



# SR&ED Newsletter

## Edition 2012 –1

Welcome to the first 2012 edition of our newsletter regarding recent developments to Scientific Research & Experimental Development (SR&ED) project management & tax credit claims.

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## March 29, 2012 Federal budget - Science & Technology (S&T) funding changes

Finance Minister Jim Flaherty, announced the 2012 budget will be released Thursday, March 29.

In a Dec.16, 2011 speech to reporters, Prime Minister Stephen Harper indicated the 2012 federal budget will have significant changes to the SR&ED tax credit program stating,

“It is the government's most explicit commitment to act on the recommendations of, Innovation Canada: A Call to Action:”

- an expert panel report headed by
- Open Text Corp. chairman, Tom Jenkins
- that was released in October, 2011

We propose the relevant reports on S&T include

- Jenkins - Federal Commission / POV
- Mowat (U of T) - Academic POV
- Matthews/ CATA - VC + industry POV
- CD Howe / PWC - Private Commission POV
- Canada's S&T Policy- Conservative Party POV

The related SR&ED issues have been **discussed in prior meetings and newsletters** and have been summarized in the following documents ([click to view](#)):

- [SR&ED newsletter 2011-2](#) (12pages)
- [SR&ED newsletter 2011-4](#) (25 pages)
- SR&ED Practitioner meeting Sept 22, 2011
  - o [Minutes](#) (58 pages)
  - o [Webcast of meeting](#) (90 minutes)
- [Letter to Mike Wallace, MP](#) (Feb. 3, 2012, 11 pages)
- [Slides on key issues](#) (Feb. 8, 2012, 45pages)

### Survey administered

We submitted the issues cited to SR&ED stakeholders (practitioners and claimants) in the form of an [online survey](#).

### Summary of findings (next page)

To date we have compiled approximately 120 responses.

In general term most SR&ED practitioners and claimants appear to;

- 1) **Agree with most recommendations** but
- 2) **Strongly Disagree** with proposals to;
  - o **shift of SR&ED funds to grants &**
  - o **have a new NRC agency (vs. CRA) administer the program**

## S&T / SR&ED Survey responses



### SURVEY - OPINIONS ON POTENTIAL SR&ED CHANGES - 2012 BUDGET

Prime Minister Harper has indicated the 2012 federal budget will have significant changes to the SR&ED tax credit program stating, "It is the government's most explicit commitment to act on the recommendations of, Innovation Canada: A Call to Action." (aka the "Jenkins's Report")

The purpose of this survey is to gather input from SR&ED Practitioners.

#### RECOMMENDATIONS FOR SR&ED (JENKIN'S & RECENT REPORTS)                      Agree                      Disagree                      No Opinion

1) Refund of ITC's to large & foreign companies (full or partial)	70%	10%	20%
2) Concentrate new funds on 4 key industries "strategic clusters"	20%	30%	50%
3) Restrict eligible costs to labour only vs. materials & capital	40% initial - 90% > discussion*	10-60% *	0%
4) Shift funding from SR&ED tax credits to direct (grants, contracts & VC)	5%	90%	5%
5) Reduce filing deadline to 6 (vs. 18 months)	60-90%*	10-30%*	0%
6) CRA administer technological eligibility vs. new "NRC" based agency	80%	10%	10%

#### POTENTIAL METHODS TO ACHIEVE "OBJECTIVES" IN JENKIN'S REPORT                      Agree                      Disagree                      No Opinion

1) COMMERCIALIZATION: Refund ITC's to large co's if "collaborate" with CCPC's	90%	0%	10%
2) Understand industry preference SR&ED (25,000+ claimants/yr.) to IRAP (2,500?)	100%	0%	0%

#### COMMENTS:

THE RESULTS ABOVE REPRESENT THE OPINIONS OF APPROXIMATELY 120 RESPONDENTS AT FEB 2, 2012.

\* NOTE: MANY RESPONDENTS WERE UNCERTAIN ON VARIOUS POSITIONS. ONCE THESE WERE DISCUSSED DIRECTLY THEY TENDED TO SHIFT THEIR ORIGINAL OPINIONS. THE %'S OUTLINED IN THE RESPONSE TABLE DISPLAY THE ORIGINAL THEN FINAL %'S (AFTER DISCUSSION).

