions

The IP doesn't have to be registered or owned locally; it is sufficient if an exclusive license has been granted to the taxpayer which meets the requirements aforementioned under *qualifying taxpayers*. It is necessary that the Dutch taxpayer is the economic owner of the patent or exclusive license.

Development and management conditions

Acquired IP only qualifies for the innovation box if it is further self-developed into a 'new' intangible asset under an approved R&D project. The innovation box is applicable to existing IP as long as the IP is self-developed, and the tax return of the concerning fiscal year is not yet finalized.

The R&D activities can be performed abroad provided that the gravity point of development takes place in the Netherlands under an approved R&D project and subject to the Nexus Approach (including 30% uplift). Note that, even though R&D activities performed abroad (up to 30%) does not frustrate the applicability of the Innovation Box, the Innovation Box benefit will decrease if more R&D is performed abroad.

Qualifying income (eligible income)

The types of income eligible are embedded income in turnover derived from finished product, royalty income and capital gains realized by the sale of the IP.

Quantifying the benefit

Companies must demonstrate their R&D activities to assess the actual amount of the profit that can be allocated to the innovation box. It is common practice that the amount of income that can be allocated to R&D (and thus the basis for the nexus calculation) is discussed with the tax Authorities and confirmed in a ruling. Often a pragmatic transfer pricing approach is used to determine what part of a taxpayers' income is attributable to the different routine and core functions carried out.

The calculation of the income is also subject to the modified nexus approach:

Qualifying IP income = (qualifying expenditures x 1.3 / overall expenditures) x IP income.

The qualifying expenditure is limited to the expenditure on in-house development activities – which are not subcontracted within the group – and expenditure on development activities subcontracted to third parties. In the context of the nexus approach the R&D expenditures of a foreign permanent establishment are considered to be 'in-house' R&D expenditures.

Under the innovation box incentive, eligible R&D income is taxed at 9% (as of 2021) instead of the statutory corporate income tax (CIT) rate of 25.8%. Losses are deductible at the statutory rate of 25.8%, but future profit will be taxed at 25.8% for the amount of the loss related to the R&D allocated to the innovation box.[1]

Any net operating losses (NOLs) can be carried back for one year (for CIT) and indefinitely carried forward subject to a maximum of EUR 1 million and 50% of the superior of EUR 1 million .

Application process

The innovation box is claimed in the corporate income tax return filed by the taxpayer. Rulings are usually concluded with the Dutch tax authorities for a period of five years, prior to filing the Innovation Box position in the corporate income tax return and can be applied retroactively as long as the tax assessment has not become final.

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[1] https://taxsummaries.pwc.com/netherlands/corporate/taxes-on-corporate-income.

Other aspects

The Dutch innovation box regime is aligned with the modified nexus approach as described in the OECD report on Action 5 and is considered as non-harmful by the EU Code of Conduct Group.[1]

The upcoming Pillar Two regulations ensure that a minimum effective tax rate of 15% is met per jurisdiction. Therefore, a taxpayer in the Netherlands should pay at least 15% corporate income tax on its taxable base. The effective tax rate of the Dutch Innovation Box is 9%, which could frustrate the Pillar Two regulations. Therefore, there might be a Pillar Two impact on taxpayers who use the Innovation Box. However, it is most likely that – on an overall basis – almost every (or even all) taxpayers will pay a minimum effective tax of 15% in the Netherlands, regardless of the application of the Innovation Box (since not all profit before tax qualifies for the lower tax rate within the Innovation Box regime).

R&D tax credit (WBSO)

In the Netherlands, the WBSO (Wet Bevordering Speur- en Ontwikkelingswerk) consists of a reduction of wage tax on qualifying wage costs. For other costs and expenses (such as for (raw) materials, prototype construction, investments in equipment) in an R&D project, taxpayers can calculate the amount of the tax credit by choosing one of two approaches: a fixed sum or actual costs and expenses. Eligibility is not limited to specific industries.

Entitlement

Every entrepreneur in the Netherlands planning to carry out R&D – apart from public knowledge institutes – is entitled to submit a claim for a R&D tax credit. The company may be of any size and be active in any business area.
Specific eligibility for each incentive requires employee performance of the following R&D activities:

- Technical scientific research. This concerns explanatory research that is technical in nature. ‘Technical’ refers to research in fields such as physics, chemistry, biotechnology, production technology, and information and communication technology. Scientific’ relates to the objective and results of the research, as well as to the way the research is designed and implemented. The objective of scientific research is to find an explanation for a phenomenon that cannot be derived from generally available knowledge. Scientific research must be designed and carried out in a structural and planned manner.
- Development of technically new (components of) physical products, physical production processes or software. The most important criterion to be met for development work is the element of technical innovation. Technical innovation requires the presence of a research element in the project or technical uncertainties or risks relating to the achievement of the required result.[2]

Ownership conditions

There are no ownership conditions, since the R&D tax credit applies to wage costs and other costs and expenses made for R&D. As the R&D tax credit (WBSO) is the key entry ticket to the Innovation Box and both can be applied simultaneously bear in mind that for the latter tax scheme ownership conditions do apply.

Development and management conditions

The R&D activities must take place inside the EU territory and by staff on a Dutch payroll. There is only one exception on this rule. That is for outsourced work. Outsourced work – being eligible for RTC - is described as work not being outsourced research but being essential for the R&D project itself. To enable outsourced activities being qualified as outsourced work, these activities should concern activities that are supportive to your own R&D. However, not being able to execute these yourself since you lack specific expertise or specific facilities to do so. Example: you have a (laboratory) test necessary for the R&D project carried out by a specialized company (third party). You then use the test results for your own research or development. Or you request a specialized company to construct a specific prototype. Related costs being defined and linked to out-sourced work are eligible for the R&D tax credit - no matter whether the contractor is established inside or outside the EU.

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[1] https://taxsummaries.pwc.com/netherlands/corporate/taxes-on-corporate-income
[2] WBSO manual 2023, page 9 – 13.

Sub-contracted research, however, is not eligible for the R&D tax credit. Sub-contracted research (or outsourced research) are activities that can be considered as R&D in itself and being outsourced by the applicant to a third party. These costs are excluded for the WBSO (R&D tax credit). Most relevant reason behind this is the fact that this third party is able to apply for the R&D tax credit for related R&D itself.

Finally, it is important to note that if the activities carried out by foreign entities or external parties take place under the supervision of the Dutch entity, the costs can only be eligible for WBSO when the activities serve a R&D-project based in the Netherlands.

Quantifying the benefit

When applying for the R&D tax credit there has to be made a choice between the fixed amount (fixed sum for R&D costs and expenditures based on the number of approved R&D hours) and actual R&D costs/expenditures.

Eligible expenses include any R&D costs (i.e., wage costs for R&D employees, other R&D-related costs, R&D investment expenses) and other expenses that are directly and technically related to the R&D projects. R&D-related costs and R&D investment expenses must exclusively support the performance of R&D related work and must be directly attributable to the R&D project (there needs to be a clear connection between the costs specified and executed R&D activities).

Concerning the other costs and expenses, under the fixed-sum approach, the amount is calculated by reference to the number of allocated R&D hours. The fixed-sum amount per calendar year is:

- EUR 10 per R&D hour for the first 1,800 R&D hours.
- EUR 4 per R&D hour for all R&D hours exceeding 1,800. Repayment is required in cases in which realized R&D hours and costs and expenses are less than forecasted.[1]

Under the actual costs and expenses approach, the amount is calculated on the basis of the estimated costs and expenses incurred by R&D work. Whether the fixed sum or actual costs and expenses approach is chosen, only those costs/expenses incurred as a result of carrying out "own R&D" (i.e., in-house) are eligible for the R&D tax credit.

Examples of such costs include specific equipment or instruments for R&D, specific equipment or instruments for the manufacturing of models, and trial batches or prototypes. Any specific software and computer equipment used for R&D also qualify. Investments in land are excluded.

Costs that are linked to activities performed under an R&D declaration include costs related to consumer goods, materials and raw materials; costs related to experiments, the production of trial batches, materials and parts regarding the manufacturing of prototypes by the taxpayer or by third parties; acquisition of licenses for specific software packages or information and communication technologies (ICT) tools; carrying out of measurements or testing of prototypes; and rental of equipment from third parties.

Eligible costs exclude costs with respect to wage costs other than those of salaried R&D staff, outsourced R&D, costs of hiring labor, financing costs, costs of acquiring or improving land, and costs forming a remuneration for the disposition of capital equipment for which the taxpayer was already awarded an R&D declaration.

The R&D tax credit is accumulated as follows:[2]

- The tax credit rate for eligible expenditure is 32% of outlays up to EUR 350,000 per year, and 16% over this limit.
- A start-up company is eligible for an R&D tax credit of 40% instead of the regular 32% on the first EUR 350,000 of total underlying R&D cost. An entity qualifies as a startup if it has employed personnel for a maximum of four out of the past five calendar years and has been issued the R&D tax credit for a maximum of two years.
- The standard hourly wage of EUR 29 applies for the first and second year a R&D tax claim is submitted and awarded. For the years thereafter the average salary of involved R&D personnel is the baseline for eligible wage costs (this calculation is renewed on a yearly basis).

