



Innovation Monitor

Insights on Knowledge Development Box

2016/2017 Edition





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Methodology:

This survey was conducted by RedC Research on behalf of KPMG. Over 200 Irish based companies participated. The survey was confined to businesses with at least 10 employees and quotas were placed on company size to ensure a nationally representative sample. Interviews were conducted with the Finance Director, Tax Director or a similar individual/partner in the company.

Introduction

For many companies across Ireland, innovation is a strategic priority. Eighty percent of businesses who participated in recent research conducted by Red C on behalf of KPMG are innovating in Ireland and/or abroad. The most significant influence on their decision to innovate is the availability of funding. Access to qualified in-house personnel is also very important.

Despite the high level of participation in innovative activities, many companies, particularly SMEs, miss out on financial benefits through lack of awareness of incentives like the R&D tax credit and the Knowledge Development Box.

Our research highlights opportunities to improve Ireland's innovation ecosystem and shows that businesses would like government to do more to nurture and support innovation.

Key findings:

- 80 percent of businesses who participated in the latest KPMG Red C research are engaged in innovative activity in Ireland and/or abroad.
- 70 percent of businesses believe Ireland is innovation friendly.
- The most significant influences affecting the decision to innovate are availability of funding and access to qualified in-house personnel.
- 42 percent of businesses have availed of the R&D tax credit.
- 57 percent of businesses were unaware of the Knowledge Development Box prior to being contacted for our research,

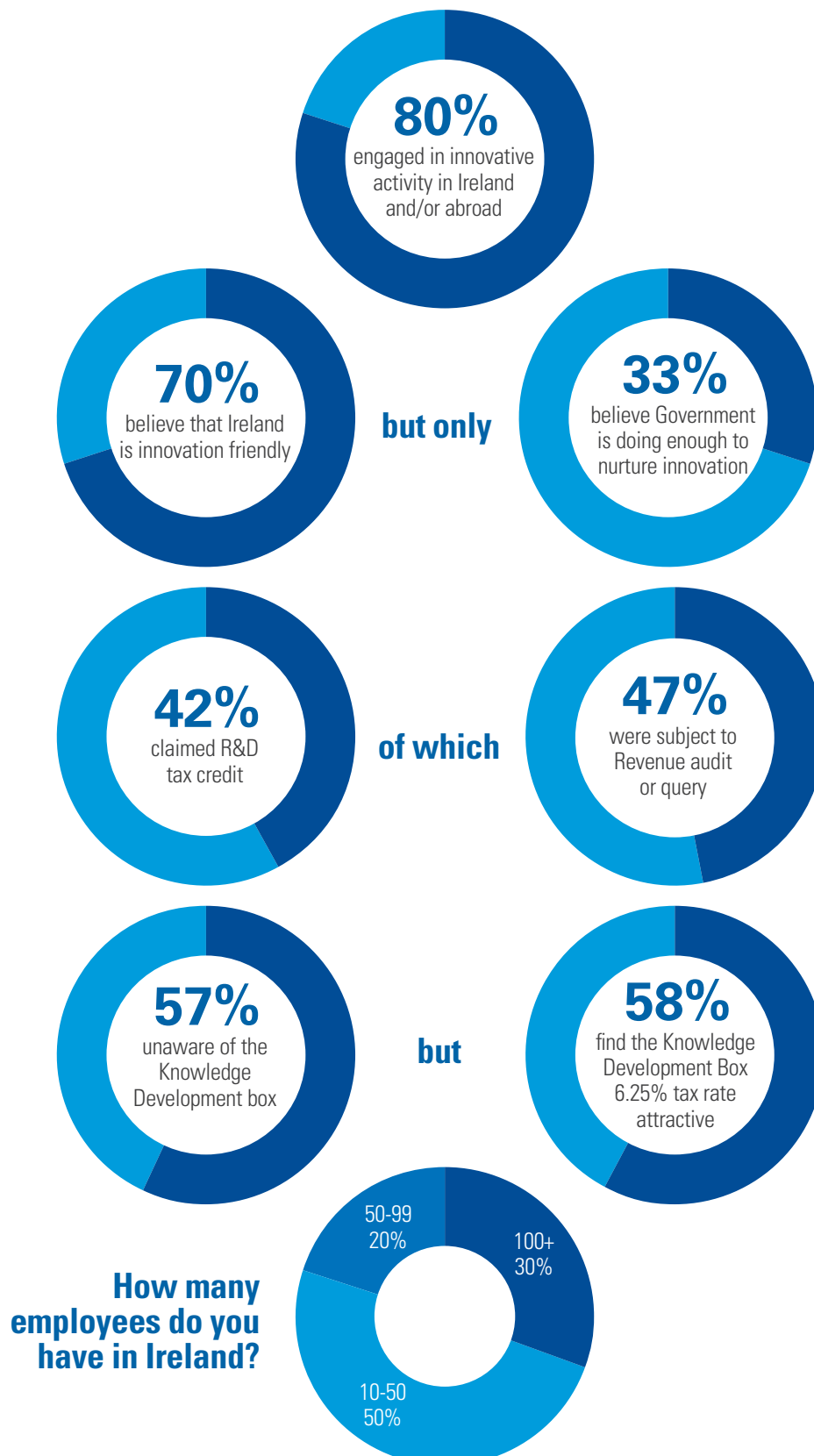
We hope that you will find this snapshot of current innovation matters in Ireland useful and thought provoking. If you would like further information or to discuss how to build more innovation into your business, please do get in touch — our contact details are included at the back of this report.



