

## Incentive Guidelines

### Aid for Research and Development Projects (Tax Credit)



MALTAENTERPRISE

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# 1. Introduction

1.0.1 This incentive measure allows companies to claim tax credits on costs incurred directly or indirectly in carrying out an R&D project or projects relevant to the company's trade. Eligible projects should seek to achieve an advance in a field of science or technology through the resolution of scientific or technological uncertainty.

## 1.1 Duration of the incentive

1.1.1 These Incentive Guidelines will be active between 1st January 2017 and 31st December 2020. Malta Enterprise Corporation may periodically review, update and amend these Incentive Guidelines.

## 1.2 Legal Basis

1.2.1 Malta Enterprise is enabled to issue and publish official Incentive Guidelines in terms of Article 8(3)(a) of the Malta Enterprise Act, Chapter 463 of the Laws of Malta.

1.2.2 Assistance for Research and Development and Innovation Regulations is a Subsidiary Legislation 463.05 to the Malta Enterprise Act Chapter 463 of the Laws of Malta enables the support described in these Incentive Guidelines.

## 1.3 Designated Authority

1.3.1 This incentive is administered by Malta Enterprise Corporation (hereinafter referred to as the 'Corporation').

## 2 Definitions

### 2.1 R&D activity

- 2.1.1 An R&D activity is an activity directly or indirectly contributing to seeking advances in science or technology. Such activity should be taken as part of a set of tasks that can be defined as industrial research or experimental development which addresses a scientific or technological uncertainty.
- 2.1.2 An R&D activity should directly contribute towards scientific or technological advances through the resolution of scientific or technological uncertainty.
- 2.1.3 Indirect activities which contribute to the resolution of the project's scientific or technological uncertainty may also be considered as R&D activities.
- 2.1.5 Even if the advancement in science or technology sought by a project is not achieved or not fully realised, R&D still takes place. It is understandable that an R&D project carried out with the intention to achieve an advance in science or technology may fail to achieve its aims.
- 2.1.6 The design, construction, and testing of prototypes shall fall within the scope of R&D until any scientific or technological uncertainty related with the prototype has been resolved. Further work following the resolution of the scientific or technological uncertainty will not be R&D.
- 2.1.7 Design activities are only considered as an R&D Activity if the objectives of the design require the resolution of scientific or technological uncertainty.
- 2.2.3 R&D activities include the use science or technology to produce a product, process, device or material that provides the same purpose of an existing produce but is achieved in a fundamentally different manner to the existing product, process, device or material.
- 2.1.8 The use of science and technology in the development of a process, material, device, product, or service does not constitute R&D.
- 2.1.9 A product or process which is innovative does not necessarily constitute a scientific or technological advance. The product, process, or functionality etc. being developed is usually not good indicators of whether the actions carried out qualify as R&D activities.
- 2.1.10 R&D activities do not include work in the arts, humanities and social sciences (including economics).

## 2.2 Advance in Science or Technology

- 2.2.1 An advance in science or technology results in the creation of new knowledge or capabilities in a field of science or technology (not simply in the company's own knowledge capacity).
- 2.2.2 This includes the adaptation of scientific and technological knowledge or capabilities from other fields of science or technology to a new application where such an adaptation is not readily deducible.

## 2.3 Scientific or technological uncertainty

- 2.3.1 In principle a scientific or technological uncertainty refers to a situation to which no existing scientific or technological solutions are known. This includes instances where others may have already tried and failed to resolve these uncertainties or may have resolved the uncertainties, but how this was achieved is not of public domain.
- 2.3.2 Scientific or technological uncertainty may also arise from the development of an established scientific certainty into a cost-effective, reliable and reproducible process, material, device, product or service. (In some industries this may be referred to as scaling-up).
- 2.3.3 If an uncertainty can be readily resolved by a competent professional working in the field then it is not a scientific or technological uncertainty. Furthermore, improvements, modifications and optimisations which do not affect the science or technology in the product, process or service do not constitute work to resolve scientific or technological uncertainty.
- 2.3.4 Scientific or technological uncertainty could also occur due to the complexity of a system rather than its individual components. (This is sometimes referred to as system uncertainty). This could include, work on combining technologies, devices, and/or processes where a competent professional working in the field cannot readily deduce how the separate components should be combined to achieve the intended function.