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[1] WBSO manual 2023, page 17.
[2] https://taxsummaries.pwc.com/netherlands/corporate/tax-credits-and-incentives.

- The total underlying R&D costs & expenses are determined in two steps:
  - eligible R&D hours * R&D hourly rate (fixed amount of EUR 29 in the first two years); and
  - costs & expenses. The taxpayer needs to make a choice between either a lump sum approach or budgeted costs and expenses. The lump sum amount per calendar year is:
    - EUR 10 per R&D hour for the first 1800 R&D hours.
    - EUR 4 per R&D hour for all R&D hours above the first 1800.

Application process

The R&D tax credit has to be obtained in advance by filing a request with the Netherlands Enterprise Agency (Rijksdienst voor Ondernemend Nederland), a department within the Ministry of Economy and Climate. The application should be filed in advance. The application should be submitted ultimately the last day before the period in which the R&D work is going to take place. In the event that this period starts on 1 January, the latest commencement date is 20 December of the previous calendar year. Four applications may be filed per calendar year. These applications must cover a minimum period of 3 months and a maximum period of 12 months within the same calendar year. Please note that as of 2022 application periods may now overlap. For example, in case an application with the start month of January is submitted it is allowed to submit a new application with, for example, the start month of February or March. This allows you to respond in a more flexible way to specific developments within your company or related markets. The R&D tax credit for future activities can be claimed as long as the qualifying activities are performed.

After the incentive is granted, progress in terms of realized worked hours, costs and investment has to be administrated and filed at the agency after the financial year has ended. The obligation to retain the administrative records lasts for seven years after the end of the period covered by the Declaration.

The tax benefit can be set off in the tax return to the Dutch Tax and Customs Administration. The WBSO enables the R&D withholding agent to deduct a tax credit from the payroll tax for R&D-staff, thereby reducing the amount of payroll tax to be paid. The credit may be deducted solely from the payroll tax (wage tax and social insurance contributions). The credit may not be deducted from the employee insurance or healthcare insurance contributions. You may deduct the R&D withholding tax credit solely in tax periods that end during the calendar year to which the R&D Declaration relates.[1]

As of 2022 it is allowed to decide yourself how much of the granted WBSO benefit you want to include and in which tax return period you want to include it. Please note the entire amount can even be settled in one tax return period (if the amount of wage taxes is sufficient).

Other R&D related incentives

Private-public partnerships project allowance for research and innovation

The PPS is a partnership between public entities and private parties or investors. Cash grants of 40% are available on the private investment costs for the first EUR 20,000, and 30% for the excess. To receive funding for the PPS, the cash grant has to be invested in the R&D project of the partnership. Companies are required to seek preapproval to obtain PPS.[2]

SME Innovation Stimulus for Regional and Top Sectors (MIT)

The SME Innovation Stimulus for Regional and Top Sectors program (MIT in Dutch) is specifically aimed at stimulating innovation at small- and medium-sized companies in five different regions across the Netherlands. There are two grant options:

- Feasibility studies: Cash grant for studying the technical and financial feasibility of an intended innovation, up to 40% and EUR 20,000 per project[3];
- R&D collaboration projects: Cash grant for an R&D collaboration between at least two SMEs, up to 35% and EUR 350,000 per project[4].

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[1] WBSO manual 2023, page 39.
[2] https://english.rvo.nl/subsidies-programmes/ppp.
[3] https://www.rvo.nl/subsidies-financiering/mit/haalbaarheidsprojecten.
[4] https://www.rvo.nl/subsidies-financiering/mit/rd-samenwerking.

European Regional Development Fund (ERDF)

The European Regional Development Fund (ERDF) is intended to reduce major economic differences between regions. There are four EFRD programs in the Netherlands that offer subsidies for innovation, development, and cooperation. Available grants vary by region, project type, and arrangement, but typically range from 25-60%, with a maximum grant amount of EUR 5 million.[1]

Subsidy Mission-driven Research, Development, and Innovation (MOOI)

The MOOI program provides cash grants for large-scale innovation projects focused on electricity, the built environment and industry. Projects must contribute to the climate goals and must involve at least 3 companies across the value chain. Research institutes can also participate. The maximum grant is EUR 4 million per project (EUR 7 million for the built environment), of which at least EUR 25,000 per participant. The grant percentage varies between 40-80% of the total eligible costs.[2]

Renewable Energy Transition (HER+)

The Renewable Energy Transition (HER+) program is intended for innovative projects that will help to reduce CO_2-emissions in 2030 and result in saving on future expenditure on subsidies. Only partnerships with at least one entrepreneur can apply. The HER+ cash grant varies between 25-80% of total eligible costs, up to a maximum of EUR 6 million per project.[3]

TSE Industry Studies

The TSE Industry Studies program provides industrial parties with a cash grant to study the feasibility of an innovative pilot or demonstration project, aimed at CO_2-reduction. The grant amounts to 70% of the total project costs up to a maximum of EUR 500,000 per project. SMEs as well as large companies can apply.[4]

TSE Industry Research & Development tender

The TSE Industry Research & Development tender is for entrepreneurs in industry who research and develop cheaper, carbon neutral circular products and services. Only consortia with at least one entrepreneur can apply. The cash grant varies between 25-80%, up to a maximum of EUR 500,000 per project.[5]

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[1] https://www.rijksoverheid.nl/onderwerpen/europese-subsidies/europese-structuur--en-investeringsfondsen/europees-fonds-voor-regionale-ontwikkeling-efro.
[2] https://business.gov.nl/subsidy/subsidy-mission-driven-research-development-and-innovation-mooi/.
[3] https://business.gov.nl/subsidy/renewable-energy-transition/.
[4] https://www.rvo.nl/subsidies-financiering/tse-industrie-studies.
[5] https://www.rvo.nl/subsidies-financiering/oeno.

Spain

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Country introduction and overview

Among OECD nations and partner economies, Spain provides one of the most generous R&D tax incentive schemes. The country's average corporate tax rate within the Eurozone is moderate (25%) and incentives and tax exemptions can reduce the effective tax rate to around 20%.

The regulatory framework established by the Law 27/2014, of 27 November, on Corporate Income Tax[1] and the Science, Technology, and Innovation Law 14/2011[2], of 1 June 2011, establishes the legal basis for the fostering of scientific and technical research, experimental development and innovation in Spain, founded on a scheme based on the approval of the related Spanish Strategies for Science, Technology and for Innovation[3].

The following tax incentives stimulate research and development:

- The Patent Box
- The tax credits for R&D and Innovations (R&D&I)
- The partial exemption on employers' social security contributions (SSC)
- The Accelerated depreciation for R&D capital

Innovation/Patent Box

Entitlement

Qualifying taxpayers
The patent box basically gives tax incentives to companies developing intangible property. Firms from all industries that are incorporated in Spain (or a permanent establishment) and subject to Corporation Tax in Spain are eligible.

The tax benefit is applicable when the company that generated the asset transfers or licenses it to another entity, so that the latter uses it to develop an economic activity.

Qualifying IP
Intangibles to which the tax incentive applies are the following:

- Patents.
- Utility models.
- Supplementary protection certificates for medical purposes and phytosanitary products
- Legally protected models and designs.
- Registered software that results from R&D projects.

Blueprints, formulas, trade secrets, and industrial, commercial, or scientific know-how do not qualify for the regime. Under no circumstances may the income resulting from the license of the following assets benefit from the tax reduction: trademarks; literary, artistic or scientific work, including cinematographic films; image rights; software and industrial, commercial or scientific equipment.

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[1] Ley 27/2014, de 27 de noviembre, del Impuesto sobre Sociedades; https://www.global-regulation.com/translation/spain/1447828/law-27-2014-november-27%252c-from-corporate-income-tax.html.
[2] Ley 14/2011, de 1 de junio, de la Ciencia, la Tecnología y la Innovación; https://www.global-regulation.com/translation/spain/1437072/law-14-2011%252c-from-june-1%252c-the-science%252c-technology-and-innovation.html.
[3] The Spanish Science, Technology and Innovation Strategy (EECTI) is the multi-annual reference framework for promoting scientific, technical and innovation research, which establishes the objectives shared by all Public Administrations; https://www.ciencia.gob.es/en/Estrategias-y-Planes/Estrategias.html.

Ownership conditions

The tax benefit is applicable when the company that generated the asset transfers or licenses it to another entity, so that the latter uses it to develop an economic activity. The taxpayer must own qualifying IP or must have an exclusive right of use.

Development and management conditions

The Patent Box incentive is only applicable by a taxpayer that has totally or partially created the intangible asset. Although there is not a minimum percentage required as to the intangible's creation, the Spanish tax authorities fully disregard the application of this exemption if the taxpayer has not created it in any proportion.

