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Tax incentives on Research and Development (R&D)

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Branch Reporters
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Summary and conclusions

Austrian tax law has been providing tax incentives for R&D for more than 30 years. Already in 1980 a tax allowance, the predecessor of the current tax credit, was introduced. The reason why the Austrian legislator introduced and still offers R&D incentives for its taxpayers has always been to enhance R&D activities in Austria. Furthermore, nowadays direct funding is decreasing and most of it goes to public institutions. A huge part of the Austrian economy is constituted by small and medium-sized enterprises (SMEs); such companies often struggle to provide funds for (extensive) R&D activities. The Austrian legislator perceives tax incentive to be a good stimulus to enhance R&D, especially among such companies.

Of the various R&D tax incentives, the most important one is the R&D tax credit. This incentive is available to a wide range of taxpayers creating business income. It provides for a tax credit of 10 per cent of qualifying R&D expenses for self-performed R&D in an Austrian trade or business or permanent establishment. Furthermore, a 10 per cent tax credit can also be applied for contracted R&D. This tax credit is, however, limited to an assessment basis of 1 million euro and can only qualify if the contractor (conducting the R&D) is located within the EU or EEA. The tax credit is granted by way of a credit to the taxpayers' tax account and can either be paid out or credited against (future) tax liabilities. The Austrian understanding of R&D for the application of the tax credit is widely based on the OECD Frascati Manual. Both forms of the tax credit have certain limitations with regard to a domestic or EU/EEA nexus.

Additionally the Austrian (personal) income tax law offers a reduced tax rate for inventors obtaining income from the exploitation of patented inventions. However, this tax incentive is only available for individual taxpayers.

The Austrian tax law also offers a tax relief for researchers relocating to Austria.

Tax incentives in Austria only focus on so-called "input R&D fiscal incentives". Output R&D fiscal incentives, such as a patent box regime, do not exist in Austria and have not been the subject of broad discussions so far. The available tax incentives are available for a large range of taxpayers. There are, however, requirements especially for the tax credit and the reduced income tax rate that may be questionable

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in the light of the constitutional principle of equality, EU law or with regard to concluded double tax treaties (DTCs).

Due to the huge efforts the OECD is currently putting into the OECD base erosion and profit shifting (BEPS) project, this branch report also deals with the transfer of intellectual property (IP) to other jurisdictions and the payment of royalties to low-tax jurisdictions and intermediary IP companies. In this context it should not be left unmentioned that Austria has just recently limited limitation denying the deductibility of intra-company royalty (and interest) payments to companies located in low-tax jurisdictions.

1. R&D Incentives under domestic tax law

1.1. Introduction

The first section of this report deals with a detailed overview of the tax incentives Austria is offering with regard to R&D activities. After a general overview of Austrian business income taxation, the report will deal with tax policy considerations with regard to why such incentives were introduced, who is eligible to apply for them, whether there are any limitations or concerns (e.g. from a constitutional point of view) and finally what the Austrian legislator understands R&D to be. The last part of this section will offer a detailed description of the tax incentives currently available.

1.2. Brief overview of business income taxation

Depending on the qualification of the person generating the income, business income is either subject to Austrian personal income tax (PITA)[1] or Austrian corporate income tax (CITA).[2] PITA applies to individuals and all corporate forms that are not subject to CITA. The most relevant corporate forms subject to CITA are the *Aktiengesellschaft, Gesellschaft mit beschränkter Haftung, Privatstiftung.*

When it comes to partnerships, Austria applies a look-through approach, i.e. the income is taxed in the hands of the partners. Hence, the income of corporate partners of a partnership is subject to CITA, the income of individual partners is subject to PITA.

Income subject to PITA is generally subject to a progressive income tax rate of up to 50 per cent; however, certain income, especially most capital income, is taxed at 25 per cent. The CITA rate is 25 per cent. Dividends paid to individuals by a corporation are subject to a 25 per cent withholding tax.

Corporations with a legal seat or effective management in Austria are subject to unlimited tax liability in Austria (i.e. worldwide income is subject to Austrian tax). For PITA a domicile or the habitual abode in Austria triggers unlimited tax liability.

1 *Einkommensteuergesetz* 1988 (PITA).
2 *Körperschaftsteuergesetz* 1988 (CITA).

As regards the computation of the business income, the rules of PITA are relevant for computing income under CITA as well, unless CITA provides for specific rules (e.g. participation exemption regime, limited deductibility of intercompany interest and royalty payments made to low-tax countries, seven-year distribution of current-value depreciations of participations). In general all expenses triggered by acquiring, securing and maintaining taxable income are deductible. The deductibility of expenses is generally limited or declined, where a relationship to the personal sphere of the taxpayer exists and as regards luxurious or recreational expenses. The CITA has several limitations with respect to intercompany payments. Profit distributions by a corporation and deposits by its shareholders are disregarded for the profit/loss of the corporation. Only the arm's length outcome of transactions between a corporation and its shareholders (and related parties) are taken into account for tax purposes.

In general there is no limitation for the deductibility of R&D expenses. Intangible assets (e.g. software, goodwill) can only be activated if they were acquired from a third party, i.e. self-developed IP must not be activated.

Losses related to business income can generally be carried forward indefinitely. However, individual taxpayers calculating their tax gain on a cash basis (*Einnahmen-Ausgaben-Rechner*)[3] can only carry forward losses up to three years.[4] There used to be a general limitation regarding the deduction of losses of 75 per cent of the taxable profit of the respective year. However, this limitation was abolished for the tax years 2014 and following for taxpayers who are not subject to corporate income tax.[5] Losses cannot be carried back.[6]

In order to be of relevance for tax purposes a business activity must result in a total taxable profit in the long run. If an activity does not produce taxable profits within the first three to five years, an assessment has to be made as to whether a total gain can be expected. If an overall profit cannot be expected, tax losses resulting from this activity must not be deducted for tax purposes. Losses caused by activities which are in relation to the private sphere of the taxpayer or his personal bias will generally only be tax deductible if the realization of a total profit is possible within a foreseeable timeframe and this can be substantiated.[7]

1.3. Tax policy considerations relating to R&D incentives

1.3.1. General tax climate for R&D

Austrian tax law provides for certain tax incentives for R&D activities. On the one hand taxpayers can obtain a tax credit from their R&D expenses and additionally individual taxpayers can benefit from a reduced income tax rate on the exploitation of inventions. Furthermore, there is a tax relief available for researchers relocating to Austria.

[3] In general only available for rather small businesses.
[4] See s. 18 para. 7 PITA.
[5] See s. 8 para. 4 subpara. 2 CITA; s. 2 para. 2b PITA.
[6] See Austrian Supreme Administrative Court 13 February 1991, 86/13/0120; 7 November 1989, 89/14/0136.
[7] See *Liebhabereiverordnung*, BGBl 1993/33. This limitation, however, is generally not of high relevance for corporations.

