

Reduce your effective tax rate

Research & development opportunities for medical device companies



Ireland's research and development (R&D) tax regime was originally introduced in 2004. Improvements and refinements introduced in successive years have led to what we can now describe as a world-class R&D tax regime.

One of the most significant of the recent amendments to this regime is the 'monetisation' of the R&D tax credit.

This now enables companies to obtain cash for unutilised credits and to generate cash refunds of tax by carrying back R&D tax credits to the prior year. The ability to generate cash in the current environment is an extremely attractive proposition that merits serious consideration.

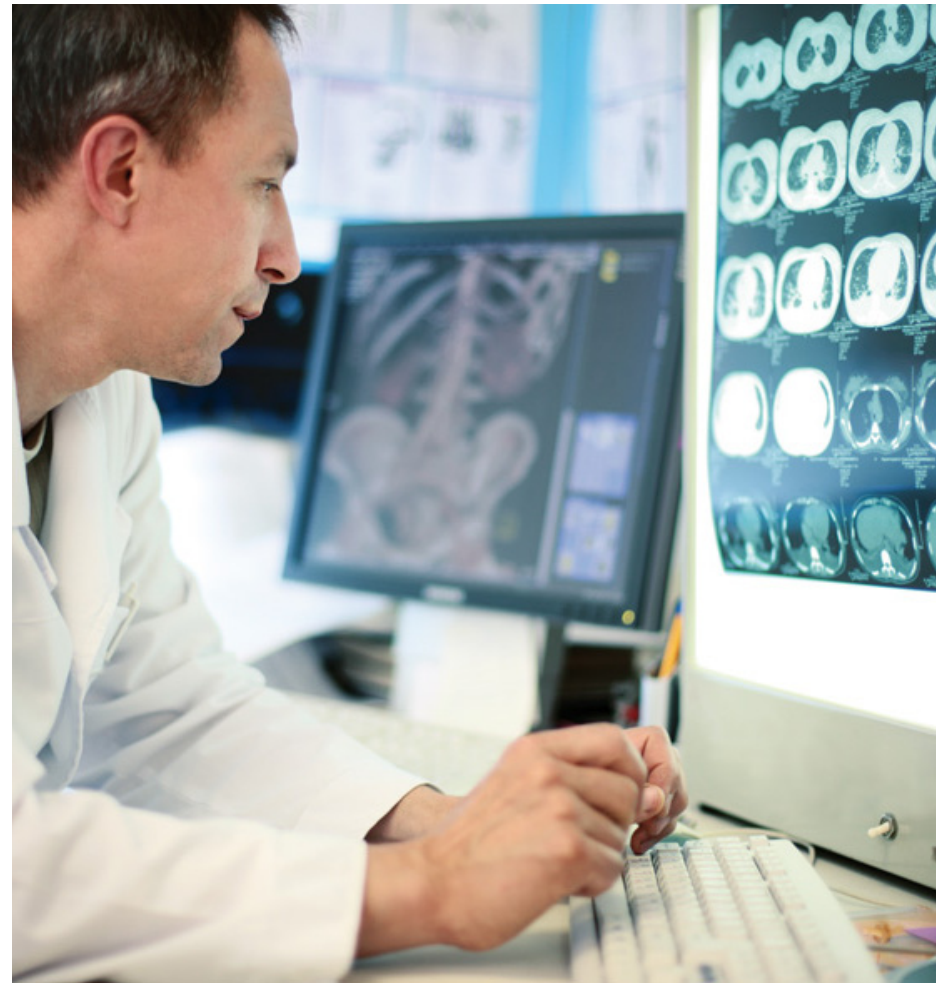
This has also resulted in widespread acceptance that the R&D tax credit can now be accounted for 'above the line' in the profit and loss account thereby increasing the attractiveness of this regime.

Such improvements together with an enhanced regime for claiming the R&D tax credit on expenditure incurred on qualifying R&D buildings should encourage companies to re-evaluate their current R&D focus.

If you would like to discuss possible tax planning opportunities for your business in this area, please contact any member of our team or your usual PwC contact.



John M Kelly
PwC Pharmaceutical & Life Science Leader



Research and development

Opportunities for medical device companies

What are the basic R&D tax credit provisions?

A 25% credit applies (on a group basis) to incremental expenditure on R&D incurred by companies that are themselves trading or are members (more than 50% owned) of a trading group. The tax credit is available for offset against the current year corporation tax liability and is in addition to the corporate tax deduction that is otherwise available for the expenditure.

The incentive is aimed predominately at in-house R&D activity, although, expenditure incurred by companies on sub-contracting R&D work to unconnected parties will qualify for a tax credit up to a limit of 10% of the qualifying R&D expenditure in any one year. A similar provision exists in relation to universities, with the limit set at 5% of the qualifying R&D expenditure in any one year.