The Patent Box incentive allows companies to reduce the taxable income from the transfer or transfer of the right to use or exploit certain intangible assets by up to 60%. For the application of the reduction, the following requirements must be met:

- The assignee must use the rights of use or exploitation in the development of an economic activity and the results of this use shall not materialise in the delivery of goods or services by the assignee that generate tax deductible expenses in the entity assignor, provided that, the latter entity is related to the assignee.
- The assignee must not reside in a country or territory with zero taxation or classified as a tax haven, unless it is located in a Member State of the European Union and the taxpayer proves that it carries out economic activities and that the operation responds to valid economic reasons
- When the same assignment contract includes ancillary services of goods or services, the considerations corresponding to those goods or services must be differentiated in the contract.
- The entity must keep the necessary accounting records to be able to determine each of the direct income and expenses corresponding to the assets subject to assignment.

Qualifying income (eligible income)

The range of intangible assets that qualify for patent box is limited by law and related to the income from the Intangibles to which the tax incentive applies.

In addition, the reduction also applies in case of transfer of the intangible assets but limited to transactions with non-related parties.

The tax benefit is applicable when the company that generated the asset transfers or licenses it to another entity, so that the latter uses it to develop an economic activity.

Quantifying the benefit

The profit subject to the exemption is calculated taking into account qualifying income derived from the intangible asset, less costs related to the creation of the intangible, provided the costs have not been capitalised and amortised or otherwise deducted when calculating taxable income.

The patent box regime has been amended to comply with the rules set by the OECD "nexus approach." Under the revised rules, a ratio is applied to determine qualifying income, which may limit or eliminate the benefits available under the patent box in situations where the taxpayer has not created the relevant intangible asset (through its own resources or through subcontracting work to unrelated third parties).

The ratio is the lower of 1 or the result of applying the following formula: 130% of expenses (other than financing expenses and depreciation of buildings) incurred by the taxpayer that are directly connected to the creation or development of the relevant intangible asset, including expenses incurred as a result of outsourcing to unrelated third parties; divided by 100% of expenses (other than financing expenses and depreciation of buildings) incurred by the taxpayer that are directly connected to the creation or development of the relevant intangible asset, including expenses incurred as a result of outsourcing and expenses incurred for the acquisition of the intangible asset.

The tax exemption is the result of multiplying the ratio described above by 60%. Therefore, if the ratio is 1, there is a full 60% tax exemption; if the ratio is lower than 1, the exemption is reduced accordingly.

Negative income obtained in a tax period is also subject to reduction if positive income of the same nature was obtained in previous tax periods to which the reduction has been applied. Where the taxpayer benefited from the patent box regime in previous years, the tax computation of negative results (i.e., losses determined on the basis of expenses linked to qualifying assets) incurred in the current year is limited as follows:

- The loss will be reduced by the applicable percentage to determine the patent box incentive if a positive result were obtained.
- This restriction on the computation of losses will apply up to the amount of positive results derived in previous years that benefited from the patent box incentive. Once this amount is exceeded, the additional loss may be computed without limitation for the purpose of calculating the corporate income tax liability and should be taken into account in offsetting future qualifying profits that benefit from the patent box regime.

Application process

For the purposes of applying the Patent Box reduction, prior to carrying out the operations, the taxpayer may request the Tax Administration to adopt a prior valuation agreement in relation to the income from the transfer of assets and expenses associated, as well as the income generated in the transmission.

The request will be accompanied by a valuation proposal, which will be based on the market value.

Other aspects

Spanish Patent Box is compatible with other grant and tax deductions for R&D.

Tax measures pursuing general economic policy objectives available to all companies on an equal access basis, such as the Spanish Patent Box regime, do not qualify as state aid. Instead, they are considered general measures.

Spain's involvement and participation in the works resulting from the OECD inclusive framework, aimed at establishing the Global Anti-Base Erosion (GloBE) and the Undertaxed Payments Rule (UTPR), has resulted in the implementation of a minimum taxation level for large Multinational Enterprises (MNE).

In this respect, effective from 2022, Spain has introduced a minimum Corporate Income Tax payment of 15% of the tax base for the following taxpayers:

- those whose net revenues are at least EUR 20 million in the 12-month period immediately preceding the start date of the taxable period; or
- those who are taxed under the consolidated tax group regime, irrespective of their net revenues figure.

This restriction states that the net tax liability (tax liability less tax credits) cannot be less than 15% of the taxable base after (i) the offsetting of tax losses, (ii) the reduction for the levelling reserve for reduced-sized companies and (iii) the investment reserve for the Canary Islands.

The Spanish tax authorities have improved and increased the exchange of information between different public entities both at a national and an international level. In addition, there has been a relevant improvement regarding their tools to verify the tax compliance of the taxpayers.

R&D&I tax credit

R&D&I stands for research and development activities and for technical innovation activities.

Entitlement

Firms from all industries that are incorporated in Spain (or a permanent establishment) are eligible as long as the qualifying R&D investments take place in Spain, in a EU/EEA Member State. All industries (except foundations) are eligible for R&D&I tax deductions for costs incurred in qualifying activities.

The qualifying activities have their regulatory framework in the the Corporate Income Tax Law 27/2014, of November 27, the income tax Chapter IV, Article 35, that sets out the measures regulating tax deductions for R&D and technological innovation, as well as rules on the application of Article 39.

Article 35.1.a) Concept of research and development.
R&D activities include original planned investigation aimed at acquiring new knowledge and greater understanding in scientific or technological fields. Development is considered to be the application of the results of research or of any other kind of scientific knowledge for the manufacture of new materials or products or for the design of new production processes or methods, as well as for the substantial technological improvement of materials, products, processes, or existing methods.

Article 35.2.a) Concept of technological innovation.
Technological innovation (I) activities are those whose result is a technological advance in the production of new products or production processes or substantial improvements of the existing ones. Advanced software activities qualify for research tax credits and generally are limited to developments that are innovative (e.g., pilot projects related to animations developed for video games).

Activities that do not involve a significant scientific or technological innovation will not be considered as R&D&I activities. Thus, industrial production activities and the provision of services or the distribution of goods and services and exploration, drilling or prospecting for minerals and hydrocarbons are not subject of these tax incentives.

The requirements for the exclusion of R&D and technological innovation tax credits from the tax credit limits are as follows:

- One tax period has passed since the tax credit was generated and the tax credit has not been applied.
- An amount equal to the tax credit applied or paid has been allocated to R&D and technological innovation expenses or to investments in tangible fixed assets or intangible assets used exclusively for R&D and technological innovation activities, excluding real property, within 24 months of the end of the tax period when the tax credit was applied or paid.
- The taxpayer's average number of staff (staff in general or staff assigned to R&D and technological innovation activities) has not decreased between the end of the tax period when the tax credit was generated and the end of the reinvestment period.
- The taxpayer has a report that certifies that the activities are R&D and technological innovation activities or it has made an advance agreement with the Spanish tax authorities regarding the valuation of the expenses and investments of the project.

The following should also be taken into consideration:

- The tax credit applied or paid for technological innovation in accordance with the foregoing comments may not exceed a total of EUR 1 million per year.
- The sum of the tax credit applied or paid for technological innovation and the tax credit applied or paid for R&D innovation in accordance with the foregoing comments may not exceed a total of EUR 3 million per year.
- If R&D expenses for the year exceed 10% of turnover, an additional amount of EUR 2 million per year of tax credit for R&D can be applied or paid without limitation and with a 20% discount.

Ownership conditions

The taxpayer must have paid for the R&D activities either in-house or to a subcontractor. IP ownership does not affect whether the taxpayer can claim the tax credit.

Development and management conditions

Qualifying expenses incurred by the taxpayer must be directly related and effectively applied to the realisation of R&D&I activities and must be itemised by project.

Eligible R&D&I expenses for the credit may correspond to activities carried out in Spain or in any Member State of the European Union or the European Economic Area. In turn, amounts paid for carrying out such activities in Spain or in any EU/EEA member state on behalf of the taxpayer, whether alone or together with others, shall be considered as R&D&I eligible expenses. The R&D&I deduction is compatible with direct aid (grants and financial instruments) as well as indirect aid (social security rebates).

The funder can claim tax relief, as the subcontracted R&D is one of the costs of the project. R&D expenditure if paid for by a third-party does not qualify for the R&I tax credit.

Quantifying the benefit

Spain offers immediate deduction of qualified R&D&I expenditures, established as a percentage of the expenses incurred by a company in R&D&I activities. These expenses, which are deductible in the company's profit and loss account, will entitle the company to an additional tax deduction. This mechanism incentivises certain activities, as the results derived from them have an impact not only on the company that carries them out, but also on society as a whole.