Generally the reporters deem the tax climate for R&D in Austria to be a positive one, especially as R&D related expenses can generally be deducted and the tax credit is widely available. However, there are obstacles such as the recently introduced limitation on the deductibility of royalty payments to intra-group companies subject to low tax on this income.[8] Furthermore, for obtaining the tax credit (for self-conducted R&D) the taxpayer now has to obtain a positive expert opinion[9] by the Austrian Research Promotion Agency *(Forschungsförderungsgesellschaft* (FFG)) as to whether his R&D activities qualify as R&D in the sense of the provisions for the tax credit. Additionally, as R&D activities often go hand-in-hand with losses in the first years (during the research period), one has to take the Austrian rules regarding tax losses into account (please see section 1.2 above).

1.3.2. Reasons for introducing R&D incentives

The main reason for introducing R&D incentives in Austria has always been to promote R&D activities in Austria.[10] This is clearly reflected in the requirement of an Austrian trade or business or permanent establishment (performing or delegating the R&D) when obtaining the tax credit, which aims at increasing R&D expenses in the books of Austrian businesses.[11]

In general Austria offers various types of R&D incentives and funding. However, direct funding mostly benefits the public R&D sector, whereas very little government funding is available for the corporate sector. One could argue that this is another reason for introducing indirect tax incentives, as direct funding is decreasing and indirect tax incentives are more easily obtainable for the corporate sector.[12]

From the reporters' practical experience Austrian businesses see a lot of advantages in a tax credit as opposed to direct funding. A very important point is that the taxpayer has a legal entitlement to the tax credit if his R&D activities meet the definition and requirements. Even if the FFG's expert opinion and the following decision of the tax authorities is negative (see section 1.6 below), the taxpayer can appeal against such a decision and bring the issue to the courts. A decision of a committee regarding direct funding is generally final and an applicant does not have a legal entitlement to such funding. Especially if the requirements are fulfilled, the chance of obtaining the tax credit is much more predictable for the applicant than is obtaining a direct funding. Additionally the possibility of an advanced ruling for larger or long-term R&D projects provides a lot of planning security for entrepreneurs. Last but not least, there is no maximum amount for claiming the tax credit for self-conducted R&D.

8 See section 2.4.3 below for details.

9 See more details regarding the application process in section 1.6.

10 See for example the accompanying materials to the government bill of the *Wirtschafts- und Beschäftigungsgesetz* 2005, 992 d.b., 5; Schneider, *Steuerliche Begünstigung von Forschung und Entwicklung*, 2014, 1 *et seq.*

11 See criticism in section 2.2.2.1 below.

12 See WIFO, *Systemevaluierung der österreichischen Forschungsförderung und -finanzierung*, 2009, available at: http://www.bmvit.gv.at/service/publikationen/innovation/forschungspolitik/downloads/ systemevaluierung/report8.pdf.

1.3.3. R&D incentives, equality of treatment and ability to pay

One of the main principles of the Austrian tax law is the ability to pay.[13] This principle might be one way to justify the limitation of the reduced income tax rate to individual taxpayers: corporate taxpayers are subject to a fixed tax rate of 25 per cent. On the other hand, individual taxpayers are subject to a progressive tax rate of up to 50 per cent. Due to inventors often being in the situation of several years without any (substantial) income, followed by periods of aggregated income, their income tax rate might be substantially higher in the years income is generated as the aggregation of income increases the (progressive) average tax rate in these years. Hence, from an overall view corporate taxpayers would be better off, as they might also be able to better offset cumulated losses.

The reduced tax rate for inventors requires a registered patent.[14] Referring to the constitutional principle of equality, it has been questioned in the past whether the requirement of a registered patent can be the correct link for such an incentive. In certain cases inventions might not be patentable[15] and as a consequence prevent the inventor from obtaining the tax incentive. Hence, this requirement might not be in line with the principle of equality.[16]

As regards the tax credit Kühbacher criticizes the limitation of R&D contracted to the EU and the EEA. Based on the reasoning of the ECJ in *Laboratoires Fournier SA* the author argues that due to this limitation an Austrian company contracting R&D to an institution in a third country is discriminated against as compared to an Austrian company contracting its R&D work to an institution within the EU or EEA.[17] Kühbacher also criticizes the fact that self-conducted R&D has to be performed in an Austrian trade or business or permanent establishment. Where Austria extends its taxing rights to the foreign business[18] an Austrian company conducting its research abroad will be in a comparably unfavourable situation as it cannot apply for the tax credit.[19] However, according to the reporters' knowledge this issue has not yet been brought to the notice of the Constitutional Court in Austria.

1.3.4. Eligible taxpayers

The reduced tax rate for exploitation of inventions is only available for individual taxpayers. Corporate taxpayers are not eligible for a reduced rate on such income. However, contrary to the CITA income subject to personal income tax is taxed at a

[13] See Doralt and Toifl in Doralt *et al.*, *EStG*, 2013, s. 2 MN1; however, opinions about this principle in the literature are very different, see Laudacher in *Jakom Einkommensteuergesetz*, 2014, s. 2 MN 2 *et seq.*

[14] See details in section 1.4.1 below.

[15] For example plant varieties, animal species, or surgical or therapeutic methods are not patentable in Austria; see Doralt in Doralt *et al.*, *EStG*, 2007, s. 38 MN 5.

[16] See Stelzer, "Gleichheitsrechtliche Aspekte der Rücknahme steuerlicher Begünstigungen am Beispiel des §38 Abs 4 EStG", ÖStZ 1988, 194.

[17] See Kühbacher, "Ist in einen Drittstaat vergebene Auftragsforschung ebenfalls prämienbegünstigt?", SWK 2014, 705.

[18] In the case of treaties where the credit method is applied, or in cases where no treaty exists with the other country.

[19] See Kühbacher, "Ist der Inlandsbezug bei der Forschungsprämie zulässig?", SWI 2014, 484.

progressive tax rate of up to 50 per cent. Furthermore, unlike taxpayers subject to unlimited tax liability in Austria, foreign taxpayers subject to limited tax liability (e.g. maintaining a permanent establishment in Austria) are generally not eligible for the reduced income tax rate; there might, however, be a possibility for them to opt into unlimited tax liability (please see section 2.2.2 below for a more detailed discussion).

The R&D tax credit of 10 per cent of R&D expenses is generally available for all taxpayers who do not calculate their tax income based on lump-sum taxation (i.e. a standard percentage of expenses is deducted from the income in order to calculate the tax basis).[20] However, self-conducted R&D must be performed in an Austrian business or permanent establishment. The principal of contracted research must be an Austrian trade or business or permanent establishment. Contracted research can only qualify for the R&D tax credit if the contractor is a company or facility having its seat within Austria or the EU or the EEA.