## **A) Survey results - Science & Technology Policy issues addressed**

Recent reports have made a series of specific recommendations relate to S&T policy:

### **1) Refund of ITC's to large & foreign companies (full or partial)**

It has long been observed that a substantial amount of R&D is moving outside of Canada due to large corporations inability to use [non-refundable credits](#).

This also provides potential mechanisms to encourage work with small & medium sized enterprises (SME's) to address further issues on commercialization.

#### Comments by Survey Respondents

- 1) "Set up separate program for Foreign companies but leave SRED as is. It works and gives much direction to Canadian companies."
- 2) "large/foreign entities should be entitled to partial refundable ITCs"

#### Group Recommendations

Consider **refundable SR&ED credits for large firms who "collaborate" with small Canadian firms.**

This meets all objectives including "commercialization" and "knowledge" transfer (discussed in section D).

It is also already supported in the current layout of the SR&ED claim form.

### **2) Concentrate new funds on 4 key industries "strategic clusters"**

Since this is more of an economic than a tax issue most respondents often showed a mixed response or no opinions.

Of those with an opinion we appear to have an equal mix of supporters (software developers) or strong resistance (manufacturing sector) however, the opinions appear based more on the specific interests of the respondents than any factual analysis.

#### Comments by Survey Respondents

- 1) I found the conclusions and recommendations of the Jenkins report to be extremely disappointing and ill-informed. Government selection of key industries has never been successful in the past.

#### Group Recommendations

This could be a source of opportunity if done with proper, "balance."

Some of the issues on determining the optimal allocations have been provide in the Industry specific commentary in the "sectors to receive new funding" section of [newsletter 2011-4](#).

### **3) Restrict eligible costs to labour only vs. materials & capital**

#### **This is one of the major areas of disagreement!**

Proponents for this method argue that unlike credits for materials & equipment which can be sources from other countries, credits based on Canadian wages represents a “hedged” transaction from a Department of Financial perspective.

In other word the only way to earn credits is to pay wages which in require income taxes withholdings to fund these credits.

It is also very easy to review form a CRA perspective since they can confirm all T-4 reported earnings & related payroll remittances.

Those against this focus cite the needs of industry for such funding & related problems in determining “adequate” time reporting.

#### **Comments by Survey Respondents**

- 1) “Len Lucier's comment at the recent annual Hamilton SR&ED Conference was right on the mark: one of the most challenging aspects for claimants relates to CRA's acceptance of the labour allocation.

It is illogical for the Jenkins Panel to have concluded that a labour-only basis to determine ITC's will simplify the determination of the SR&ED calculation.

In fact, determination of eligible contract and material expenditures is trivial compared to labour expenditures for SMEs that do not require a time card system to run their business.”

- 2) "In my MBA classes we were taught to shift resources from less profitable areas to more profitable areas regardless that both areas are profitable. By focusing the SRED resources / credits on labour only this is achieved.”

- 3) “This idea is brilliant & long overdue!

- used effectively by Quebec for decades
- it greatly simplifies the calculations
- CRA can quickly review (payroll withholdings)
- creates a hedged transaction, i.e. the only way to
  - o earn more credits is to
  - o pay more Canadian wages which in turn
  - o creates the “employee income taxes”
  - o to pay the credits.

As a result, this process is much easier to budget for all stakeholders (government & business).”

#### **Group Recommendations**

There is **little group consensus** on this issue **unless** it is **reworded** as follows:

“If we need to reduce SR&ED funding somewhere would you prefer labour or materials & capital?”

Once this issue was considered the consensus would be to;

Focus the claims on wages (labour)

- i. Using the Quebec model with
- ii. Wages (direct or via Canadian Contractors)
- iii. Simplified calculations

This can also provide a basis to:

- increase claimants incentive to keep time records,
- documentation of experimental development &
- hopefully reduce compliance costs

further addressing CRA & Parliament’s concerns on these issues.

#### **4) Shift funding from SR&ED tax credits to direct (grants, contracts & VC)**

##### **Grants**

Statistics on the total number of IRAP claimants or any of the other “direct” programs are not publicly posted. Perhaps the best current statistics are cited in the Jenkins report.

“Among the **488 survey respondents**<sup>1</sup> that had accessed a federal R&D program in the past three years,

- **73 % reported using the SR&ED tax credit program,**
- **17 % IRAP,**
- **No other program** was identified by **more than 1 %** of the companies.”