Damien Flanagan
Director, Tax



Summary of key findings



Source: KPMG 6th Innovation Monitor survey

Innovation Ecosystem

At a time when businesses face rapid change and disruption, nurturing innovation has never been more important.

While 70 percent of the 200 businesses who participated in KPMG's latest research consider Ireland to be innovation friendly or very friendly, only a third believe the innovation ecosystem is sufficiently connected.

By 'innovation ecosystem', we mean the effective interaction of funding regimes (e.g. the R&D tax credit regime and grants), non-finance supports, collaborative opportunities, and the ability to attract other innovative firms and talent.

Areas where businesses believe there is room to improve include:

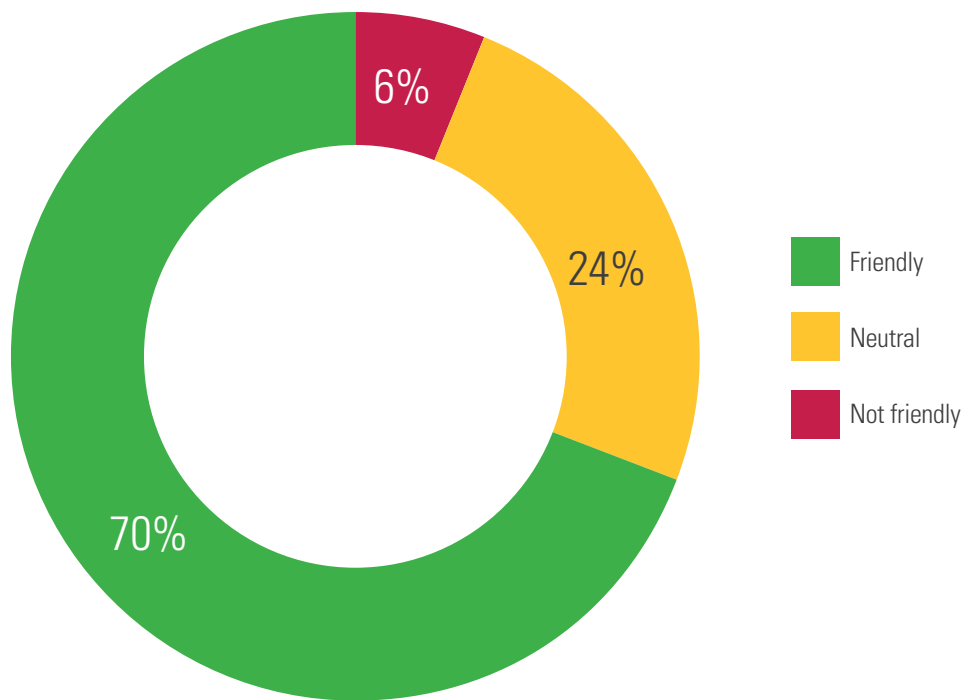
- **Funding regime and grants:** Companies would like to see more grants and incentives being made available. There is also a need for easier access to funding particularly for entrepreneurs, start-ups and smaller companies. As one respondent put it, "There's a lot of tax initiatives for well established companies that are already making profits, but not for start-ups."
- **Communication:** The need for better communication about available incentives and supports for Irish companies was highlighted by many respondents who reported difficulties accessing information, understanding application procedures and obtaining feedback.
- **Collaborative opportunities:** "For us it's the link between business and third level where there needs to be some development," explained one company director, echoing a need identified by many for improved access to collaborative opportunities.
- **Talent:** The personal tax system was flagged as a barrier to attracting talent from outside of Ireland. "We have some very good government initiatives and good incentives. But for attracting people, the taxation system does not encourage them to move here to Ireland."

