

R&D in the TMT sector

Within the technology, media and telecom (TMT) sector, R&D is second to none. Most European countries have R&D incentives that TMT companies can benefit from. Whether tax incentives (France, The Netherlands and Belgium) or grants and subsidies (Germany and Poland), they aim to encourage R&D investment in the country and help create new start-ups. Within TMT, the most important R&D is related to IT development.

Belgian tax law includes several measures to encourage R&D activities, among others an R&D investment deduction/tax credit, and a partial exemption of withholding tax for researchers. For these measures the starting point is: what is R&D?

The law does not provide a specific definition. But one is found in the so-called Frascati Manual. Published by the Organisation for Economic Co-operation and Development (OECD), the manual sets forth the

methodology for surveys on research and experimental development. Used as a reference by most tax authorities worldwide, it offers the following definition:

"Research and experimental development (R&D) comprise creative work undertaken on a systematic basis in order to increase the stock of knowledge, including knowledge of man, culture and society, and the use of this stock of knowledge to devise new applications."





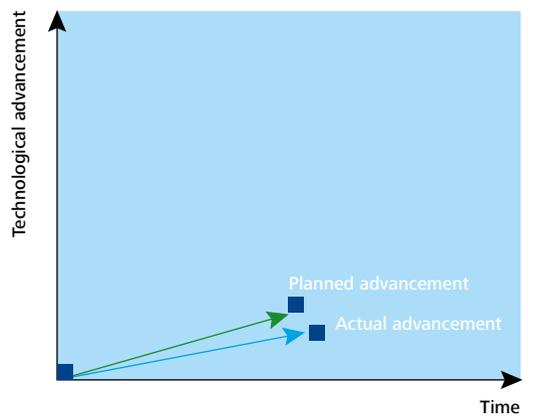
What constitutes R&D?

Based on this definition, we will examine what could constitute R&D. It covers three activities:

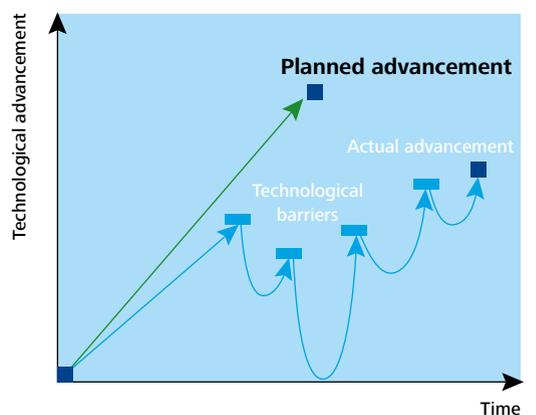
1. Basic research: experimental or theoretical work undertaken primarily to acquire new knowledge of the underlying foundation of phenomena and observable facts, without any particular application or use in view.
2. Applied research: original investigation undertaken to acquire new knowledge directed primarily towards a specific practical aim or objective.
3. Experimental development: systematic work drawing on existing knowledge, which is directed towards producing new materials, products or devices, to installing new processes, systems and services, or to improving substantially those already produced or installed.

It is important to note that R&D doesn't only occur in R&D centres. Informal R&D can also be found in other departments or business units, in particular those that support these centres.

Routine development (ineligible)



Experimental development (eligible)





Assessing eligibility

One must distinguish R&D from related activities, such as training and education. R&D should demonstrate novelty and the resolution of scientific and/or technological uncertainty. The following steps are taken to assess the eligibility of R&D activities:

- Determine, for a given project, what is the “basic stock of common knowledge” available – the **state of the art**.
- Define the **advancement** with respect to the basic stock of common knowledge. This can be expressed as “What scientific/technical capability were you trying to acquire?”
- Define the **uncertainty** and technical **obstacles** encountered during development. There can be uncertainty about the achievability of the goals and/or the means being used.
- Describe the **work performed** to overcome the uncertainty and obstacles.
- Describe the **status** of the work performed. It is not a requirement that the goal has been achieved.

Since the starting point is the state of the art, every project related to a particular technology needs to be assessed individually. Key is to determine that in your project you have gained technical knowledge not already freely available in the marketplace.

Distinguishing R&D projects from routine development can be illustrated with the following graphs:

On the left side the actual advancement has been achieved more or less as planned, without any noticeable obstacle. Hence, this would be a typical example of an ineligible routine development. If obstacles are met and iterations are required to obtain an advancement, which may be different than planned, it would be a sign that the project is an experimental development which would qualify as R&D project.

R&D and software

The Frascati Manual gives a specific focus to IT developments, which in the TMT sector represent significant investments. For software development, advances will typically be incremental rather than revolutionary.

An aggregation of individual non-R&D projects into a larger project could be eligible if it entails the resolution of some technical uncertainty.

Even if not straightforward, this analysis is a must for determining whether or not R&D tax incentives are available for projects led by the enterprise.

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