## 2.4 Activity Directly Contributing to an R&D Activity

- 2.4.1 An activity that directly contributes to R&D Activity must be such that its outcome is an attempt to resolve an element of the scientific or technological uncertainty associated with the advance being sought.

## 2.5 Activity Indirectly Contributing to an R&D Activity

- 2.5.1 These are activities which are an integral part of a project but do not directly contribute to the resolution of the scientific or technological uncertainty. These activities are:
  - a) Reporting, documenting and similar information services, insofar as they are conducted for the purpose of R&D support (such as the preparation of reports on the R&D findings).
  - b) Activities required for the carrying out of the R&D Activity (e.g. taking on and paying staff, accounting for R&D costs and procurement, security services related to laboratories and maintaining research and development equipment);

- c) Training required to directly support an R&D project; and
- d) Research (including data collection and data mining) required to plan scientific or technological testing, survey, or sampling methods. (This activity is not R&D in its own right).

## 2.6 Industrial research

2.6.1 'Industrial research' means the planned research or critical investigation aimed at the acquisition of new knowledge and skills for developing new products, processes or services or for bringing about a significant improvement in existing products, processes or services. It comprises the creation of components parts of complex systems, and may include the construction of prototypes in a laboratory environment or in an environment with simulated interfaces to existing systems as well as of pilot lines, when necessary for the industrial research and notably for generic technology validation.

## 2.7 Experimental Development

2.7.1 'Experimental Development' means acquiring, combining, shaping and using existing scientific, technological, business and other relevant knowledge and skills with the aim of developing new or improved products, processes or services. This may also include, for example, activities aiming at the conceptual definition, planning and documentation of new products, processes or services.

2.7.2 Experimental development may comprise prototyping, demonstrating, piloting, testing and validation of new or improved products, processes or services in environments representative of real life operating conditions where the primary objective is to make further technical improvements on products, processes or services that are not substantially set. This may include the development of a commercially usable prototype or pilot which is necessarily the final commercial product and which is too expensive to produce for it to be used only for demonstration and validation purposes.

2.7.3 Experimental development does not include routine or periodic changes made to existing products, production lines, manufacturing processes, services and other operations in progress, even if those changes may represent improvements.

## 2.6 Small and Medium Sized Enterprises SMEs

2.6.1 An SME is an undertaking which fulfils the criteria laid down in Annex I of Commission Regulation (EU) No 651/2014 of 17 June 2014 declaring certain categories of aid compatible with the internal market in application of Articles 107 and 108 of the Treaty (hereinafter referred to as the General block exemption Regulation)

## 2.7 Large Enterprises

2.7.1 A large enterprise is an undertaking not fulfilling the criteria laid down in Annex I of the General block exemption Regulation.

## 2.8 Competent professional

2.8.1 A 'competent professional' is a person working in his field of expertise that is expected to:

- a) be knowledgeable about relevant scientific and technological principles;
- b) be aware of the current state of technology and knowledge;
- c) have experience in the relevant field of science and technology.

2.8.2 By having been simply engaged in the relevant field of work or by having an intelligent interest in it does not, by itself, make a person a competent professional.

## 2.9 Incentive Entitlement Certificate

2.9.1 An Incentive Entitlement Certificate (IEC) means a certificate issued in terms of Part VI of the Malta Enterprise Act, outlining the support granted and including any relative terms and conditions.

## 2.10 Tax Credit Certificate

2.10.1 A Tax Credit Certificate is a document issued by the Corporation specifying the amount of tax credit has been awarded to a beneficiary as would have been approved in the Incentive Entitlement Certificate.

2.10.2 The Tax Credit Certificate shall include the terms and conditions linked to the credit provided and how it may be used.