- **Simplification:** Businesses believe that there is "still too much red tape" and want greater simplification and streamlining of administrative barriers that prevent the take up of the R&D tax credit.
- **R&D tax credit:** A number of concerns about the R&D tax credit system were highlighted including the need to simplify the application process and improve feedback. "Make it easier for a company to get the R&D credit with simpler guidelines for how to qualify" was a typical comment.
- **Knowledge Development Box:** Of the companies who were aware of the Knowledge Development Box, several suggested that the scheme should be widened and some commented on the need to improve the patents system. "I think we settled for a too narrow definition of the function equivalent of patents," observed one company director.

Overall, 44 percent of those that expressed an opinion either way, believe there is scope for government to do more to nurture innovation.



How innovation friendly is Ireland?



Source: KPMG 6th
Innovation Monitor survey

“In comparison with other countries, Ireland has fewer young patenting firms, less public spending on R&D, and less industry financed public R&D. Policy is going in the right direction to address these weaknesses but there is scope for improvement.”

OECD Economic Survey of Ireland 2015

The Innovators

Over the years, KPMG has seen a steady increase in the numbers of businesses moving from planning innovation to actively engaging in innovative activities.

Our research shows 80 percent of businesses are innovating in Ireland and/or abroad yet only a third have applied for patents.

Some companies may miss out on potential financial benefits through lack of awareness of available incentives like the R&D tax credit and Knowledge Development Box.

Too much red tape is also a barrier. As one director put it, "There's a lot of hoops for businesses to go through before they get anything."

Patents and computer programs

While almost 75 percent of the 200 businesses who participated in KPMG's research are currently innovative in Ireland, only 31 percent of these have obtained patents or developed computer programs protected by copyright.

One third of the businesses who have said they are innovative in Ireland but do not have patented products, believe their product is 'patentable'.

What this tells us is that 54 percent of those who are innovative either have a patent or believe they have something patentable, or a computer program protected by copyright. In other words, they have a 'qualifying asset' for the purpose of the KDB.

Of those that currently have patents or computer programs protected by copyright, 60 percent intend to or already are generating income from exploiting these IP assets. It is possible that these companies could avail of the KDB (see over page for more detail on the KDB).

The process to obtain a patent can be expensive and rigorous. "A lot of people know a lot of things but that doesn't mean you can patent, there's no tax incentive unless you reach the patent level and it's stringent..." one director observed. Crucially, the KDB will allow SMEs to expand the definition of intellectual property to include inventions that are certified as being

novel, non-obvious, and useful. In other words, the intellectual property must be 'patentable', but doesn't have to be patented. This reduces the administration burden and cost on SMEs and makes it easier to access the KDB.

Other barriers to applying for patents include:

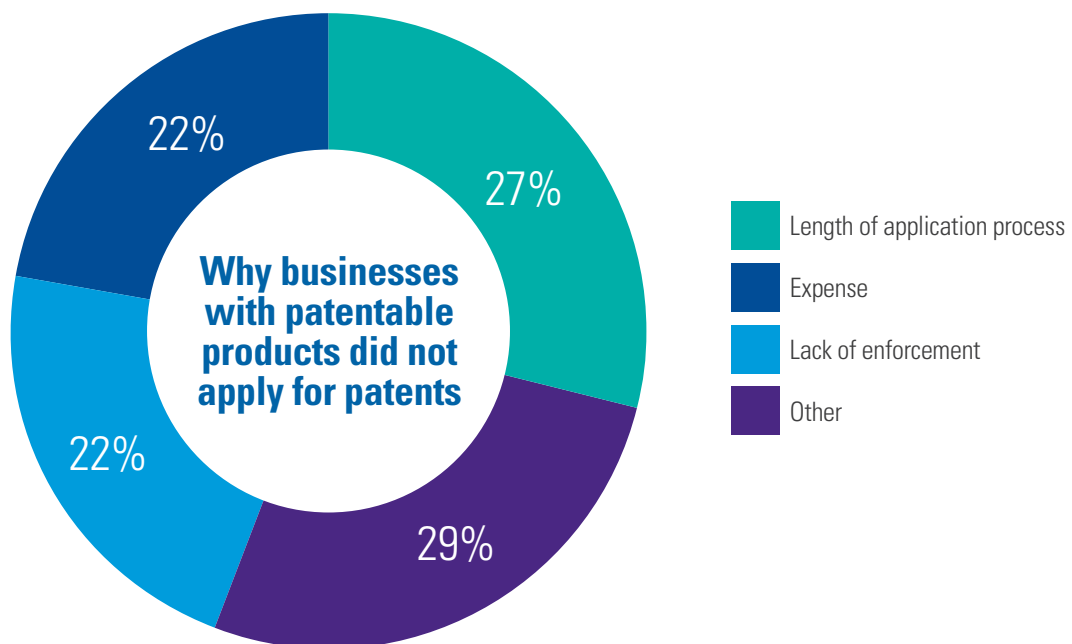
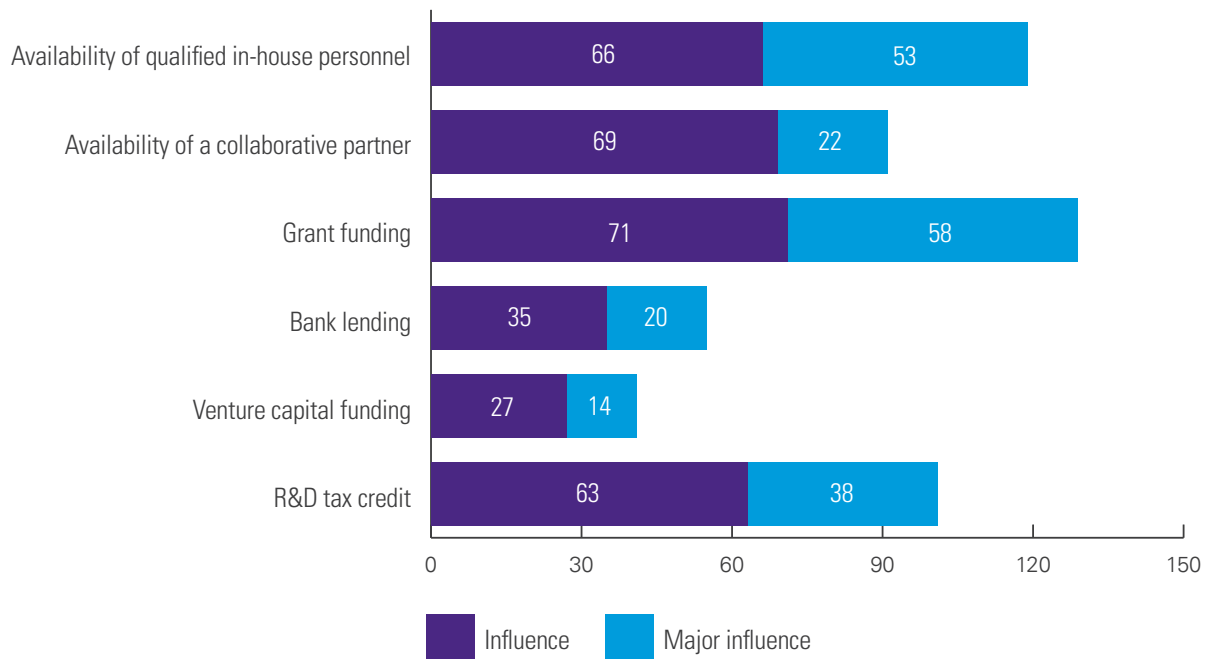
- the length of time it takes to obtain a patent which dilutes the commercial advantage,
- the expense of obtaining patents, and
- lack of effective enforcement of patents in many jurisdictions.