Monetisation of the R&D tax credit

Companies now have the ability to claim repayment of excess R&D tax credits over a three year cycle. The repayment is limited to the greater of the corporation tax payable by the company in the preceding ten years or the payroll liabilities (PAYE/ PRSI/levies) for the period in which the relevant R&D expenditure is incurred. Companies also now have

the ability to carry back excess R&D tax credits to the prior year thereby generating cash refunds of tax paid.

Accounting treatment of the R&D tax credit

Companies have the option to account for the credit 'above the line' in the profit and loss account thereby immediately impacting on the unit cost of R&D, which is the key measurement used by multinational companies when considering the location of R&D projects. This can be extremely helpful to Irish subsidiaries of multinational companies enabling them to compete with lower cost jurisdictions. Irish Revenue have confirmed that where a company accounts for the R&D tax credit through the profit or loss account before tax, the tax credit will not be regarded as taxable income of that company or another company to which the credit has been surrendered.

Expenditure on R&D buildings

A company may now claim the full credit in the year the relevant expenditure on buildings is incurred rather than spread over four years as was previously the case. The definition of 'qualifying building' has also been made more flexible and

the requirement that the building has to be used 'wholly and exclusively' for R&D purposes, has been relaxed. Instead, a 35% R&D activity 'hurdle' over a four year period is the required benchmark going forward. This is particularly beneficial where R&D is carried out in a manufacturing environment.

Claims for credit must be made within twelve months from the end of the accounting period in which the R&D expenditure was incurred.



Specific regulations on qualifying science or technology activities

Regulations have been issued outlining the categories of activities that fall within the field of science or technology under the headings of natural sciences, engineering and technology, medical sciences and agricultural sciences.

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How can we help?

Whether you are a start-up company with significant losses or an established company, now is the time to revisit opportunities around Ireland's R&D tax credit regime.

PwC has a dedicated R&D team with a wealth of experience in dealing with R&D tax credit claims for medical device companies. We have provided assistance from evaluation and submission of claims through to maximising the quantum of the credit and ensuring that the required supporting documentation is sufficiently robust. We are also happy to liaise with Revenue authorities on your behalf.

If you would like to discuss whether specific activities in your business would qualify for a R&D tax claim, we would be delighted to hear from you.

What is the base period?

The R&D tax credit system is based on incremental expenditure on R&D. In the case of a company with a calendar year end, the incremental R&D expenditure incurred in a particular year over that incurred in the year ended 31 December 2003 qualifies for R&D tax credits. The base year has been set as 2003 indefinitely.

What expenditure qualifies?

To qualify for the R&D credit, a company must incur expenditure in carrying on qualifying R&D activities in the European Economic Area. The expenditure must be tax deductible only in Ireland and not in any other country (e.g. in a branch outside Ireland).

The expenditure must be incurred on systematic, investigative or experimental activities in a field of science or technology that falls within any of the following categories:

- Basic research to acquire new scientific or technical knowledge without a specific practical application in mind.
- Applied research to acquire scientific or technical knowledge and directed towards a specific practical application.

- Experimental work which draws on scientific or technical knowledge or practical experience for the purpose of achieving technological advancement and which is directed towards producing new, or improving existing, materials, products, devices, processes, systems or services.

What level of documentation is required for activities to qualify?

The R&D activities must be systematic, investigative or experimental in nature. The guidelines issued by Irish Revenue require documentation to be maintained on:

- The nature of the project, the objective of the research and the research method
- The field of science or technology concerned
- The scientific or technological uncertainty that is being addressed by the R&D and the project's scientific or technological goals



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- A detailed research programme
- The skills and qualifications of the research team
- Time records
- Expenditure analysis, including third party expenses and royalty payments.

Irish Revenue is prepared to give an advance opinion as to whether a particular project would qualify for an R&D tax credit.

Additional Revenue guidelines

The Irish Revenue has also provided guidelines outlining its interpretation of the legislation. The guidelines state that seeking to achieve scientific or technological advancement involves the removal of scientific or technological uncertainty through systematic, investigative or experimental activity.

The guidelines also state that an advance in technology means an advance in the overall knowledge or capability in the relevant field and not a company's own state of knowledge. Work which uses science or technology but which does not

advance scientific or technological capability as a whole is not an advance in science or technology, nor is it resolving uncertainty as to whether new products or process will be commercially viable.

Technological uncertainty, in Revenue's opinion, arises in two situations:

- Uncertainty as to whether a particular goal can be achieved at all, or
- Where there is certainty that the goal can be achieved there may be uncertainty in relation to other specifications such as reliability or reproducibility.



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