1.3.5. R&D incentives: multinational enterprises (MNEs) versus SMEs?

Some (tax) benefits seem to be more easily obtainable by MNEs than by SMEs. In particuar, the compliance costs to obtain the positive expert opinion required for the R&D tax credit may prevent SMEs from applying for this tax incentive. The current Austrian regulations regarding the tax credit for R&D, however, do not in general distinguish between different taxpayers (with regard to the size of the company). Still, the introduction of a tax allowance (now tax credit) for contracted R&D in 2005 was driven by the awareness that SMEs generally perform less R&D work. In order to enhance R&D also in the SME sector, the Austrian legislator provided for an allowance for contracted R&D, as SMEs often cannot provide the funds for setting up a separate R&D department.[21]

1.3.6. Definition of R&D for tax purposes

The definition of R&D in the currently applicable regulations for the tax credit was mainly based on the OECD Frascati Manual. According to section 108c paragraph 2 PITA R&D is defined as “research and experimental development, which is performed systematically and with the aid of scientific methods in order to increase the stock of knowledge and the use of this stock of knowledge”. So far the definition as used in section 108c paragraph 2 PITA is very similar to the definition outlined by the Frascati Manual.[22] In order to further narrow the definition the Austrian Ministry of Finance has adopted the terms basic research, applied research and experimental development and their definitions as given in the Frascati Manual in the regulation *Forschungsprämienverordnung*, which provides further details to

[20] See Administrative Guidelines to the Austrian PITA, MN 8208.

[21] See accompanying materials to the government bill of the *Wirtschafts- und Beschäftigungsgesetz* 2005, 992 d.B., 5.

[22] See OECD Frascati Manual 2002, MN 63. According to the accompanying materials the Frascati Manual should be addressed if questions regarding the interpretation of the Austrian regulation arise. See accompanying materials to the government bill of the *Konjunkturbelebungsgesetz* 2002, 977 d.B., 12 *et seq.*; Heitzinger and Silber, *Forschungsfreibeträge und Forschungsprämie*, 2003, 26 *et seq.*

section 108c PITA in several areas.[23] Hence, the understanding of R&D generally ends at the stage of experimental development. Stages in the development of a new product such as the start of production, introduction into the market and diffusion (which can also be very innovative) are usually not covered by the definition.[24]

The reduced tax rate for inventors uses a very different approach. It does not relate to the OECD Frascati Manual or any comparable definition. The term "invention" is not defined in the PITA. As the provision requires an invention that is protected by a patent, the definition of the *Patentgesetz* is used.[25] According to section 1 paragraph 1 *Patentgesetz* inventions in all areas of technology are patentable, if they are new and if they would not obviously emerge out of the state of the art for a professional and if they are commercially useable.

1.4. R&D input incentives

1.4.1. General overview of R&D input incentives

Austrian tax law provides for the possibility to apply for a tax credit for self-conducted and contracted R&D. Additionally, income resulting from the exploitation of patented inventions subject to the PITA can make benefit of a reduced tax rate.

The PITA provides for tax reductions for income generated by personal inventions, i.e. only the inventor himself can benefit from this reduction. For income from the exploitation (e.g. licence payments, sale of the patent) of inventions protected by a registered patent[26] the income tax rate is reduced by 50 per cent of the average tax rate of the taxpayer. Additionally to the requirement of a registered patent a further criterion for this tax incentive is that the inventor must not exploit the invention himself. This tax reduction also applies if the invention is exploited outside of Austria, in which case the patent has to be registered in Austria or the country of exploitation.[27]

Section 103 PITA offers a tax privilege for persons relocating their residency to Austria, if this relocation benefits science, research, arts or sports. According to the clarifying regulation issued by the Ministry of Finance this regulation applies to researchers whose compensation can be considered for the assessment basis of the tax credit for R&D by the payer of the compensation. The regulation either leads to an exemption of foreign income that would otherwise be subject to Austrian taxation as well or to a reduced income tax rate on the income.[28]

According to section 67 paragraph 7 PITA employees receiving remuneration for making an invention by coincidence (i.e. their main job is not making inventions, or working in the R&D department) or making improvement suggestions can

[23] See *Forschungsprämienverordnung*, BGBl II 515/2012.
[24] See Schneider, *op. cit.*, 16 *et seq.*
[25] See Doralt in Doralt *et al.*, *EStG*, 2007, s. 38 MN 3.
[26] The patent must be registered. A duly filed pending registration is considered to be sufficient. A withdrawn registration for a patent does not qualify. See Wiesner, Grabner and Wanke, *EStG*, s. 38 MN 4 and 14.
[27] See Administrative Guidelines to the Austrian PITA, MN 7350.
[28] See Marschner in *Jakom Einkommensteuergesetz*, 2014, s. 103.

also benefit from a reduced taxation on this income if a registered patent protects the invention.

Furthermore, in section 108c PITA the Austrian tax law also offers the possibility of a tax credit of 10 per cent of R&D expenses. This tax credit is available to most taxpayers (including those subject to the CITA) and can be obtained regardless of whether the performed R&D activity is successful or not or abandoned before the final stage.

Contrary to the PITA the CITA does not provide for any special rules regarding income from inventions. Due to the fact that as a general rule R&D activities often generate royalty income it should be mentioned that with effect of 1 March 2014 intercompany royalty (and interest) payments to companies with an effective tax rate below 10 per cent on this income cannot be deducted for CITA purposes (see section 2.4.3 below for details).[29]

As an additional note it should be mentioned that there are certain additional measures in the Austrian tax laws, which indirectly can lead to an incentive for or promotion of R&D activities. An important one is the deductibility of donations for certain purposes and to certain institutions and organizations (among others universities, institutions solely engaged with certain research or teaching activities, etc.) of up to 10 per cent of the tax gain of the respective year.[30] Furthermore, income of non-profit, charitable or clerical organizations is comprehensively tax exempt and there is also a reduced VAT rate applicable for such organizations.[31]

1.4.2. Privileged R&D expenditures

Expenses relating to self-conducted R&D can qualify for a tax credit of 10 per cent of these expenses. Qualifying expenses are:[32]

- salaries and wages of employees engaged in R&D. If the employees' activities are not limited to R&D activities, only parts of their salaries or wages can be taken into consideration for computing the tax credit (e.g. based on time recordings of the respective employee). Contributions for social security and other personnel expenditures (e.g. voluntary social benefits) can also be included for computing the tax credit;
- immediate expenses for R&D as well as immediate investments for R&D as long as these are sustainably used for R&D. Expenditures for any fixed assets that are subject to depreciation have to be included in the basis for the tax credit in the year of acquisition at full acquisition costs. The taxpayer must not consider the depreciation in the basis for the tax credit. If assets are used only partly for R&D purposes, the expenses relating to this asset can only be considered partly. If for example a new four-storey building is built, one floor of this building will be used for R&D activities. Hence 25 per cent of the

29 See s. 12 para. 1 subpara. 10 CITA.

30 See s. 4a PITA.

31 See s. 5 para. 6 CITA; s. 10 para. 2 subpara. 7 UStG (Value Added Tax Act). There are further similar exemptions or tax reductions (e.g. for scientific activities of public bodies); however, these provisions have minor relevance for business purposes and for this report, hence no further comments will be provided with regard to them.