<table>
<tr><th colspan="2"></th><th colspan="2">Tax deductions for R&D</th><th>Tax deductions for Technological Innovation</th></tr>
<tr><td colspan="2">Tax incentive</td><td colspan="2">Tax credit</td><td>Tax credit</td></tr>
<tr><td colspan="2">Type of instrument</td><td colspan="2">Hybrid (volume-based and incremental)</td><td>Volume-based</td></tr>
<tr><td colspan="2">Eligible expenditures</td><td colspan="2">Directly related to the activities carried out until the creation of the first prototype: Labour, Subcontractors, Machinery and equipment depreciation, Intangible’s depreciation, Consumables, Other expenses</td><td>Directly related to the activities: Labour, Subcontractors, Machinery and equipment depreciation, Intangible’s depreciation, Consumables, Other expenses</td></tr>
<tr><td colspan="2">Headline rates (%)</td><td>25%
+17% (R&D staff)
+ 8% (ME & Intangibles)</td><td>Increment (on top of volume) 17% on excess over last two-year average expense</td><td>12%</td></tr>
<tr><td colspan="2">Refund</td><td colspan="2">One year after the tax credit was generated (optional at 20% discount)</td><td>One year after the tax credit was generated (optional at 20% discount)</td></tr>
<tr><td colspan="2">Carry-over (years)</td><td colspan="2">18 (carry-forward)</td><td>18 (carry-forward)</td></tr>
<tr><td>Threshold</td><td>Base amount</td><td colspan="2">Average R&D expenditure in the preceding two years</td><td>Technological innovation expenditure</td></tr>
<tr><td rowspan="2">Ceilings</td><td>Tax relief</td><td colspan="2">25% of gross tax liability if the tax relief for R&D equals or is less than 10% of the tax due; else the cap is increased to 50% of the gross tax due</td><td>25% of gross tax liability if the tax relief for technological innovation equals or is less than 10% of the tax due; else the cap is increased to 50% of the gross tax due</td></tr>
<tr><td>Refund-specific</td><td colspan="2">EUR 3 million; raised to EUR 5 million when R&D expenses exceed 10% of turnover</td><td>EUR 1 million</td></tr>
</table>

Figure 1. Main design features of R&D&I tax incentives in Spain

The base of the deduction will be constituted by the amount of the research and development expenses and, where appropriate, by the investments in elements of tangible and intangible assets excluding buildings and land.

- A 25% tax credit can be availed of for expenses incurred from R&D activities. If the expenses are higher than the average R&D expenses incurred by the company during the previous two years, the tax credit is 42% for the excess amount.
- An additional tax credit of 17% can be availed of for staff expenses incurred for staff exclusively carrying out and qualified to carry out R&D activities.
- An 8% tax credit can be availed of for investments made in tangible fixed assets (excluding buildings) and intangible assets that are exclusively assigned to R&D activities.
- A 12% tax credit can be availed of for technological innovation activities.
- With effect for tax years starting in 2020 and 2021, the 12% percentage of deduction will be increased by 38 points for expenses incurred by small and medium-sized enterprises in projects starting after 25 June 2020 that involve the implementation of technological innovation activities whose result is a technological advance in obtaining new production procedures in the value chain of the automotive industry or substantial improvements of the already existing production procedures. Entities that do not qualify as small and medium-sized may benefit from an increase of 3% if they collaborate with small and medium-sized enterprises according to the conditions legally set.

The Autonomous Communities of the Basque Country and Navarre offer additional R&D&I tax incentives. The headline tax credit rate in the Basque Country is 30% (50% incremental) and 40% (42% incremental) in Navarre. In the Basque Country, the rate goes up to 50% in the case of R&D subcontracted to universities or accredited research and technology organisation.

The basis of the deduction will be reduced by the amount of subsidies received for the promotion of such activities if they are attributable as income in the tax period.

If the amount of qualifying R&D&I expenses for the tax year exceeds 10% of the tax due (after reducing the deductions to prevent double taxation and bonuses from other incentives), the tax credits may not be used to offset more than 50% of the gross amount of tax due. If the amount of R&D&I expenses does not exceed 10% of the tax due (after reducing the deductions to avoid double taxation and bonuses), the credits may offset up to 25% of the gross amount of tax due.

Cash refund limits to an entire group of companies shall apply in the case of entities in the same group according to the criteria set out in Article 42 of the Spanish Commercial Code[1], regardless of their residence and the obligation to prepare consolidated financial statements. Unused credits may be carried forward for 18 years and the Spanish tax authorities will have 10 years to review tax credits that have been generated but not utilised.

R&D&I tax credits can be excluded from the limits on tax credits applied on tax liabilities, which will have a cost of 20% of the tax credits applied, meaning that, if certain requirements are met, 80% of R&D&I tax credits may reduce tax liability after double tax deductions and tax allowances to zero, and any excess tax credits (up to 80%) may be refunded by the tax authorities. Costs for land and buildings and supplies and indirect expenses are excluded. A pre-assessment of qualifying R&D&I expenses is in place under the R&D&I tax deductions scheme.

Application process

Qualified R&D&I expenditures can be directly applied by the taxpayer in the corporate income tax declaration as a percentage of the expenses incurred by a company in R&D&I activities. Nevertheless, the taxpayer may request a motivated report which confirms or denies the R&D or technological nature of the expenses and investments carried out. This report will be binding for the Tax Administration.

The application must be filed with income tax return 25 days following the six months period from the taxpayer's financial year-end. As general rule, the request for a report should be sent with a technical analysis issued by an official certifying entity. The authorities have three months to issue the report; however, the expiry of the term has no effects for the authorities or the taxpayer.

Likewise, the taxpayer may request the tax authorities to adopt prior valuation agreements for expenses and investments corresponding to research and development or technological innovation projects. The pre-agreed valuation report should be requested prior to the project commencement and the tax authorities have six months to respond. Expiry of the term without tax authority response implies that the tax authorities accept the taxpayer’s proposal

In addition, taxpayers may submit queries on the interpretation and application of this deduction, the answer to which will be binding for the tax authorities, in accordance with the terms set out in Articles 88 and 89 of the General Tax Law. Entities that cannot apply the tax deductions (because of insufficient tax liability or because they have exceeded the joint limit) may request the Tax Administration to payback the amounts deductible for R&D&I activities with a 20% discount.

The taxpayer may provide a reasoned report issued by the Ministry of Economy, Industry and Competitiveness (currently the Ministry of Science and Innovation), or by a body attached to the same, on compliance with the scientific and technological requirements stipulated in letter a) of Article 35.1 of the LIS for research and development expenditure, and in letter a) of Article 35.2 of the same Law for technological innovation expenditure, taking into account in both cases the provisions of Article 35.3 of the LIS. This report, issued under the terms established in Royal Decree 1432/2003, of 21 November (BOE of 29 November), will be binding for the Tax Administration.

Other aspects

Tax measures pursuing general economic policy objectives available to all companies on an equal access basis, such as the Spanish R&D&I tax credit do not qualify as state aid. Instead, they are considered general measures.

Spain's involvement and participation in the works resulting from the OECD inclusive framework, aimed at establishing the Global Anti-Base Erosion (GloBE) and the Undertaxed Payments Rule (UTPR), has resulted in the implementation of a minimum taxation level for large Multinational Enterprises (MNE).

In this respect, effective from 2022, Spain has introduced a minimum Corporate Income Tax payment of 15% of the tax base for the following taxpayers:

- those whose net revenues are at least EUR 20 million in the 12-month period immediately preceding the start date of the taxable period; or
- those who are taxed under the consolidated tax group regime, irrespective of their net revenues figure.

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[1] Real Decreto de 22 de agosto de 1885 por el que se publica el Código de Comercio; https://www.mjusticia.gob.es/es/AreaTematica/DocumentacionPublicaciones/Documents/Code_of_Comerce_%28Codigo_de_Comercio%29.PDF.

This restriction states that the net tax liability (tax liability less tax credits) cannot be less than 15% of the taxable base after (i) the offsetting of tax losses, (ii) the reduction for the levelling reserve for reduced-sized companies and (iii) the investment reserve for the Canary Islands.

In practice, this minimum payment means that large taxpayers won't be able to use certain deductions to lower their net tax liability below this amount; essentially, this will affect how the tax credits for R&D&I or the tax credits for gifts to non-profit organisations are applied.

In any case, tax credits that cannot be used due to this restriction will be usable in later tax seasons as long as they adhere to the same limitations as before.

Tax incentives to promote business in particular regions, such as Ceuta, Melilla and the Canary Islands, are excluded from the scope of this measure and will continue to apply as before.

The Spanish tax authorities have improved and increased the exchange of information between different public entities both at a national and an international level. In addition, there has been a relevant improvement regarding their tools to verify the tax compliance of the taxpayers.

Other R&D related incentives

Social security exemptions (SSC)

The Royal Decree 475/2014[1], of June 13, introduced a system of bonuses in the corporate share of the Social Security contribution for the research personnel assigned exclusively to R&D&I activities.