Deciding to innovate

The availability of grant funding is the most significant influence when businesses are considering innovation, well ahead of bank lending and venture capital funding. Access to qualified in-house personnel is also important, closely followed by R&D tax credits and the availability of collaborative partners.



What factors influence innovation?



Source: KPMG 6th
Innovation Monitor survey

Funding & Incentives

A majority of the businesses who participated in KPMG's research said that the availability of the R&D tax credit would influence their decision to innovate while 58 percent said that the Knowledge Development Box is attractive to their business.

R&D Tax Credit

"The R&D tax credits are very welcome but the process is quite rigorous, so maybe simplify it."

Despite considering themselves innovative, some businesses exclude themselves from applying for the R&D tax credit because they do not believe they are engaged in R&D. However the definition of 'innovative' is closely aligned to the definition of 'R&D' for the purposes of the R&D tax credit, suggesting that some businesses not currently claiming the credit could in fact do so.

Of the 200 businesses who participated in KPMG's research, 85 have claimed the R&D tax credit. Just under half of these businesses had their claims subjected to a Revenue Audit or query. This is a large percentage of claims but is reflective of what we see in our dealings with companies that have claimed the R&D tax credit.

Knowledge Development Box

"Definitely publicise it more. I wasn't aware of the Knowledge Development Box."

The objective of the Knowledge Development Box is to provide a highly attractive low effective tax rate for income generated from exploiting certain IP that was developed as the result of R&D activity by an Irish company.

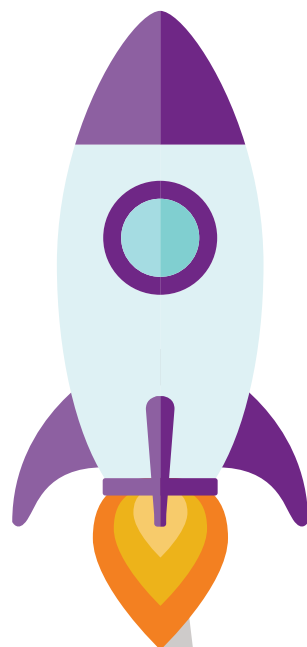
The scheme, which is the first of its kind to be fully compliant with OECD rules, provides that profit from 'qualifying assets' earned by an Irish company can potentially be taxed at a rate of 6.25 percent.

'Qualifying assets' include patents, copyrighted software and, in relation to smaller companies, other intellectual property that is similar to an invention which could be patented.

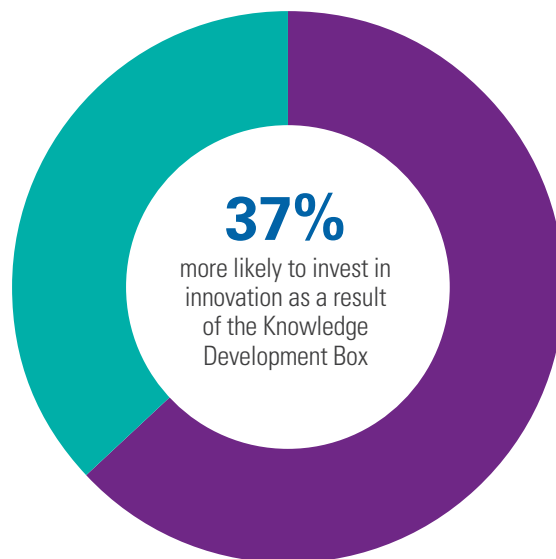
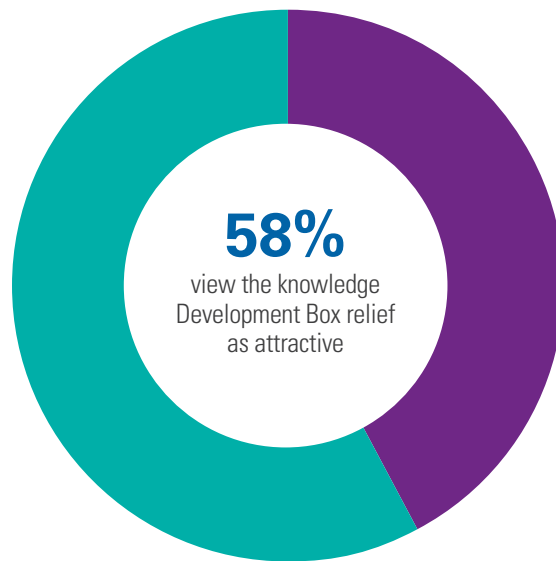
For the KDB, smaller companies are defined as companies with annual income from intellectual property not in excess of €7.5m, employing fewer than 250 people, and with a turnover of less than €50m or a balance sheet of less than €43m.