32 See *Forschungsprämienverordnung*, BGBl II 515/2011; Administrative Guidelines to the Austrian PITA, MN 8208f *et seq.*

building costs of this building can be taken into consideration for the basis of the 10 per cent tax credit;

- financing expenses related to R&D activities;
- overheads as long as they can be attributed to R&D. The term "overheads" stands for costs (such as energy costs, telecommunications) that are not directly attributable to one cost unit (e.g. a research project). Another example would be investments, which are not directly used for R&D, like a canteen. In this case a part of the depreciation of this building would be attributed.

In general R&D expenses can only be used for the tax credit of one taxpayer, i.e. if a taxpayer conducting R&D is reimbursed for the R&D expenses (or part of them), he can still consider these expenses in his assessment basis, as long as the person reimbursing the expenses does not include these expenses in his assessment basis.[33] R&D expenses paid to someone else can only be part of the assessment basis for contracted R&D (e.g. R&D laboratory expenses paid to someone else must not be part of the assessment basis for self-conducted R&D) even if the outcome of this R&D project contributes to the payer's own R&D activities.[34] Moreover, contracted R&D expenses paid to companies under the controlling influence[35] of the principal, or to members of the same tax group, do not qualify for the tax credit.[36]

R&D expenses funded by any (tax-exempt) subsidies must not be included in the assessment basis.[37] The purchase price or royalty payments for a patent must not be part of the assessment basis.[38]

The assessment basis for the tax credit for contracted R&D is the fee paid to contractors in the respective tax year. Yet, other than for self-conducted R&D there is a maximum amount for the assessment basis of the tax credit for contracted R&D. The assessment basis for contracted research (i.e. expenses paid to contractors charged with R&D in one given year) is limited to 1 million euro per business year. Hence, the maximum tax credit can be 100,000 euro. If the business year is not a full calendar year, the maximum amount must be reduced in accordance with the months covered by the business year.[39]

1.4.3. Tax credit versus allowance

The current Austrian tax law only allows for a tax credit. This used to be different in the past. Before the assessment year 2011 taxpayers could choose between a

33 See Mayr, "Auftragsforschung: Neuer Freibetrag vorrangig beim Auftraggeber", RdW 2005, 508.
34 See Administrative Guidelines to the Austrian PITA, MN 8208f.
35 According to the Austrian Ministry of Finance whether or not someone has controlling influence depends on the circumstances of the case. In the case of widely held stock a rather small shareholding can constitute controlling influence. See Administrative Guidelines to the Austrian CITA, MN 1126.
36 The Austrian tax group is regulated in s. 9 CITA. In general subsidiaries where the shareholding amounts to more than 50 per cent can become members of the tax group. Foreign entities directly owned by an Austrian group member can be group members as well, with certain limitations.
37 See Austrian Supreme Administrative Court 22 October 2002, 2001/14/0030; Austrian Tax Court 28 August 2013, RV/0098-S/12; Administrative Guidelines to the Austrian PITA, MN 8208f.
38 See Austrian Tax Court 24 September 2010, RV/2297-W/09.
39 See s. 108c para. 2 subpara. 2 PITA.

tax allowance and a tax credit for self-conducted R&D. The tax credit used to be 8 per cent, the allowance used to be 25 per cent or 35 per cent. Additionally it was possible to obtain a tax allowance for contracted research at a rate of 25 per cent limited to 100,000 euro. The tax allowance was first introduced in 1980 and changed at various times over the years. The tax credit was first introduced in 2002 as an alternative to the tax allowance.[40]

The crucial criterion for the tax allowance was that the invention was protected by a patent or "economically valuable". This term, however, was not defined in the tax code.[41] According to the jurisdiction, anything that qualified as an invention in accordance with patent law generally also qualified under the tax code. In order to prove the economic value of the invention the inventor could either obtain a confirmation by the Ministry of Science, Research and Economy (name changed over time) or provide a patent certificate.[42]

The purpose of introducing the tax credit was to provide a tax incentive, which is based on the broader definition of R&D developed by the OECD in the Frascati Manual. Furthermore, the general determination of the respective tax reform was to stimulate the Austrian economy. As a tax allowance would only benefit companies in a profit situation, a tax credit seemed to be the right measure to encourage R&D in companies that are in a loss situation.[43] As mentioned above the tax credit now in place allows for a clearer distinction between "qualified" and "not qualified" R&D expenses. The reason for choosing a definition based on the Frascati Manual was to have an internationally accepted and common definition of R&D. Furthermore, the Frascati Manual definition is also used in order to produce statistics on R&D in Austria.[44]

With the abandoning of the tax allowance and its controversial definition of invention and only keeping the tax credit, the Austrian regulation now focuses on the internationally well known system and definition provided by the OECD Frascati Manual. Furthermore, the entire system has become much easier and user-friendly, as the taxpayer does not have to decide between various different allowances and credits using different definitions. For the Austrian government the purpose of introducing tax incentives for R&D has always been the dedication to support and enhance R&D activities in Austria. In the past it often used to be hard to determine whether expenses qualified for allowances or not. By limiting the tax credit to the stage of experimental development, the legislator has made it much clearer to the taxpayer to what extent R&D activities can qualify for an incentive.[45] Additionally, in the past it was possible to obtain a tax incentive twice for the same expenses, also within groups of affiliated companies.

[40] See *Konjunkturbelebungsgesetz* 2002, BGBl I 2002/68.

[41] The term "economically valuable" was heavily criticized by the literature and some parts of the literature even expressed constitutional concerns. See Mrázek, *Forschung und Entwicklung im Bilanz- und Steuerrecht*, 1997, 102 *et seq.* for an overview.

[42] For details see Schneider, *Steuerliche Begünstigung von Forschung und Entwicklung*, 2008.

[43] See accompanying materials to the government bill of the *Konjunkturbelebungsgesetz* 2002, 977 d.B.

[44] See for example Statistik Austria, *Forschung (F&E), Innovation*, available at: http://www.statistik.at/web_de/statistiken/forschung_und_innovation/index.html.