This non-tax incentive, linked to the hiring and maintenance o full-time employment for R&D&I activities, establishes a bonus up to 40% for business contributions to the Social Security regarding the research staff and foresees a full compatibility of this incentive with tax deductions for R&D&I in the case of “innovative SMEs”[2]. For the rest of organisations, this compatibility can exist as long as both incentives are not applied on the same researcher.

Accelerated depreciation for R&D capital

Accelerated depreciation is a tax-reduction strategy in which a capital asset reduces its book value at a faster rate than it would using traditional depreciation methods such as the straight-line method. Therefore, under accelerated depreciation, R&D capital faces greater deductions in its value in the earlier years than in the later years.

All investment costs related to R&D activities capitalised as intangible assets (and net of amortisation) are eligible, regardless of the source of funding of these activities. Qualifying R&D expenditures include investment cost on property, plant and equipment and intangible assets (excluding buildings) pertain to the activities of research and development. Buildings will be amortised linearly over a period of 10 years in the part related with research and development activities.

As a general rule, the amount of tax-deductible depreciation shall be the amount obtained by applying to the depreciable value a coefficient resulting from multiplying by 2 the maximum straight-line depreciation

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[1] Real Decreto 475/2014, de 13 de junio, sobre bonificaciones en la cotización a la Seguridad Social del personal investigador; https://www.global-regulation.com/translation/spain/1452557/royal-decree-475-2014%252c-13-june%252c-about-bonuses-in-the-sta-of-social-security-contributions.html.

[2] "Innovative SMEs" are those considered as R&D&I intensive if one of the following circumstances applies:

(i) the company has received public funding in the last three years, without undergoing revocation due to an incorrect or insufficient implementation of the funded activity, through public calls under the a. Sixth National Plan for Scientific Research, Development and Technological Innovation Plan or b. the State Scientific and Technical Research and Innovation Support for the realisation of R&D&I, c. the Center for Industrial Technological Development and d. the 7th Framework Programme for R&D&I of the Horizon 2020 Programme of the European Union.

(ii) it has demonstrated its innovative nature through their own activity by a. having a patent itself in operation over a period not exceeding five years preceding the exercise of application to the deduction; b. having obtained in the three years prior to the application for the deduction a reasoned binding and positive report allowing the company to apply for the deduction.

(iii) it has demonstrated its capacity for innovation, through one of the following recognised certifications recognised by the Ministry of Economy and Competitiveness: a. Young Innovative Company (JEI), according to the specification AENOR EA0043; b. Innovative small or micro enterprise according to specification AENOR EA0047; c. Certification according to the UNE 166.002 "Management Systems R&D&I". These SMEs are recognised as such by the official seal of "innovative SMEs" and appear in the Register managed by the Ministry of Economy and Competitiveness.

coefficient provided for in the officially approved depreciation tables set out in Article 12.1 (a) of the Spanish Corporate Income Tax Law.

The accelerated depreciation is compatible with other tax incentives and deductions for R&D&I activities.

Cash grants

There are several funding programs offered by national and regional institutions also in connection with European programs. This funding mainly consists in non-repayable cash grants for wages, assets and consumable materials.

Grants for R&D&I activities are available from the federal government and the 17 autonomous communities. They are often focused on certain industries or outcomes and can pay up to 40% of eligible project costs for small and medium-sized businesses (SMEs) and 25% for large corporations. The most noteworthy funding National authorities are the following:

Centro para el Desarrollo Tecnológico y la Innovación (CDTI) / Centre for the Development of Industrial Technology
https://www.cdti.es/index.asp?MP=100&MS=898&MN=1 (in Spanish only)

Instituto para la Diversificación y ahorro de la Energía (IDAE) / Institute for the Diversification and Saving of Energy
https://www.idae.es/en/home

Empresa Nacional de Innovación (ENISA) / National Innovation Company
https://www.enisa.es/en

Special tax regime of the Canary Islands

Due to the remoteness of the Canary Islands, they have traditionally enjoyed a special economic and tax regime with specific economic and tax measures different to those established for the rest of Spain. As a result, they have one of the most advantageous tax regimes in Europe which, in addition, is not affected by the minimum effective tax rate established in the rest of Spain (amounting to 15% of profit). Consequently, the tax incentives can very easily reduce the effective tax rate to around 4% or even less of profit.

Regarding R&D&I tax credits, the Canary Island economic and tax regime establishes the following tax benefits for companies and businesses domiciled in the Canary Islands or with a PE in the Canary Islands:

- A 45% tax credit can be availed of for expenses incurred from R&D activities. If the expenses are higher than the average R&D expenses incurred by the company during the previous two years, the tax credit is 30.6% for the excess amount.
- An additional tax credit of 37% can be availed of for staff expenses incurred for staff exclusively carrying out and qualified to carry out R&D activities.
- An 28% tax credit can be availed of for investments made in tangible fixed assets (excluding buildings) and intangible assets that are exclusively assigned to R&D activities.
- A 45% tax credit can be availed of for technological innovation activities.

If the amount of qualifying R&D&I expenses for the tax year exceeds 10% of the tax due (after reducing the deductions to prevent double taxation and bonuses from other incentives), the tax credits may not be used to offset more than 90% of the gross amount of tax due. If the amount of R&D&I expenses does not exceed 10% of the tax due (after reducing the deductions to avoid double taxation and bonuses), the credits may offset up to 60% of the gross amount of tax due.

Switzerland

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Country introduction and overview

As part of the Swiss corporate tax reform that became effective 1 January 2020, Switzerland as one of the leading places for research and innovation introduced an OECD compliant patent box and an R&D super-deduction regime. The respective measures promote research and development located in Switzerland and create incentives for innovative value creation. In addition to the R&D related tax incentives, the Swiss tax reform also provides for a notional interest deduction on excess equity (currently only available in the canton of Zurich).

The tax measures introduced by the Swiss tax reform may be combined. However, the Swiss tax law provides for a maximum relief limitation based on which the relief effect is limited to a maximum of 70% (certain cantons provide for a lower reduction). Accordingly, at least 30% of the taxable income (before considering any relief measures) remains subject to ordinary taxation. Furthermore, no tax loss carry forward shall result from the applicable tax incentives.

Innovation/Patent Box

Entitlement

Qualifying taxpayers
The patent box regime can be applied on cantonal level and is not only available to large multinational companies but also to the numerous small and medium-sized enterprises which are domiciled and subject to taxation in Switzerland. While the introduction of the patent box is mandatory for all cantons, the tax law provides for some leeway with respect to the scope of the deduction.

Qualifying IP
Based on the Swiss tax law, all patents under the European Patent Convention and the Federal Act on Patents for Inventions as well as equivalent foreign patents qualify for the patent box. This also applies to equivalent right such as:

- Protection certificates under the Patent Act (medical products or pesticides);
- Topographies protected under the Topographies Act (semiconductors);
- Plant varieties protected under the Plant Variety Protection Act;
- Documents protected under the Therapeutic Products Act;
- Reports for which report protection exists on the basis of the provisions for implementation of the Agriculture Act;
- Foreign rights that correspond to the above-mentioned.

While not explicitly mentioned in the law, also revenues generated based on exclusive licenses for the use of (qualifying) patents may qualify for the patent box. Furthermore, patented software may also be eligible to the patent box regime.

Ownership conditions

For the patent box deduction, not the legal but the economic ownership is decisive. Accordingly, the entitlement is basically with the party which has borne the costs for the development of the qualifying asset.

Development and management conditions

The patent box is available for both (qualifying) IP developed prior to the introduction of the patent box mechanism and new IP (to the extent qualifying). When the patent box deduction is claimed for the first time, an entry tax is levied based on the R&D expenses considered for tax purposes during the 10 preceding years.

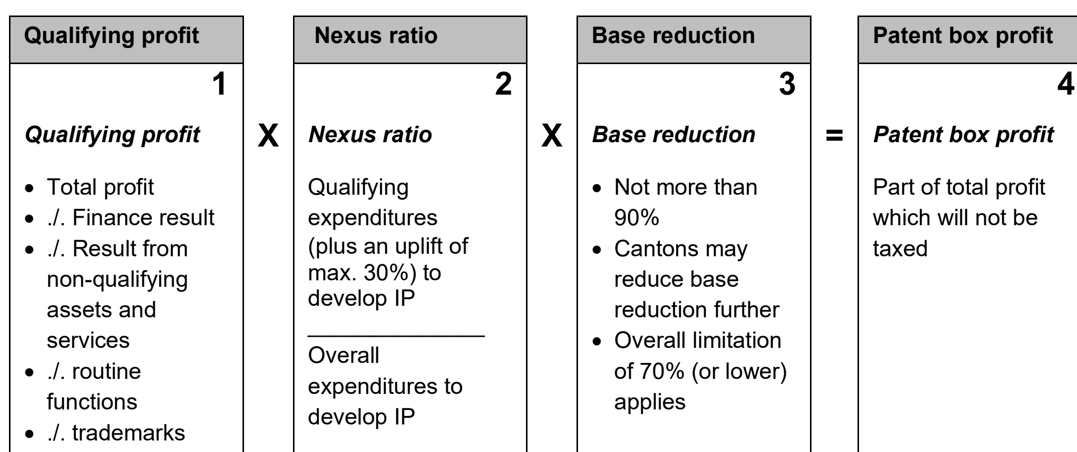
Based on the modified nexus approach, which shall ensure sufficient substance with respect to qualifying R&D and is consistent with the international OECD standard, the patent box reduction is only granted in the proportion of the qualifying R&D expenses to the total R&D expenses attributable to the taxpayer. The qualifying R&D expenses consist of own R&D expenses incurred by the taxpayer, contract R&D in Switzerland by related and unrelated parties as well as contract R&D by unrelated firms (domiciled in Switzerland and abroad) borne by the taxpayer. The relevant total R&D expenses further include contract R&D expenses from related parties abroad as well as IP acquisition costs for qualifying IP, which reduce the nexus ratio (and ultimately the benefit under the patent box) accordingly.