This strongly suggests that federal programs are;

- not well known or
- accepted by business.’

##### **Contracts (procurement)**

Few respondents addressed this issue.

A great example of past failures might be the 1990’s when federal government decided to license Microsoft Office (US firm) instead of Corel Office (Canadian firm) which;

- had combined Lotus & WordPerfect technologies
- representing a realistic challenge to what is effectively
- now a worldwide product monopoly.

##### **Venture Capital**

Venture Capital represents a source of opportunity if done properly. The real issues will come down to a matter of “balance.”

These investors typically do <**1,000 deals / year** in Canada and generally **demand a minimum 40% annual return** on investment. This is discussed further in [newsletter 2011-4](#) page 23-24.

##### **Comments by Survey Respondents**

- 1) “I am against any further support being forwarded to IRAP. For 25 years my company and 35 of my clients have witnessed the continued arrogance and incompetence of IRAP’s consultants. How the government has justified supporting such a group of ineffective freeloaders is beyond our understanding to give these people even more power will certainly destroy R&D in Canada.”
- 2) “IRAP is a process which needs fixing - never any allocations and far too long lead time to hope of funding - companies can't invest the time for the hope of getting 50% that will only grind their SRED claim. Jenkins report was so self-serving and too restricted in what could be recommended it is useless.”
- 3) In the early 2000's, there was much criticism of direct funding programs such as TPC. Media criticism was that government (and academia) did not have a good track record at ""picking winning companies"" and the investment decision was best left to industry (through the SR&ED program). It is interesting how the pendulum has started to swing back the other way.”
- 4) “The VC market has disappeared in Canada as angel investors have had their wings clipped. This is a key driver to the economy to the point that the government gave \$50 m to the BDC as a VC fund and these bureaucrats didn't know what to do with it.”
- 5) “Grants for SR&ED as a replacement for tax credits is a very bad idea. Decisions on grants take too long and usually have to be made by technically uninspired people. Is the government trying to reduce the costs of ITCs? I don't know, but if so, then specifically address that issue.”
- 6) “Need more certainty in the program to encourage investing funds in new research, but don't want to slow down process with extensive grant applications before starting research.”
- 7) “In my experience, grants such as IRAP and regional grants are far more susceptible to fraud than the SR&ED program. Recent SR&ED cases in Montreal are the exception. IRAP field officers have been (and may still be?) contractors, not employees of NRC. There have been many cases of nepotism, kick-backs, etc. There are few checks on them except the fact that their pot of money is more limited.”

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<sup>1</sup> “Jenkins” report (Figure 5.3)

8) The reports largely ignore the history of the debate of grants versus tax credits and why Canada went to tax credits.

I was a heavy participant in the period 1977 to 1989 when SR&ED was young and grants were still the main government support. I ran contract R&D labs in Calgary and in Sydney, Nova Scotia. I witnessed the growth of regional grant agencies, under both Liberal and Conservative governments.

The selective grants dried up in 1989 because the NAFTA and other trade agreements made direct grants to industry not possible if it interfered with fair trade of goods or services. SR&ED did not interfere – all companies are treated equal.

A return to grants would be to institutes not companies – otherwise, any benefits would go to lawyers to fight the WTO and NAFTA litigations.

9) Why not simplify (and expand) the direct funding approach instead of SR&ED? A rhetorical question, it would seem, as the intent of government in introducing change to the latter program, I believe, is to ultimately reduce its financial commitment and burden under the cloak of improved program efficiency. "

#### Other recent comments – Globe & Mail

A March 11, 2011 Globe & Mail [article](#) provides quotes from Andrew Dunn, a managing partner at Deloitte, expressing worries Ottawa will slash the credit scheme on a potentially "faulty" premise.

"Moving from credits to grants puts the decision in the hands of government," he said.

"Canada has a bad history of grant-type programs. The global trend is from grants to credits."

#### **Group Recommendations**

Industry recommends that the government first understand "industry" preference of SR&ED (tax credits) over direct funding (grants):

- > 25,000 companies claim SR&ED every year vs.
- < 1,000 VC funded deals / year &
- < 5,000 ? IRAP/NRC funded grants / year

Venture capital represents an opportunity but if overfunded, it may not only

- play havoc with "free market" forces but also
- "play into" a strategy of putting,
- "all of the eggs into very few baskets."