[45] See Schneider, *op. cit.*, 1 *et seq.*

1.4.4. Territorial scope

The Austrian legislator has applied a territorial limitation to R&D input incentives. Self-conducted R&D will only qualify for a tax credit if the R&D is performed in an Austrian trade or business or permanent establishment. In order to qualify for the tax credit for contracted R&D, the principal also has to be an Austrian trade or business or permanent establishment. The R&D contractor on the other hand must have its seat within the EU or the EEA.

The reduced income tax rate for the exploitation of patented inventions can also be applied to income generated outside Austria. As mentioned above the invention either has to be patented in Austria or in the country of exploitation.

1.4.5. Anti-avoidance provisions

The general anti-avoidance provision of the Austrian tax law can be found in section 22 AFC.[46] In order to combat situations where transactions are entered into solely for the purpose of obtaining tax advantages, this section provides guidance. It states that tax liability cannot be avoided or reduced by malpractice of legal forms and methods offered by the civil law. In case of such an abuse, the tax authorities will assess the case by disregarding the abuse. Such misuse is inappropriate and unusual in relation to the economic results and can only be explained by the optimization of the tax burden.[47] Section 23 paragraph 1 AFC additionally clarifies that sham transactions must also be disregarded for tax purposes.

Austrian tax law does not provide for specific anti-avoidance provisions which focus on R&D tax incentives, apart from limitations for the tax credit for contracted R&D. According to section 108c paragraph 2 subparagraph 2 PITA a tax credit for expenses for contracted R&D must not be obtained if the company engaged with the R&D is under the controlling influence of the principal, or if both companies are members in the same tax group. Furthermore, in order to avoid having two companies receiving a tax credit for the same R&D expenses in the case of contracted R&D, the principal must notify the contractor about the extent of expenses used for his tax credit. Consequentially, the contractor must not include expenses considered by the principal for his tax credit.

Moreover, for tax years after 2012 taxpayers have to file an application for an opinion by the FFG.[48] The FFG issues an expert opinion on whether the activities detailed by the taxpayer qualify as R&D in the sense of the law (see definition above) and will then issue an opinion. In the past the tax authorities had to assess whether the activities of a taxpayer qualified as R&D. The daily business of the FFG is dealing with the promotion of R&D and hence the legislator deems the employees of the FFG to be better qualified for assessing the qualification of R&D and therefore reducing the misuse of the tax credit.[49]

[46] *Bundesabgabenordnung*, BGBl 1961/194 (AFC).

[47] See Ruppe, *BAO*, 2014, s. 22 MN 1 *et seq.*

[48] See section 1.6 for further details.

[49] See Mitterlehner *et al.*, “Die Neuregelung der Forschungsprämie durch das 1. Stabilitätsgesetz 2012”, SWK 2012, 803.

A very new anti-avoidance measure is the recently introduced limitation of tax deductibility of royalty (and interest) payments to intra-group companies, where the royalty income is subject to a very low tax rate (see section 2.4.3 below for details).

1.5. Output R&D fiscal incentives (patent box or similar incentive)

So far Austria has not implemented any output R&D fiscal incentives. According to the branch reporters' knowledge such fiscal incentives and here especially a patent box regime have not yet been the subject of broad discussions in Austria, at least not in the last 20 years.

1.6. Procedural requirements

The procedural requirements in order to apply for the tax credit have just recently become more complex. For tax years after 2012 the taxpayer has to obtain an opinion expressed by the FFG. Therefore the taxpayer has to file an application detailing his R&D activities. The FFG will then assess whether these activities qualify as R&D in the sense of the law (see definition above) and will then issue an expert opinion. Generally an opinion has to be obtained on a yearly basis.[50] No opinion is necessary for the application for a tax credit for contracted R&D, nevertheless the R&D project has to be described in detail in the application and the contractor has to be named.[51]

After having received a positive opinion of the FFG the taxpayer can then apply for the tax credit with the tax authorities. The opinion is subject to the free appraisal of evidence by the tax authorities in order to determine whether the tax credit will be granted. The application for the tax credit can only be filed after the tax year has ended and is to be filed as an attachment to the income tax return of the respective year. Even though the application for the Austrian tax credit is filed with the income tax return, the tax credit is not dependent on the outcome of the income tax return and the appraisal is made in a separate decision. If the tax authorities confirm the application for the tax credit, the tax credit will be credited to the tax account of the applicant.[52] The credited amount can then either be paid out or used for future tax payments. Furthermore, the tax credit is independent of the situation of the applicant, i.e. it can also be granted in a loss situation and it can exceed the tax liability of the year in question. It can even be granted in a situation of insolvency.[53]

In order to provide legal security for taxpayers before starting a larger R&D project, there is also the possibility of applying for an advanced ruling for future R&D projects in accordance with section 118a AFC. In this case the taxpayer must also first obtain an opinion from the FFG and can then apply for an advanced ruling with the tax authorities. However, the R&D actually conducted must be in line

[50] See for example Jann and Pock, "Forschungsprämie – das neue Verfahren", RWZ 2013, 52 *et seq.*; Mitterlehner *et al.*, *op. cit.*, SWK 2012, 803 *et seq.*; Schneider, *op. cit.*, 2014, 30 *et seq.*

[51] See Administrative Guidelines to Austrian PITA, MN 8209.

[52] See Administrative Guidelines to PITA, MN 8208a *et seq.*

[53] See Administrative Guidelines to PITA, MN 8208.

with the project description provided for the ruling, otherwise the taxpayer cannot rely on the ruling. The advanced ruling, however, only provides security as to whether the planned activity itself qualifies, it does not comment on the amount of the tax credit.[54]

2. R&D incentives in an international context

2.1. Introduction

Even though the Austrian tax incentives for R&D are widely available for taxpayers, there are certain limitations. Section 2 of the report will therefore assess whether these limitations are contradicting with the non-discrimination provision of concluded double tax treaties and, as Austria is an EU Member State, whether they are in line with EU law. Given the current importance of the OECD BEPS report the last two sections of this part will deal with the treatment of a transfer of intangibles from Austria to another jurisdiction as well as the payment of royalties to other jurisdictions.

2.2. Eligible taxpayers and territorial scope of R&D incentives

2.2.1. Compatibility with the non-discrimination provisions of DTCs

In an international context the question arises of whether the tax incentives for R&D granted by the Austrian legislator are limited in a way that could lead to a conflict with the non-discrimination provisions of existing DTCs.[55] As mentioned above, an Austrian permanent establishment of a foreign company can claim the Austrian tax credit as well. Hence, no issue should arise with regard to article 24(3) of the OECD MC.