2.10.3 The Tax Credit Certificate may be used to deduct Income Tax payable. The value of the Certificate is consequently recorded in the income tax return of the company and a running balance is maintained to track any unutilised tax credits.

2.10.4 A Tax Credit Certificate awarded under this Incentive Guidelines does not give rise to a right of any tax refund.

## 2.11 Undertaking in Difficulty

2.11.1 Undertakings in difficulty defined in terms of the Commission Regulation (EU) No 651/2014 of 17 June 2014. Such firms are excluded from benefiting from assistance under this incentive.



## 3. Incentive Description

### 3.1 The Incentive

- 3.1.1 This incentive provides a tax credit to registered companies that carry out a Research Activity. The tax credit shall be calculated by establishing the eligible costs and the size of the undertaking that may be used to deduct Corporate Income Tax.

### 3.2 Eligible Undertakings

- 3.2.1 This measure is available to limited liability companies registered under the [Companies Act \(Chapter 386 of the Laws of Malta\)](#), with the exclusion of undertakings in difficulty as defined in Article 2 of the [General Block Exemption Regulation](#).
- 3.2.2 Undertakings whose line of business is that of conducting R&D activities under contractual agreement to third parties are not eligible for this incentive. This exclusion does not include instances where a group of companies has a reached arm (company) that carries out research on behalf of other linked companies with the group.

### 3.3 Eligible R&D Projects

- 3.3.1 The supported R&D Activity must be identified in specific projects that seek to address a scientific or technological uncertainty and which can fall with the definitions of Industrial Research or Experimental Development.
- 3.3.2 The commencement of an R&D projects supported under this incentive may not be prior to the 1<sup>st</sup> of January 2017. An R&D project begins when work to resolve the scientific or technological uncertainty starts and ends when that uncertainty is resolved or work to resolve it ceases.
- 3.3.3 The project or projects carried out must relate to your company's current trade activity or to a trade activity that the company intends to start based on the results of the R&D activity.
- 3.3.4 A company claiming the tax credit must own any intellectual property that might arise from the R&D Activity claimed.

### 3.4 Aid Intensities

- 3.4.1 Beneficiaries that carry out an eligible R&D activity will receive a tax credit calculated at twenty five percent (25%) of the eligible expenditure.
- 3.4.2 The percentage shall be increased by 10% when the applicant is a medium sized enterprise and by 20% when the applicant is a small enterprise.
- 3.4.3 The total support shall be limited to EUR 15 million for any project cover by the R&D activity.

## 4. Qualifying Costs

4.0.1 The project or projects carried out must relate to the company's current trade activity or to a trade activity that the company intends to start based on the results of the R&D activity.

4.0.2 Costs related to prototypes that are sold to third parties following the completion of a project are not considered eligible.

### 4.1 Qualifying Employee costs

4.1.1 Staffing cost of directors and employees actively engaged on an eligible R&D activity can be considered as qualifying expenditure. (When a director or employee is not fully engaged actively on an eligible R&D activity, then only the proportion on which the person is engaged actively on an eligible R&D activity shall be considered as qualifying).

4.1.2 Employee costs may be considered when a person is directly or indirectly contributing to the R&D Activity. A person's extent of engagement in the R&D Activity is based on the duties performed in relation to the activity and not on the job title. It is therefore not possible to establish a list of eligible role as in many cases employees (especially support staff) are only partly engaged in R&D Activity.

4.1.3 To directly contribute to an R&D Activity, the persons must be engaged in attempting to resolve an element of scientific or technological uncertainty. This would include activities:

- a) aimed to create or adapt software, materials or equipment needed to resolve the scientific or technological uncertainty, provided that the software, material or equipment is created or adapted solely for use in R&D; and
- b) of planning, design, testing and analysis undertaken to resolve the scientific or technological uncertainty.

4.1.4 To indirectly contribute to an R&D activity the persons must be engaged in:

- a) carrying out feasibility studies to support and define the strategic direction of a specific R&D Activity;
- b) research (where this research is not R&D in its own right) to devise new scientific or technological testing, survey, or sampling methods;
- c) providing information services, insofar as they are conducted for the purpose of R&D Activity;

4.1.5 Supporting activities such as maintenance, training, security, administration, finance and personnel activities, insofar as these activities are carried out for the purposes of an R&D activity.