Qualifying income (eligible income)

The income qualifying for the patent box includes license fees and capital gains resulting from the sale of patents (or comparable rights). In these cases, the direct method may be applied whereby the directly allocatable costs are taken into account for the determination of the patent box profit. In contrast, the residual method is typically applied for proceeds from patents and equivalent rights which cannot be separated from the profit of the products sold («embedded income»). Based on the respective approach, the statutory result basically serves as a starting point from which the income and expense which are not related to patents and similar rights are excluded.

Quantifying the benefit

The patent box deduction is basically limited by 3 factors: (i) the nexus ratio, (ii) the cantonal base reduction as well as (iii) the overall maximum relief limitation. While the basic concepts of the nexus ratio and the overall relief limitation have already been outlined above, the cantonal base reduction stated in the Swiss tax law provides for a maximum reduction of 90% in relation to the patent box (only a few cantons decided to provide for a lower reduction). As depicted below, the cantonal base reduction does not replace the overall maximum relief limitation but is to be understood as an additional constraint.



The patent box reduction is calculated on an annual basis and cannot be carried forward to subsequent years or carried back to prior years.

The applicable tax rate varies from canton to canton and depends on the actual facts and circumstances and is therefore typically simulated prior to applying the patent box regime.

Application process

The patent box deduction can be claimed within the annual corporate tax return. However, an advance tax ruling with the competent tax authorities is strongly recommended.

Other aspects

The Swiss patent box regime is OECD compliant. Switzerland as non-EU member state is not subject to the EU state aid regulations and to the Pillar Two EU directive. These regulations/directives do hence not apply to the R&D super-deduction.

Tax credits are in principle available but are limited to the actual tax paid on license income.

R&D tax credit

Swiss tax laws do not foresee a classical R&D tax credit but can provide for a R&D super-deduction.

Other R&D related incentives

R&D super deduction

Entitlement
In more detail, while not mandatory, the vast majority of the Swiss cantons have introduced the R&D super-deduction which provides for an additional deduction of up to 50% on qualifying R&D expenses, i.e. scientific research (including basic research and application-oriented research) as well as science-based innovation within the meaning of the Federal Act on the Promotion of Research and Innovation. The R&D super-deduction is available to all companies which are domiciled and subject to taxation in Switzerland.

The Frascati Manual published by the OECD in 2015 serves as an interpretation guidance. According to the guidelines of the respective manual, research qualifying for the R&D super-deduction must cumulatively meet the following principles:

- novel (gaining of new knowledge)
- creative (based on original, non-obvious concepts and hypotheses)
- uncertain (in relation to the final result)
- systematic (following a plan and budget)
- transferrable (leading to reproducible results)

Accordingly, to qualify for the R&D super-deduction, the research and development shall not be related to imitations, copies of products, product cosmetics, routine changes, etc. In the product life cycle, qualifying research and development typically takes place between the initialisation phase and the transition to the production. This also excludes subsequent stages such as quality control.

Ownership conditions
Given that the focus of the R&D super-deduction lies on the input promotion, there are no specific provision with respect to the economic or legal ownership or even the need for a recognition and/or patenting of the output.

It is however important to note that in a contract R&D set-up, the entitlement to claim the R&D super-deduction is firstly allocated to the principal company and only if the principal company is not entitled to an R&D deduction (e.g. because the principal company is located abroad) the company that performs the R&D contract activity may claim the R&D super deduction.

Development and management conditions
The R&D activities must be performed in Switzerland. For sub-contracting rules please compare previous paragraph.

Quantifying the benefit
Own R&D expenditures are limited to personnel costs (salary including social security costs) of employees whose function and activity is R&D related. Own R&D expenses are considered with an uplift of 35% on the relevant personnel costs (which shall compensate for other R&D related expenses) but may not exceed total costs related to the R&D activities. In addition to the own R&D expenditures, also domestic contract R&D costs can be considered. However, the respective costs are limited to 80% of the invoiced amount. On that basis, an additional deduction of 50% can be claimed (a few cantons decided to limit the surplus deduction to a lower limit).

As the patent box, the R&D super-deduction is in scope of the mandatory maximum relief mechanism. Accordingly, the combined relief is limited to a maximum of 70% of the taxable income before considering any relief measures. This excludes the creation of a tax loss carry forward as a result of the R&D-super deduction.

Application process
The R&D super-deduction can be claimed within the annual corporate tax return. However, an advance tax ruling with the competent tax authorities may be advisable to e.g., clarify which R&D activities do meet the Frascati criteria.

Other aspects
Switzerland as non-EU member state is not subject to the EU state aid regulations and to the Pillar Two EU directive. These regulations/directives do hence not apply the R&D super-deduction.

R&D provision

On federal level, provisions recognized in the statutory financial statements for future R&D contracts awarded to third parties corresponding to up to 10% of the taxable income are accepted for tax purposes (provided they do not exceed CHF 1 million), which may result in a liquidity benefit. The cantonal tax laws provide for similar provisions.

R&D creation jobs benefit

R&D activities that create jobs may benefit from a tax break at cantonal and in certain regions at federal level based on economic promotion laws.

United Kingdom

Country introduction and overview

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The UK patent box regime was introduced as a tax incentive to UK businesses to create a competitive environment for the development and exploitation of intellectual property in the UK. Those businesses which qualify for the scheme will benefit from an effective Corporation Tax rate of 10% on income derived from the commercial exploitation of patents.

Research and development (R&D) tax reliefs aim to incentivize UK companies to increase investment in research and innovation for the benefit of the UK economy. Under RDEC, large companies (and certain SME's) can claim to receive a taxable credit payable at 20% from 1 April 2023. The credit is normally booked 'above the line' in operating profits (similar to a grant). A cash credit is repayable to the company irrespective of the tax profile of the business.

Small or medium sized companies (SME) (criteria listed below) incurring R&D expenditure can obtain an additional tax deduction against their taxable profits, the expenditure is enhanced by 86% from 1 April 2023. Where a company has tax adjusted losses after the additional R&D credits deduction, the losses can be surrendered for a cash credit of up to 10% from April 2023 of the lower of the losses or 230% (186% from April 2023) of the R&D expenditure incurred.

Innovation/Patent Box

Entitlement

UK tax resident trading companies that hold qualifying IP rights and meet the qualifying criteria (more information below) can elect into the patent box regime and potentially benefit from the reduced rate of tax on patented profits. The headline rate of UK corporation tax for most companies is 25% from 1 April 2023, compared with as low as 10% for patent box profits.

To benefit from patent box, a UK company must hold, or have an exclusive license to, patents granted by either the UK patent office (Intellectual Property Office) or the European Patent Office, as well as patents granted by certain other prescribed European countries. Also, some other less common IP rights qualify, including holding Supplementary Protection Certificates and Plant Breeders' Rights.

In calculating the benefit for companies elected into patent box a 'nexus fraction' is required to be calculated which can impact on the overall benefit. This calculates the proportion of R&D performed by the company that holds the IP rights as a fraction of the R&D costs plus the costs of acquiring patents and other group companies supporting the R&D.

Ownership conditions

A UK company must either have the legal ownership of a qualifying IP right or have an exclusive license to a qualifying IP right.

Development and management conditions

Existing IP held by a UK company can qualify for patent box where the company created or significantly contributed towards the creation of the patented invention, or process / product incorporating the patent. The company should also be undertaking 'active management' of the qualifying IP, meaning formulating plans and making decisions in relation to the development or exploitation of the qualifying IP.

Acquired qualifying IP rights can qualify for the UK patent box rules (whether acquiring the legal rights to the IP or paying for an exclusive license) so long as 'qualifying development' is performed by the company. However, when calculating the nexus fraction mentioned above, payments in respect of acquiring qualifying IP can reduce the overall benefit of patent box for the company.

Qualifying income (eligible income)

There are five main heads of income that are considered in calculating a company's profits attributable to qualifying IP.