The reduced taxation of income from the exploitation of inventions is, however, only applicable to taxpayers subject to unlimited tax liability. As Austrian permanent establishments of foreign companies are only subject to limited tax liability in Austria they are not able to benefit from this regulation. Even though there is a possibility to opt into the unlimited tax liability a lot of permanent establishments will not qualify for this opt-in (see details in the next section). Hence, this issue could lead to a conflict with other contracting states. It should be noted that this issue is only relevant for permanent establishments owned by taxpayers other than corporations as the reduced income tax rate only applies to taxpayers subject to PIT but not to corporations.[56]

54 See Mitterlehner *et al.*, *op. cit.* SWK 2012, 803 *et seq.*

55 As a full analysis of the treaties in force would exceed the limits of this report, art. 24(3) and (4) of the OECD MC were looked at in this report. No comments were provided for art. 24(4) as the reporters did not see any need for comments.

56 See section 1.3.3. above for further commentary on this topic.

2.2.2. Compatibility with EU fundamental freedoms

2.2.2.1. Domestic nexus of the R&D tax credit

Due to Austria being part of the EU the fundamental freedoms of the EU have to be taken into consideration by the Austrian legislator. With regard to the tax credit self-conducted R&D has to be performed within an Austrian trade or business or permanent establishment and for contracted R&D the principal has to be an Austrian trade or business or permanent establishment. The Austrian legislator defends this by stating that the tax credit is not a tax but rather a general economic measure, which has been introduced primarily for historic reasons. According to the Austrian legislator this limitation to an Austrian trade or business or permanent establishment does not constitute a conflict with EU law.[57] In the light of the fundamental freedoms of the EU this limitation, however, seems questionable.[58]

Compared to a company conducting its research in an Austrian trade or business or permanent establishment, a company conducting its research in an EU permanent establishment would be discriminated against. While the first company will be able to apply for the R&D tax credit in Austria the second company will not, and hence the first company will be treated more favourably. This could lead companies to refrain from establishing R&D departments in other countries. However, discrimination only arises where Austria applies the credit method to the income of the foreign trade or business or permanent establishment. Only in this case Austria does still have the right to apply tax on the worldwide income of the Austrian company.[59] According to ECJ case law a Member State, aiming to tax the worldwide income of a taxpayer, must not differentiate between income from domestic or foreign sources. On the other hand in the case of the exemption method Austria exempts the foreign income and hence tax benefits can be denied.[60]

As an argument against such discrimination one could bring forward the necessity to ensure the balanced allocation of the power to tax between Member States. However, Austria (by applying the credit method) is neither limited in taxing the activities located on its territory, nor limited in taxing activities located in other Member States.[61] By taxing the income of the foreign permanent establishment, the discrimination can also not be defended with the coherence of the tax system. According to ECJ judicature the justification of coherence can only be applied where a direct connection between a tax benefit (here: tax credit) and the equalization of this benefit through a specific tax burden (here: taxation of the income) exists at the level of the same taxpayer.[62] The argument of coherence rather leads

[57] See accompanying materials to the government bill of the *Budgetbegleitgesetz* 2011, 981 d.B., 8f; likewise: Puchinger and Marschner, *Budgetbegleitgesetz 2011 reloaded*, FJ 2011, 15.

[58] See Doralt in Doralt *et al*., *EStG*, 2007, s. 38 MN 16; Kühbacher, *op. cit*., SWI 2014, 481 *et seq*.; Lenneis in *Jakom Einkommensteuergesetz*, 2014, s. 108c MN 2.

[59] See Kühbacher, *op. cit*., SWI 2014, 483 *et seq.*

[60] See ECJ 15 July 2004, C-315/02, *Lenz*, MN 49; 7 September 2004, C-319/02, *Manninen*; 12 December 2006, C-374/04, *Test Claimants in Class IV of the ACT Group Litigation*, MN 55.

[61] See ECJ 13 March 2014, C-375/12, *Margaretha Bouanich*, MN 82 *et seq*.; 4 December 2008, C-330/07, *Jobra*, MN 33.

[62] See ECJ 28 January 1992, C-204/90, *Bachmann*, MN 21 *et seq*.; 13 April 2000, C-251/98, *Baars*, MN 40; 6 June 2000, C-35/98, *Verkooijen*, MN 57 *et seq*.; 12 December 2002, C-324/00,

to the conclusion that the tax credit should also be allowed for R&D permanent establishments in other Member States.[63]

So far the requirement of a domestic nexus of the R&D tax credit has not been questioned in Austrian case law in the context of the EU fundamental freedoms. Nevertheless, in *Jobra* the ECJ had to answer the question whether the domestic nexus for applying the investment growth premium[64] constituted discrimination against the fundamental freedoms. According to the provision in section 108e paragraph 2 PITA assets can only qualify for this premium if they are being used in an Austrian permanent establishment. However, assets hired out by an Austrian permanent establishment, which are mainly being used in another Member State, do not constitute "assets used in an Austrian permanent establishment". In this case the court came to the conclusion that

> "Article 49 EC precludes Member State legislation, such as that at issue in the main proceedings, pursuant to which undertakings which acquire tangible assets are refused the benefit of an investment premium solely because the assets in respect of which that premium is claimed, which are hired out for remuneration, are used primarily in other Member States."[65]

2.2.2.2. Compatibility of the R&D tax credit for contracted R&D work

As mentioned above the R&D tax credit for contracted R&D work can also be obtained if the qualified contractor is located in the EU or EEA. When in 2005 a tax allowance for contracted research was introduced, the first draft of the amendments to the tax law did not include this option. After criticism by the literature[66] with reference to the ECJ decision in *Laboratoires Fournier SA* the final amendment included the possibility of contracting R&D to companies and institutions within the EU or EEA.[67] Hence, the R&D tax credit for contracted R&D work seems to be in line with the EU fundamental freedoms, apart from the discussion regarding Austrian nexus in section 2.2.2.1.

2.2.2.3. Reduced income tax rate for inventions available to EU residents?

As regards the reduced tax rate for the exploitation of inventions it should be mentioned again that this reduced tax rate is not applicable for corporate taxpayers. Furthermore, according to section 102 paragraph 2 subparagraph 3 PITA taxpayers

cont.
Lankhorst-Hohorst, MN 42; 18 September 2003, C-168/01, *Bosal Holding*, MN 30; Kühbacher, *op. cit.*, SWI 2014, 484.

63 See Kühbacher, *op. cit.*, SWI 2014, 484.

64 An investment growth premium of 10 per cent may be claimed in respect for the acquisition or manufacture of certain assets, which are subject to depreciation for wear and tear.