4.1.6 Staff costs may only be claimed in respect to employees who are covered by a contract of employment and registered as employees of the company claiming the benefit. Only the following costs shall be considered as eligible:

- a) the emoluments paid by the company to its directors or employees prior to any tax or social security deduction collected by the company from the directors or

- employees on behalf of the Government, insofar that only salaries, wages, and predetermined fixed cash benefits shall be considered as eligible; and
- b) the compulsory Social Security contributions paid by the company.

4.1.7 It is understandable that some groups entrust one group company to employ all the staff for the group, and recharge other group companies for their services. Since the company claiming under this measure is recharged for the use of employees from another group company these costs cannot be considered directly as the claimant's own staffing expenditure. In such instances, the value of eligible costs should be established as a function of the actual staff costs based on the remuneration received by the staff engaged in the R&D Activity.

#### 4.2 Contracted R&D expenditure

4.2.1 Costs of contractual research purchased for enterprises as well as costs of consultancy and equivalent services used exclusively for the research activity may be claimed as long as the transactions are conducted at arm's length conditions.

4.2.2 Contracted R&D costs may not exceed 20% of total costs claimed in respect of a specific R&D project.

#### 4.3 Materials and Utilities

4.3.1 Costs for the procurement of materials used directly, thus consumed or transformed in the process of carrying out of an R&D activity, is eligible for these tax credits. Such materials must consequently be no longer so useable in their original form following the R&D activity.

4.3.2 Eligible materials would include: chemical products transform through the R&D process (even if the resultant chemical product may be recycled and used for a purpose that is not its original purpose); electronic components which may not be used for other purpose following the use in the project; and components required for a prototype.

4.3.3 Costs for the procurement of water and power.

4.3.4 Telecommunication costs are not considered as eligible costs unless the transmission of information over a telecommunications network is an integral part of a research project.

4.3.5 In instances where materials and utilities are only partly directly utilised in R&D an appropriate apportionment of the expenditure should be established. This calculation will depend significantly on the particular R&D activity and on other parameters such as the facility and the number of employees. A practical approach should be adopted to establish an adequate apportionment which should be backed by reasonable arguments justifying the approach and methodology adopted.

#### 4.4 Software

4.4.1 Software As A Service (SAAS) costs are considered as eligible expenditure to the extent that the software is used directly for the R&D Activity. If the SAAS is partially used for in R&D, the cost should be apportioned to reflect the cost in respect to the R&D Activity.



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- 4.4.2 Costs for the purchase of Software procured specifically for the R&D activity and which will have no use following the completion of the specific R&D project or projects for which it is purchased are eligible.
- 4.4.3 Software costs which are considered by as amortisable or registered in the fixed asset register of a company are not eligible.

## 5. Claims

- 5.0.1 Before claiming, read these Incentive Guidelines.
- 5.0.2 You must claim the R&D tax credits within two years of the end of the relevant fiscal year in which the activities were carried out.

### 5.1 Collating all the Information required to submit a claim

- 5.1.1 As a first task to compiling a claim for tax credits covering your R&D activity you should gather the relevant information about your R&D project or projects. In compiling your claim you will require:
  - a) Facts that demonstrate that the project qualifies as a R&D activity as defined in these Guidelines.
  - b) Calculations showing how the eligible R&D expenditure was established.
  - c) Information of other partnered and linked enterprises so that you may determine the size of your enterprise.
- 5.1.2 The claim document submitted to Malta Enterprise should include a report endorsed by a certified auditor and a person competent in the area of science and technology which is relevant to your project or projects. The report shall include the following sections:
  - a) A confirmation that the project is R&D, explaining the scientific or technological advance is being sought. In confirming that the project constitutes an R&D activity it is recommended that you refer to the definitions provided in these Incentive Guidelines and to the [Frascati Manual](#). To determine eligibility, it is suggested that your focus on the scientific or technological advance is being sought.
  - b) An explanation why the knowledge being sought, is not readily deducible by a competent professional.
  - c) A description of the methods adopted to overcome the uncertainties and the investigations and analysis undertaken. This should not be in great detail, but simply sufficient to show that the matter was not straightforward. A description of the successes and failures and the impact of these on the overall project. If the uncertainties were not overcome, explain what happened.
  - d) An explanation on how the eligible R&D expenditure was established. It is not a requirement to keep time sheets and usage logs (although this might facilitate establishing the R&D expenditure) yet an explanation of how the costs were determined accompanied by a reasoned positive opinion issued by a certified auditor should be included in the report.