These are:

- Head 1 – Sales income from products which incorporate one or more qualifying IP rights.
- Head 2 – Income consisting of any license fee or royalty.
- Head 3 – Proceeds of sales of qualifying IP rights or an exclusive license in respect of such rights.
- Head 4 – Damages for infringement over a qualifying IP right in cases where the company was a qualifying company for patent box purposes.
- Head 5 - Other compensation including damages or infringement income under other circumstances.

In addition to these five heads there is also the concept of a 'notional royalty' which typically applies to process patents or service income when none of the above heads are applicable.

Quantifying the benefit

Companies are required to 'stream' their patent box calculations by calculating the profit or loss on a particular income stream. This is typically for a particular product family or patent. The total gross income of the trade is the aggregate of accounting credits under each of five heads of income of the company for the accounting period as set out above less the relevant debits for the applicable steam.

Once the relevant profits are calculated for each stream, there are a number of mandatory steps in calculating the patent box benefit. This includes a deduction of a 'routine return'. This is equivalent to 10% of certain types of expenditure, including personnel and premises costs, accounting for a standard profit margin applicable to routine activities, not linked to the IP. A further adjustment is required to remove elements of the profits attributable to the marketing assets of the business. Finally, the remaining profits are multiplied by the nexus fraction mentioned above which may reduce the patented profits where the fraction is below 1.

This then calculates an additional tax deduction which reduces the taxable profits of the company.

The headline rate of UK corporation tax for most companies is 25% from 1 April 2023, compared with as low as 10% for patent box profits.

Where a patent box loss is generated in a period, this either reduces patent box profits of other group companies elected into patent box in the same period, or the loss is carried forward and offset against future patent box profits, thus reducing the benefit for those patent box periods.

Application process

The company must make an election into the patent box regime to be eligible for the benefit. This is typically done within a company's annual corporation tax computation. An election into the Patent Box regime must be made by the company within two years after the end of the relevant accounting period in which relief is claimed. Each year the company is elected into the patent box regime, they are required to calculate the profits or losses associated with qualifying IP rights, and include this within their corporation tax computation.

A company can elect out of patent box in the same way as electing it, but it is not eligible to elect back in for at least 6 accounting periods after electing out from.

Other aspects

We understand that patent box would likely reduce a group's effective tax rate for Pillar Two purposes.

R&D tax credit

Entitlement

UK companies can claim for R&D credits where they are performing qualifying R&D activities and incurring expenditure under one of the qualifying expenditure types.

For an activity to be considered as R&D for tax purposes, two key criteria must be met:

- It must seek to achieve a scientific or technological advance, and
- It must need to resolve scientific or technological uncertainties in order to achieve the advance:
    - Includes activities which directly and indirectly contribute to the advance while resolving the uncertainty is R&D,
    - R&D begins when work to resolve the uncertainty begins and ends when the uncertainty has been resolved, and
    - Success is not a requirement.

Currently, there are two regimes in the UK for R&D credits. One for large companies and one for small or medium sized companies (SME).

Typically, for a company to be classed as an SME for R&D purposes the group must have:

- Fewer than 500 staff and either.
- A turnover of no more than EUR 100 million; or
- Gross assets of no more than EUR 86 million.

However, other factors such as the share ownership of the group are required to be considered.

Where R&D activities of an SME are subsidized or subcontracted by another party, these are ineligible to be claimed under the SME R&D credits regime but may be eligible to be claimed under the large company rules.

However, there are proposals from the UK government to merge the reliefs into a single relief from 2024 and it is yet to be confirmed the specifics of the new rules.

Ownership conditions

There is no requirement for the company to own the IP of the product, so long as the R&D definition above is met for the activities.

From accounting periods beginning on or after 1 April 2023, there will be only limited cases where overseas R&D is allowable.

The resulting IP from the R&D development can reside abroad and does not need to be held by the UK company.

Where R&D is subcontracted to a large company, the activities performed by the large company typically qualify for R&D credits unless they were subcontracted by a UK company that is a SME as defined above.

SME companies can claim for costs paid to other companies for subcontracted services. Currently this includes overseas companies, but from April 2023, this will be restricted to UK companies only.

The rules may change from 2024, due to the on-going consultation set out above. One of the key areas that is being looked at is which party is eligible for R&D credits in a subcontractor relationship.

Quantifying the benefit

There are a number of types of qualifying expenditure that may be able to be included within the R&D credits claim. Only costs that fall within one of these categories qualify for R&D credits.

These include:

- Staffing costs - including salary, bonuses, employers’ pension contributions, but excluding benefits in kind.
- Externally provided workers (EPWs) - payments to other companies for the provision of workers (for example agency workers)
- Subcontractors - subcontractor payments to other companies only qualify within the SME scheme.
- Consumables - including:
    - Utilities
    - Consumed items
    - Software licenses
    - Cloud computing costs and Data acquisition costs (from April 2023)
- Payments to “qualifying bodies” for large companies - this includes payments to universities and charities.

Large companies
R&D credits for large companies are given as a taxable “R&D expenditure credit” (RDEC) which is calculated as a percentage of the qualifying expenditure for the relevant accounting period. The expenditure

credit rate is 20% from 1 April 2023 (previously 13%), with the main rate of tax being 25% (previously 19%, leading to a net cash benefit of 15% (previously 10.5%).

The RDEC is first offset against a company's tax liability for a period. Any remaining amount may be payable to the company from the UK tax authorities in cash, subject to a number of steps and restrictions.

One key restriction is that any RDEC balance remaining after offsetting against the company's tax liability is capped by the PAYE/NIC amounts paid by the company in respect of the R&D workers for the period. Any amount which exceeds the cap is carried forward and treated as an expenditure credit for the next accounting period, subject to the same cap mechanism.

SME companies
SMEs incurring R&D expenditure can obtain an additional tax deduction against their taxable profits, from 1 April 2023 expenditure is enhanced by 86% (previously 130%). Where a company has tax adjusted losses after the additional R&D credits deduction, the losses can be surrendered for a cash credit of up to 10% (previously 14.5%) of the lower of the losses or 186% (previously 230%) of the R&D expenditure incurred.

The cash credit for SME companies is typically capped at £20,000 plus 300% of the income tax and social security costs of the company, subject to some exceptions.

Application process

A company makes an R&D credit claim by the submission of their corporate tax return to include the required information. The company has 2 years from the end of the accounting period to submit a claim.

There are some upcoming changes to the documentation requirements for making a claim, including providing the UK tax authorities with:

- information about the company, including details of any agent who assisted with the claim and a named internal contact responsible for the claim,
- a breakdown of qualifying expenditure into the various expenditure types, and
- project documentation setting out how each project meets the advance / uncertainty criteria, generally between 3 and 10 projects per claim.

There may also be a 'pre-notification' requirement. This means that a company may have 6 months from the end of the accounting period to notify the UK tax authorities that an R&D claim is going to be made, if the company has not made a claim within the past three years.

Other aspects

Whilst the UK is not part of the EU state aid rules, the SME scheme is subject to EU state aid regulations. Albeit, with the potential merger of the reliefs from 2024, it's possible that this would no longer be applicable after this time.

We understand that the large company RDEC will likely be considered a "qualified refundable tax credit" (QRTC) for Pillar Two purposes, therefore this should not adversely affect the group's effective tax rate for the Pillar Two purposes.

Regarding the SME relief, we understand that this won't be considered a "qualifying refundable tax credit" (QRTC) for Pillar Two purposes, this may affect the group's effective tax rate for the Pillar Two purposes. However, due to the SME entry requirements, it is unlikely that a company that meets the SME definition would also be affected by the Pillar Two rules.

Other R&D related incentives

There are various government grants available for companies to apply for, however, these change regularly. For further details on these grants, please contact us.