65 See ECJ 4 December 2008, C-330/07, *Jobra.*

66 See Aigner, *Förderung der Auftragsforschung durch neuen Forschungsfreibetrag*, taxlex 2005, 267.

67 See *Regierungsvorlage* (government Bill) 992, *Wachstums- und Beschäftigungsgesetz* 2005, BGBl I 2005/103; Kühbacher, *op. cit.*, SWK 2014, 705 *et seq.*; Mayr, "Auftragsforschung: Neuer Freibetrag vorrangig beim Auftraggeber", RdW 2005, 508.

subject to limited tax liability must not apply this reduced tax rate. This regulation (in itself) was clearly discrimination against the freedom of movement and the freedom of service.[68] Taking into account the ECJ judgment in this regard,[69] the Austrian legislator introduced section 1 paragraph 4 PITA in 1996. According to this regulation a taxpayer which is a resident of the EU or the EEA and only subject to limited tax liability in Austria, can opt into unlimited tax liability. The benefit of an opt-in is that the taxpayer can apply any regulation, which is only available for taxpayers subject to unlimited tax liability, such as the reduced tax rate for the exploitation of inventions. However, this opt-in is only possible if 90 per cent of the taxpayer's income is subject to Austrian taxation or if the income not subject to Austrian taxation is less than 11,000 euro. Whereas the regulation generally seems to be in line with the legislation of the EU[70] and might help in some cases, a taxpayer earning income in several Member States will not be able to benefit from it and would therefore be discriminated against.[71]

2.2.3. Compatibility with EU state aid rules

With regard to EU state aid rules the question arises whether the Austrian R&D incentives are restricted to certain taxpayers, size of enterprises, location or sector. The R&D tax credit is not limited in any of the mentioned criteria. As long as the general requirements are fulfilled a taxpayer receiving business income can obtain the tax credit. For partnerships the tax credit can only be claimed at the level of the partnership. The partners are excluded from claiming the tax credit.[72] A limitation of the tax credit based on the legal form of the taxpayer does not exist in Austria. Due to a missing limitation in the above-mentioned criteria and the regulations being based on internationally accepted standards of the Frascati Manual the reporters do not see a conflict with EU state aid rules.

The reduced tax rate for the exploitation of inventions is only available for individual taxpayers. This is defended by the fact that corporate taxpayers are subject to a fixed tax rate of 25 per cent, whereas individual taxpayers are subject to a progressive tax rate of up to 50 per cent. The requirement that only a patented invention can qualify for the reduced tax rate was in the past questioned in connection with regard to the Austrian principle of equality.[73] As mentioned above, for example surgical or therapeutic treatments cannot be patented.

[68] See Lang and Loukota, *EG-Grundfreiheiten und beschränkte Steuerpflicht*, 2006, 232; Tumpel, *Harmonisierung*, 388; Zöchling, "Diskriminierungsverbote im österreichischen Steuerrecht", SWI 1994, 20.

[69] See ECJ 11 August 1995, C-80/94, *Wielockx*; 14 February 1995, C-279-93, *Schuhmacker*.

[70] See ECJ 14 September 1999, C-391-97, *Gschwind* on the comparable German regulation in s. 1 para. 3 German PITA, which was used as a model for the Austrian regulation.

[71] See Kofler, "De Groot: Arbeitnehmerfreizügigkeit gebietet eine volle steuerliche Berücksichtigung der persönlichen und familiären Situation im Wohnsitzstaaat", ÖStZ 2003, 184.

[72] See s. 108c para. 1 PITA; Administrative Guidelines to the Austrian PITA, MN 8208a.

[73] See Stelzer, *op. cit.*, ÖStZ 1988, 194.

2.3. Patent box regimes and harmful tax competition

As Austrian tax law does not provide for a patent box regime, no comments have been made in this section.

2.4. Intangibles and BEPS situations

2.4.1. Introduction

From experience the reporters can say, that, as in many other jurisdictions, the Austrian tax authorities have become very concerned about Austrian companies moving their intangibles to low-tax jurisdictions. Rushing ahead of the OECD BEPS initiative Austria has already limited the deductibility of intercompany royalty (and interest) payments to low-tax countries.

2.4.2. Transfer of intangibles to low-tax jurisdictions

The transfer of assets from Austria to another jurisdiction generally triggers exit taxation of the capital gains, if Austria loses its rights to tax capital gains of these assets.[74] However, due to the ECJ decision *Hughes des Lasteyrie du Saillant* the Austrian legislator introduced a deferral of exit taxation for transfers within the EU or the EEA (only if an extensive agreement on administrative and enforcement assistance is in force).[75] The request for the proposal has to be filed in the income tax return of the year of the transfer. The deferred Austrian exit tax will be triggered as soon as the transferred assets are transferred to a third country or disposed of.[76] Due to the statute of limitations the deferred exit taxation can generally only be triggered within a ten-year period.

As self-developed intangible assets must not be activated they do not constitute an asset. In order to avoid a double deduction of expenses for such (non-activated) assets,[77] exit taxation applies if such an asset is activated in the foreign country it is transferred to. The tax is assessed on the basis of the expenses that have been deducted as expenses for Austrian income tax purposes.[78]

Besides exit taxation the arm's length principle[79] as well as general anti-avoidance rules (see above section 1.4.5) must be considered by taxpayers transferring IP to foreign entities, as the tax authorities will apply these principles in order to determine whether the chosen structuring is tax avoidance.[80] Moreover, the transfer of IP has to be made for sound business reasons. If the transfer is only made for tax reasons, the tax authorities will disregard the transfer itself,

74 See s. 6 para. 6 PITA.
75 See Laudacher in *Jakom Einkommensteuergesetz*, 2014, s. 6 MN 148.
76 In case the asset is transferred outside the EU or EEA in a second transfer, this second transfer constitutes a final disposal. See Laudacher in *Jakom Einkommensteuergesetz*, 2014, s. 6 MN 156.
77 Expenses for developing were deducted in Austria; after transfer abroad the now activated asset is depreciated.
78 See s. 6 para. 6 PITA.
79 Implemented in s. 6 para. 6 PITA.
80 See for example Austrian Ministry of Finance, EAS 3074.

i.e. the tax authorities would treat the case as if the transfer has never happened. Furthermore, the foreign IP holder must qualify as the beneficial owner of any payments. In order to assess this, the Austrian tax authorities will generally look at the substance (active business, own personnel and own office space) of the foreign company.[81]

The transfer of intangible assets to low-tax jurisdictions might also be challenged by the Austrian tax authorities by applying the "substance over form principle" for attributing assets and the corresponding profits. The entity in the low-tax jurisdiction could be considered to be a trustee with the result that according to section 24 AFC both the assets and the corresponding income would be attributed to the trustor. In practice the Austrian tax authorities apply a theory used by the Austrian Administrative Court denoted "market income theory".[82] According to this "theory" income has to be attributed to the taxpayer who can dispose of an asset, who is in the position to participate in market activities and has the chance to use business opportunities and can decide not to deliver business performance. If an entity established in a low-tax jurisdiction is set up as a shelf it is not considered to be the economic owner of the assets. According to decisions of the Austrian Administrative Court no income could be attributed to such a shelf company.[83]

2.4.3. Royalty payments to intermediary IP companies

In general royalty payments made by an Austrian company to a foreign company are subject to Austrian withholding tax of 20 per cent.[84] This is the case if the rights (the royalties are paid for) are used in an Austrian permanent establishment. The understanding of "in an Austrian permanent establishment" in this case is that the permanent establishment can also be that of a third party and not necessarily that of the recipient of the royalty payments.[85]

An exemption at source is either possible in correspondence with the concluded DTCs or in correspondence with the EU Interest and Royalties Directive for payments to countries covered by the directive. In Austria the EU Interest and Royalties Directive has been implemented in section 99a PITA.