While the majority (57 percent) of businesses who participated in KPMG's research were previously unaware of the KDB, most view it as attractive.

The KDB relief is available to companies for accounting periods beginning on or after 1 January 2016.



Influence of the Knowledge Development Box



Source: KPMG 6th
Innovation Monitor survey

Conclusion

As the pace of change and disruption accelerates across virtually every sector of the economy, innovation has become a strategic priority for most Irish businesses.

Eight out of every 10 participants in KPMG's latest research regard their companies as innovative and most believe that incentives like the Knowledge Development Box and the R&D tax credit will benefit their businesses.

While there is room for improvement across many areas of the innovation ecosystem, it is encouraging that seven out of 10 participants consider Ireland to be innovation friendly.

Nevertheless, our research indicates an awareness gap about incentives and the workings of specific schemes such as the R&D tax credit and the KDB. We know from our research that 60 percent of companies with 'qualifying assets' intend to or are already generating income from these assets. These are the companies that the KDB is designed for — it would be a shame if they missed out on claiming the KDB because of a lack of awareness.

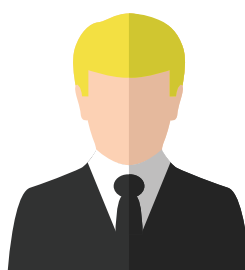
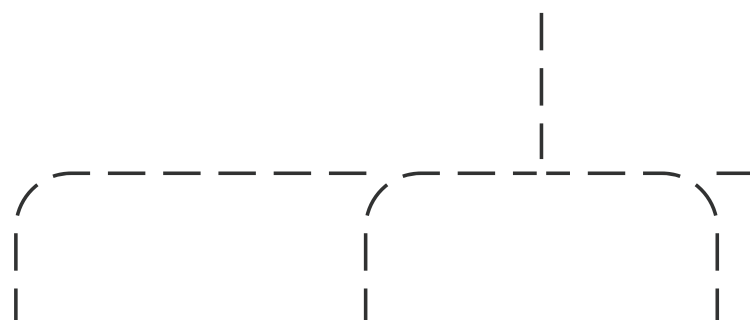
70% of the survey respondents currently employ less than 100 people in Ireland, and thus could be said to fit within the SME definitions. Many smaller businesses believe they are not engaged in qualifying activities and consequently do not apply for incentives even though some could in fact do so. Experience shows that companies also decide against claiming because they are too busy, feel it is too much effort to claim, or simply do not understand the application procedures.

An information campaign to educate companies on the availability and workings of the available incentives would help to address the knowledge gap.

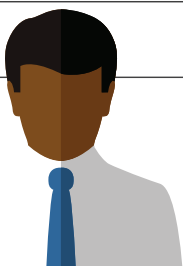
How KPMG can help

At KPMG, we understand how difficult it can be to undertake and fund an innovation project. We have a proven record of working with ambitious businesses, from indigenous start-ups to leading multinationals, and can help with a wide range of business and finance issues to ensure that companies stay focused on what matters. In particular, we have a dedicated R&D Incentives Practice who can advise companies on relevant tax incentives like the R&D tax credit and the Knowledge Development Box.

Our team of tax and finance professionals can guide companies through all the issues that need to be considered during the innovation process. We are approachable, efficient and jargon free. Get in touch with us today to find out more about how we can help your business succeed.



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Notes

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