Comparison

Innovation/Patent Box by country

Tax Factors	Belgium	France	Germany
Reduced tax rate to standard tax rate	3.75% - Effective tax rate is based on the CIT rate of 25% as of tax year 2021.	10% / 25%	N/A
Qualifying IP rights	Patents and Supplementary Protection Certificates, Breeders' Rights, Orphan Drugs, Data & Marketing exclusivity (as granted by EU or other government bodies) and IP of Copyrighted Software.	Patent, manufacturing processes, software under copyrights, plant variety rights	N/A
Qualifying income / types of income included	License income, income embedded in sales income, income derived from process innovation, remunerations from a court/ arbitral decision, amicable settlement or insurance contract and proceeds derived from the sale of an IP right.	Royalties, licensing fees, gains on sale of IP.	N/A
Acquired IP favored?	Yes, in case they are further developed.	No	N/A
Applicable to existing IP?	Yes	Yes	N/A
Cap on benefit?	No	No	N/A
Includes embedded royalties?	Yes	No	N/A
Includes gain on sale of qualified IP?	Yes, subject to conditions.	Yes	N/A
Can R&D be performed abroad?	Yes	Yes, under conditions that not to related company.	N/A
Tax credit WHT on qualified income?	Yes	Complex issue.	N/A
Year enacted	July 2016	2019	N/A

Tax Factors	Italy	The Netherlands	Spain
Reduced tax rate to standard tax rate	Patent box allows the 110% super-deduction for CIT and Regional tax purposes of R&D and Innovation expenses. Given CIT is levied at 24% and regional tax at 3,9%, the tax benefit of the patent box is equal to 30,69% of the eligible expenses.	Standard (corporate) tax rate: 25.8% Innovation Box effective tax rate: 9% (as of 2021).	Reduction of 60% in the tax base for income coming from the cession (or transfer) of certain intangible assets.
Qualifying IP rights	Patents, registered software, legally protected drawings, and models.	Software and patented IP, e.g. plant breeders rights, EU trading license for a medicine, protection certificate granted by Dutch Patent Centre, and registered utility models developed under approved R&D projects for large taxpayers. For small taxpayers also non-patented IP developed under approved R&D projects.	Patents, utility models, supplementary protection certificates for medical purposes and phytosanitary products, legally protected models and designs, registered software that results from R&D projects.
Qualifying income / types of income included	Super-deduction mechanism is applicable on eligible expenses.	Net income from qualified IP.	Taxable income from the license of IP created or held by Spanish companies.
Acquired IP favored?	Yes, if purchased from third parties and further developed.	Yes, if further self-developed under an approved R&D project.	No
Applicable to existing IP?	Yes. Expenses incurred for the development of existing Ips can be super-deducted year per year.	Patented IP developed or redeveloped from 2007; IP from approved R&D projects from 2008; IP from 30 June 2016 subject to Nexus Approach and other BEPS 5 criteria.	Yes
Cap on benefit?	No	No	No
Includes embedded royalties?	N/A	Yes	Yes
Includes gain on sale of qualified IP?	N/A	Yes	Yes
Can R&D be performed abroad?	Yes, subject to conditions.	Yes, subject to conditions.	Yes, subject to conditions.
Tax credit for WHT on qualified income?	N/A	Yes, subject to limitations.	No
Year enacted	2021	2007, 2010, 2017	2008

Tax Factors	Switzerland	United Kingdom	
Reduced tax rate to standard tax rate	Qualifying income is de facto exempt at cantonal level.	10% for patent box profits vs 25% main rate of corporation tax from 1 April 2023.	
Qualifying IP rights	Swiss and foreign patents, exclusive licenses that qualify the OECD nexus requirements.	Mainly UK and European patents.	
Qualifying income / types of income included	License fees, capital gains and "embedded" income.	Sales of products, license income, sale of the patent, patent infringement. For process patents a 'Notional royalty' is required to be calculated.	
Acquired IP favored?	No	In house developed IP is typically favored. Acquired IP can qualify where the company does some development on the IP or product.	
Applicable to existing IP?	Yes (after buy-in)	Yes	
Cap on benefit?	Yes	No	
Includes embedded royalties?	Yes	Yes	
Includes gain on sale of qualified IP?	Yes	Yes	
Can R&D be performed abroad?	Contract R&D by unrelated parties	Potentially, but this may reduce the benefit.	
Tax credit for WHT on qualified income?	N/A	N/A	
Year enacted	2020	2013 with significant changes from 2016	

R&D tax credit by country

Tax Factors	Belgium	France	Germany
Incremental or volume based	Volume based	Volume based	Volume based
Funding rate	• One-time R&D investment deduction of 13.5% (tax year 2023); • Spread R&D investment deduction of 20.5% (tax year 2023); and • The above incentives can be claimed in the form of an R&D tax credit which corresponds to the R&D investment deduction, multiplied by the standard corporate tax rate of 25% (as of tax year 2021).	30%	The funding rate is 25% on eligible costs. Eligible costs: • personnel expenses for R&D employees (wages and social security contributions) • 60% of the costs for contract research
Cap /Ceiling on benefit?	No, but for both the R&D investment deduction and the R&D tax credit, the yearly carried-forward amount that can be claimed is capped.	5% Benefit for amount above EUR 100m	Yes, max EUR 1m per year
Can R&D be performed abroad?	Yes, subject to condition and country restrictions.	Yes, subject to conditions and country restrictions.	Yes, subject to conditions and country restrictions.
Subcontracting rules / Contract Research	Yes, subject to conditions. According to ruling practice, the taxpayer should be able to demonstrate that the know-how created will contribute to the taxpayer’s future profitability.	Open, with the accreditation of the 1/3 by the French Ministry of research.	Yes, subject to conditions. In case of contract research the principal only is entitled to claim the R&D tax credit.
Can resulting IP reside abroad?	Requires Analysis	Yes	Yes
Carry forward / carry back	Unused R&D investment deduction is carried forward for an unlimited period. Unused R&D tax credit is repayable after five tax years.	Carry forward yes and refundable.	R&D tax credit assessed in a year is offset against the next income tax assessment issued in the same year. No allocation to fiscal years.
Refundable option	Yes, unused R&D tax credits after five tax years is paid to the company.	Yes	Yes, if R&D tax credit assessed in a year is higher than income tax assessed in the same year.
Year enacted	1982	1983	2020

Tax Factors	Italy	The Netherlands	Spain
Incremental or volume based	Volume based	Volume based	R&D: Hybrid TI: volume-based
Funding rate	From FY 2023: • 10% tax credit for R&D expenses. R&D activities are those described in the OECD's Frascati Manual. • - 5% tax credit for Innovation expenses as described in the OECD's Oslo Manual and design activities for specific sector, such as fashion.	R&D credit for qualifying R&D wages, investments and expenses: 32% for the first EUR €350,000 and 16% on the excess amount (known as WBSO). Startups are eligible for an increased deduction of 40% on the first EUR €350,000 of the R&D wage costs and other R&D costs and expenses.	R&D: ≥ 42% TI: 12%
Cap /Ceiling on benefit?	Tax credit must not exceed 5m€ or 2m€ per year respectively for R&D and Innovation. The tax credit must be utilized to offset CIT, Regional tax, VAT, WHT and SSC and must be split in 3 yearly installments from the tax period after the one in which the eligible expenses are incurred.	N/A	R&D: EUR 3 million TI: EUR 1 million
Can R&D be performed abroad?	Yes, under the subcontracting rules and with country restrictions.	Yes, but the activities must take place inside the EU territory and by staff on a Dutch payroll.	Yes, with country restrictions.
Subcontracting rules / Contract Research	Yes, provided the Italian taxpayers can be considered as "Investor" (bears the risk, the cost, owns the IP, has the right for the economic exploitation of the resulting Ips.	Not allowed for R&D but for auxiliary work that serves your own R&D project.	R&D expenditure if paid for by a third-party does not qualify for the R&I tax credit
Can resulting IP reside abroad?	No, please see the "Investor" requirements for Subcontracting roles	Yes	Yes
Carry forward / carry back	R&D and Innovation tax credits can be carried forward to be utilized in future tax periods if the amount exceeds the tax payments due.	No	Yes, with a 20% discount
Refundable option	No	No	Yes
Year enacted	R&D tax credit is applicable until FY 2031, Innovation until FY 2025.	1994	2014

Tax Factors	Switzerland R&D super deduction	United Kingdom (Large Company)	United Kingdom (SME)
Incremental or volume based	Volume based	Volume based	Volume based
Funding rate	up to 50% at cantonal level.	For large company rules, provides a cash benefit of 10.5% of R&D expenditure, increasing to 15% from 1 April 2023.	Additional tax deduction against their taxable profits, the expenditure is enhanced by 86% from 1 April 2023. Where a company has tax adjusted losses after the additional R&D credits deduction, the losses can be surrendered for a cash credit of up to 10% from April 2023 of the lower of the losses or 186% from April 2023 of the R&D expenditure incurred.
Cap /Ceiling on benefit?	Yes (max. 70% of taxable income before R&D super-deduction, patent box etc.)	If not tax paying, cash credit is limited to the amount of UK employee income tax and social security paid by the company for R&D workers in the period.	The cash credit for SME companies is typically capped at £20,000 plus 300% of the income tax and social security costs of the company, subject to some exceptions.
Can R&D be performed abroad?	Yes	From 1 April 2023 the rules are changing, limited overseas R&D expenditure is able to be claimed.	From 1 April 2023 the rules are changing, limited overseas R&D expenditure is able to be claimed.
Subcontracting rules / Contract Research	Domestic contract R&D	Currently the company performing the R&D claims for the amount (rather than the one paying for this). However there is a consultation ongoing and this may change.	Currently, SME companies can claim for costs paid to other companies for subcontracted services.
Can resulting IP reside abroad?	Yes	Yes	Yes
Carry forward / carry back	No	Either offsets against company's tax liability or payable in cash from UK tax authorities.	If not surrendered for the credit, losses generated from the R&D credit claim can be carried back to the previous accounting period, or into future periods with some restrictions.
Refundable option	N/A	Yes	Yes
Year enacted	2020	2013 for the latest iteration	2008

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