In order to obtain an exemption at source in accordance with a DTC the tax authorities require the payer to have either form ZS-QU1 (for payments to individuals) or ZS-QU2 (for payments to legal persons) available in their files. In this form the recipient of the payments must confirm that it fulfils the following substance requirements:[86]

[81] See for example Austrian Ministry of Finance, EAS 1035.

[82] Ruppe, "Möglichkeiten und Grenzen der Übertragung von Einkunftsquellen als Problem der Zurechnung von Einkünften", in Tipke, *Übertragung von Einkunftsquellen im Steuerrecht*, DSTJG 1979, 18; Administrative Guidelines to Austrian PITA, MN 104; Austrian Supreme Administrative Court 23 April 2001, 99/14/0321.

[83] Austrian Supreme Administrative Court 20 September 2007, 2007/14/0007; Renner, "Briefkastenfirmen und internationaler Gestaltungsmissbrauch, Erscheinungsformen und ihre Bekämpfung", in Lang and Jirousek, *Praxis des Internationalen Steuerrechts*, 2005, 405.

[84] See s. 98 para. 1 subpara. 6 PITA in connection with s. 99 para. 1 subpara. 3 PITA.

[85] See Austrian Supreme Administrative Court 24 November 1999, 2006/14/0109; 21 February 1964, 2007/63.

[86] See *DBA-Entlastungsverordnung*, BGBl III 2005/92.

- own active business exceeding mere asset management;
- employing own personnel;
- maintaining office premises.

These requirements have to be fulfilled cumulatively. Additionally the tax authority of the recipients' country must confirm the tax residency of the recipient in the respective form. Furthermore, the recipient has to confirm that he is the beneficial owner [87] of the payments.[88] If the payer does not receive such a form or if he has or should have doubts about its correctness he has to withhold the withholding tax in accordance with domestic tax law, as he will be liable for this tax otherwise.[89] The date of the certificate of residence should not be older than one year prior to the time of payment.[90]

If withholding tax has to be withheld by the payer, the recipient can claim back the withholding tax (or parts of it – depending on the treaty) in accordance with section 240 AFC; the refund will, however, not be granted if the recipient does not have personnel and his own office space or is not the beneficial owner of the payments.[91] From experience the reporters can say that the tax authorities do check the fulfilment of the abovementioned (substance) requirements, e.g. by calling the foreign company, performing online searches (e.g. manager of the company is registered for several companies with the same address), etc.

As mentioned in the first section of this report it has to be noted here again,that Austria just recently introduced a new regulation in section 12 paragraph 1 subparagraph 10 CITA, limiting the deductibility of interest and royalty payments. With effect from 1 March 2014 intercompany royalty (and interest) payments to companies with an effective tax rate below 10 per cent on this income must not be deducted for CITA purposes. If the recipient is not the beneficial owner of the payments, the tax situation at the level of the beneficial owner is relevant for determining whether these payments are deductible in Austria.[92] The Austrian Ministry of Finance has just recently (October 2014) published the 2014 Draft Amendments to the Administrative Guidelines of the Austrian CITA (*Wartungserlass 2014 der KStR 2013*), which bring some clarity to this provision.

[87] Beneficial ownership as a precondition to attribute income to a taxpayer is interpreted by the Austrian tax authorities in the way done by the OECD in their report issued in 2012 concerning the meaning of "beneficial owner". See OECD model tax convention: revised proposals concerning the meaning of "beneficial owner" in arts. 10, 11 and 12.

[88] See for example Austrian Ministry of Finance, EAS 886 and EAS 1035, regarding Dutch intermediary companies used for royalty payments.

[89] See Administrative Guidelines to the Austrian PITA, MN 8013 *et seq.* If the payments made by a payer to a recipient do not exceed 10,000 euro per calendar year and the recipient does not have a domicile in Austria, simplified documentation requirements might be applied. See *DBA-Entlastungsverordnung*, BGBl III 2005/92, s. 2 para. 2.

[90] See Administrative Guidelines to the Austrian PITA, MN 8021b.

[91] See Administrative Guidelines to the Austrian PITA, MN 8022 *et seq.*

[92] E.g. the payments are subject to a taxation of 20 per cent at the level of the recipient. The recipient, however, has to pass these payments to his parent company that is subject to only 5 per cent tax on this income. As the parent company is regarded as the beneficial owner and the royalties are only subject to 5 per cent tax at this level, the Austrian payer will not be able to deduct these payments as expenses.

Concerning the minimum taxation of royalties (and interest payments) at the level of the recipient, the deductibility in Austria is denied if one of the following criteria is met:[93]

- the royalties are subject to an exemption which leads to zero taxation at the level of the recipient; or
- the royalties are subject to a tax rate of less than 10 per cent; or
- the royalties are subject to an effective tax rate of less than 10 per cent due to a tax allowance.

It is generally irrelevant how the remaining income of the recipient company is taxed; the provision at hand only focuses on the taxation of the royalties at the level of the recipient (i.e. beneficial owner).[94] Hence special regimes or treatment for the taxation of royalty income in the recipient's country can lead to a denial of deductibility at the level of the Austrian payer if they lead to one of the above-mentioned criteria being fulfilled. In the 2014 Draft Amendments the Austrian Ministry of Finance names several examples of such special treatment: notional patent income deduction; lump-sum deduction of e.g. 80 per cent of royalty income; partial tax exemption of the royalty income, etc.[95] If the low taxation of the royalty income is due to a usage of a loss carryforward by the recipient, or if the royalties can be offset against losses of other group members in a group regime, this will not lead to a denial of the deduction in Austria.[96]

[93] See s. 12 para. 10 CITA.

[94] See 2014 Draft Amendments to the Administrative Guidelines of the Austrian CITA, MN 1266be.

[95] See 2014 Draft Amendments to the Administrative Guidelines of the Austrian CITA, MN 1266bi *et seq.*

[96] See 2014 Draft Amendments to the Administrative Guidelines of the Austrian CITA, MN 1266bk.

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