## 6. Approval and Review

### 6.1 Approval

- 6.1.1 Following a positive review of a claim the Corporation shall issue an Incentive Entitlement Certificate and a Tax Credit Certificate. The awarded Tax Credit may be claimed in the tax return from the year of assessment immediately following the year in which the relative expenditure is incurred. The Tax Credit Certificate may only be used against tax due and may not be used to settle any pending tax payments.

### 6.2 Monitoring

- 6.2.1 Applicants will be subject to monitoring to ensure that the project is being or was implemented according to:
- a) These Incentive Guidelines.
  - b) The terms and conditions set in the Incentive Entitlement Certificate issued by the Corporation.
  - c) Commission Regulation (EU) No 651/2014 of 17 June 2014.

### 6.3 On-Site Verifications

- 6.3.1 Malta Enterprise may carry out or commission third parties to carry out on-site checks during the implementation period or up to five years from completion of the project in order to verify the implementation of the project, its consistency with the submitted documentation and the actual works carried out. Such visits may also entail a review of the tax credit claimed in relation to the documentation held in the project file.

### 6.4 Record Keeping

- 64.1 All documentation must be kept for at least ten (10) years from the date on which the aid is granted.

### 6.5 Sanctions and recovery of aid

- 6.5.1 The Corporation may revoke, amend or modify the Incentive Entitlement Certificate and apply penalties or request recovery of aid in the case of breach of these Guidelines or the conditions set down in the Incentive Entitlement Certificate.

## 7 State Aid Rules and Obligations

### 7.1 Applicable State Aid

7.1.1 The terms and conditions set out in these guidelines are in line with the Commission Regulation (EU) No 651/2014 of 17 June 2014, declaring certain categories of aid compatible with the internal market in application of Articles 107 and 108 of the Treaty 4.

7.1.2 The incentive is not applicable to the following:

- a) Activities listed down in Article 1 (2), (3), (4) and (5) of Commission Regulation No 651/2014 of 17 June 2014.
- b) Undertakings in difficulty defined in terms of the Commission Regulation (EU) No 651/2014 of 17 June 2014. Such firms are excluded from benefiting from assistance under this incentive. Aid shall not be granted for training which undertakings carry out to comply with national mandatory standards on training.

7.1.3 Furthermore, assistance may not be granted if the aid is:

- a) related to export activities towards third countries or Member States, namely aid directly linked to quantities exported, to the establishment and operation of a distribution network or to the other current expenditure linked to export activity.
- b) A contingent upon the use of domestic in preference to imported goods.
- c) in favour of a beneficiary which is subject to an outstanding recovery order following a previous Commission decision declaring an aid illegal and incompatible with the internal market should be excluded from the scope of this Regulation.

### 7.2 Rules on Cumulation of Aid

7.2.1 Rules on Cumulation of aid shall be in line with Article 8 of the Commission Regulation (EU) No 651/2014 of 17th June 2014.

## 8. Further information

- 8.0.1 If you have any queries or require any clarifications related to these Incentive Guidelines please contact your relationship manager at Malta Enterprise. If you have not been appointed a relationship manager or you are unsure who your relationship manager is, we advise you to contact Business First to be guided accordingly.

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- 8.0.2 You may also find further information on these Websites:

<http://www.maltaenterprise.com>

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