#### **Notable quote:**

"Clarification on these issues would be helpful to taxpayers so they are not blind-sided at the time of the next Federal Gov't budget."

- SR&ED survey respondent

## **5) Reduce filing deadline to 6 (vs. 18 months)**

**This is one of the major areas of disagreement!**

According to a recent CATA white paper approximately 30% of the Canada Revenue Agency's costs of compliance relate to amended claims (typically filed between 6-18 months from year end).

They propose that,

“Almost **one-third of claims** received by the CRA in any given year are **retrospective** claims being filed for **previous years**.”

A significant portion of these claims appear to be of a speculative nature, providing windfall revenues to businesses & consultants [resulting in] questionable value as incentives for the SR&ED.”

They then go on to suggest,

“if the SR&ED program eliminated retrospective claims filed for previous years ... it could free up as much as 30 per cent in funding to be redeployed into direct investment.”

### Comments by Survey Respondents

While most survey respondents were against this measure, when it was reworded as

“If some costs had to be cut and this could save 30% of CRA review time would you consider this?”

the consensus tended to shift to support the reduction of this filing timeline.

### Group Recommendations

In a properly structured SR&ED system companies should be able to report these costs with their tax return (filing due date of 6 months from year end)

As a related issue the CRA may in turn relax its filing requirements on a “complete claim” so as not to “punish” claimants for simple omissions or “honest” mistakes.

### **Notable quote:**

“Each person's work is always a portrait of himself.”

- Samuel Johnson

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## **6) CRA continue to administer technological eligibility vs. new "NRC" based agency**

Many of these issues have also been addressed in the our discussion of Grants vs. SR&ED tax credits (issue 4).

The following additional comments are specific to this issue.

### **Comments by Survey Respondents**

1) "Is the government trying to get more consistent adjudication of claims? If so, we need a few more technical people at HQ and a hiring policy for technical reviewers which attracts more recently retired technical professionals rather than MSc.s with little practical experience."

2) "Nothing to do with R&D funding should be in the Tax Act. Period."

3) "SR&ED – administer by CRA or other party?"

Key factors favoring the CRA include,

- Respect – It is a felony to file a false income tax return. Most people could cite stories of the laws and precedence that both protect the "rights" of the taxpayer (e.g. Duke of Westminster decision) & punish those who violate the system (e.g. Al Capone).
- Corruption - Can you name anyone convicted of "grant" or "government procurement" frauds? The only ones I can recollect involved unsuccessful attempts to charge former Prime Ministers Brian Mulroney & Jean Cretien with complicity in improper funding allocations to their "friends."
- Rights – as a taxpayer if you have performed SR&ED you can appeal decisions to the tax court since you have a "right" to the funds. You can't do this with IRAP or any grants. As a result there is NO certainty which is the most important criteria for industry acceptance of any program.

- History / Infrastructure – Tax law has a system of lawyers, CA's, and judges trained in tax law. Moving this to a grant system represents the elimination of the full recourse process & shifts the funding to a fully discretionary process at the discretion of politicians and their friends."

### **Group Recommendations**

Continue to use the CRA as the primary reviewer of SRED claim since this;

- Maintains strong history and basis for objection, appeal and tax court review &
- No similar rights or objectivity under grant programs.

### **Notable quote:**

"If you give a man a fish you feed him for a day.  
If you teach a man to fish you feed him for a lifetime."

- Chinese proverb

## **B) S&T Policy Issues NOT directly (or fully) addressed**

### **1) Macro vs. Micro Economics –benefit of every \$ invested**

Several newspaper articles have provided factual information in a potentially “misleading manner” when they discuss the [“marginal tax utility” of every dollar](#) the government invests in SR&ED incentives.

The articles report that the tax investment only provides

- equal 1:1 payback of every tax \$ invested
- by way of direct tax revenues (marginal utility)
- however, this creates an estimated 500% social return on this investment
- by way of “spillovers!”

Mathematically speaking the “full picture” indicates up to 600% (economic + social) return of every tax \$ invested.

#### Authors Recommendations

While the facts stated in the article are correct: the marginal utility for every tax dollar invested is “break even,” this is only one piece of a “larger picture.”

When considering the Jenkin’s report recommendations we should endeavor to consider the;

- o full “economic” vs.
- o just the marginal value of incentives.

