

Improving the R&D Incentive for Large, Public and Foreign Companies

A submission to the Toronto Region Research Alliance (TRRA)

Canada is an international leader in supporting Research & Development in large part due to the federal government's SR&ED tax incentive program. Although not all companies operating a business in Canada benefit from the program equally. To fully realize all of the benefits of job and knowledge creation; however, it should be universally available to all companies.

At present, small Canadian controlled corporations recover up to 72% of their investments in R&D, and even more importantly, the tax credit is refundable, which means the company gets the full refund whether or not it has a loss or taxes payable. Large private Canadian corporations and foreign controlled companies operating in Canada unfortunately will only receive a non refundable tax credit within the range of 20% to 34.5%, which means the benefit is not only smaller, but it is not paid out if the company is in a loss position. Even though the tax credit is carried forward up to 20 years, the large private or foreign controlled companies investing in R&D may not recover the associated credit for years to come. The disparity is further amplified for subsidiaries of American companies. Thus, negatively impacting the economic investment attractiveness of Canada to large multi-national companies.

In the United States the R&D tax incentive is far less lucrative for companies than the Canadian R&D program. For instance, the American R&D incentive provides for only 10% recovery, and is based on a three year rolling average of expenditures. This creates an opportunity for American companies with US subsidiaries to perform their R&D in Canada, and creating jobs and development of new knowledge here in Canada. However, the benefit is more often than not neutralized when the U.S. parent company files its US Taxes. At the consolidated level, taxes paid in Canada become a Foreign Tax Credit (FTC) for the American parent company. So given the American tax regimes deems "non refundable" SR&ED credit a reduction of Canadian Taxes paid thus reducing the FTC and consequently neutralizing the benefit of the SR&ED. On the other hand, if the Canadian government made the SR&ED tax credit "refundable" it would simply be considered government assistance in the U.S. and the American parent company would yield the benefit from the SR&ED tax credit, and likely shift its investment in R&D in Canada.

Alternatives to making the SR&ED tax credit universally "refundable" are as follows:

- Refund the credit over three to five years, whether or not the company has generated taxable income; this would ensure that the Canadian subsidiaries



obtain the funding which it could re-invest in new technology development. Additionally, the U.S. Tax regime would consider it a “refundable” incentive or government assistance, and not negatively impact the U.S. parent company FTC position.

- Allow the SR&ED tax credit to be applied against any other Federal taxes or levies, including payroll taxes, which would encourage job creation in Canada.

The implementation of these recommendations or changes to the Canadian tax system would make the SR&ED tax benefit universally available to all companies, including foreign companies, and not only significantly contribute towards the creation of new knowledge, but equally important an increased attraction of new economic investment and new job creation in Canada.

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