### **2) US vs. Canada – collaboration vs. confrontation**

- The US continues to [announce expansion of this credit](#)
- The governor of Michigan<sup>2</sup> has questioned the [fairness of Canadian policies](#)
- There appears to be a huge potential for collaboration since
  - o The IRS code provides for credits using similar definitions &
  - o The Canadian SR&ED form already contemplates “collaborative” claims for SR&ED projects.

#### Authors Recommendations

Recommendation for US vs. Canada collaboration

- Consider co-operative
- Claim & Review functions
- Between US & Canadian Companies (claims)
- Using both IRS & CRA staff (reviews)
- For claims in both jurisdictions

*See example on page 16*

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<sup>2</sup> “Canada Should End Business Tax Breaks, Michigan’s Snyder Says,” Business Week, Nov., 8, 2011

### 3) Regulation of fees for consultant support

Changes are expected to limit consultants' share of the SR&ED credit as Ottawa expresses concern that too much federal science cash is flowing outside the "intended" sector.

#### Globe & Mail articles on % SR&ED paid to consultants

To "sensationalize" this issue in March 11, 2011 the Globe and Mail ran an article entitled,

[Flawed R&D scheme costs taxpayers billions](#)<sup>3</sup>

which, in the author's opinion,

- a) Provided examples of specific (inappropriate) practices used by one of these Rogue consultants
- b) presented "opinions" which may mislead readers.

The article stated,

"This year, Ottawa and the provinces will dispense \$4.7-billion to more than 20,000 Canadian companies.

But a third or more of that cash is being wasted and paid to consultants as a result of hazy rules on what's legitimate R&D and limited government auditing resources,

according to dozens of interviews with consultants, claimants and government officials."

[Ottawa eyes keeping science cash out of accountants' hands](#)<sup>4</sup>

According to this March 7, 2012 article,

**Gary Goodyear, the federal minister of science and technology**, is hinting that upcoming changes will aim to limit these added costs to the SR&ED program.

"I'm not concerned about what accountants charge for their everyday business. My concern is simply that that money then moves out of the science, research & development sectors & into another area of our economy."

The article also quoted **Andrew Dunn, a managing partner at Deloitte** who disputed that consultants are pocketing too much of the R&D credits.

"While some consultants charge contingency fees of 30 or 40 percent, the overall numbers are much lower."

He pointed to a survey by the Canadian Institute of Chartered Accountants which found that the

"top six accounting firms in Canada earned \$117-million in 2010 from SR&ED".

Mr. Dunn then recommended the,

"government could root out overly aggressive practices by banning contingency fees and requiring registration of all consultants."

#### Authors Commentary

Using the example quoted, if the top 6 CA firms can be assumed to complete 100% of the claims for large corporations (i.e. not "Qualified CCPC's") the

Average compliance costs of SR&ED would be

$$\begin{aligned} &= \text{Total SR\&ED fees} / \text{total SR\&ED credits claimed} \\ &= \$0.117 \text{ billion} / \$ 4 \text{ billion} \\ &= 2.9\% \text{ (cost of compliance as \% credit received)} \end{aligned}$$

<sup>3</sup> Globe & Mail, March 11, 2011 Link to article:  
<http://www.theglobeandmail.com/report-on-business/flawed-rd-scheme-costs-taxpayers-billions/article1939418/>

<sup>4</sup> Globe and Mail March 7, 2012, By Bill Curry & Barry McKenna

## Authors personal experience, examples & opinions

### Facts & Issues

1) **Client choice** - I have practiced in the SR&ED field since 1993. From 1993 to 2000 I worked on some of the largest SR&ED files in Canada on an hourly or flat fee basis.

On almost all hourly agreements “sophisticated” clients required a budget and authorization before incurring any fee overruns. In reality these resulted in “flat fees.”

When I left partnership and started MEUK Corporation I decided to offer clients all 3 billing options:

- hourly,
- flat fee or
- % of recovery

I have **clients who prefer each of these options** for various reasons.

2) **Needless complexity** - As the co-author of the SR&ED course for the Canadian Institute of CA's and seminar leader for the past 15 years I can say that I spend over 30 minutes explaining the just the rules on “specified employees.”

He course itself runs a full 8 hours and only provide an overview of many “complex” issues.

Most CA's walk out of the course claiming it is:

- needlessly complicated &
- one of the most confusing areas of income tax they have ever explored.

The result is that they tend to charge a minimum \$5,000 for compilation of the SR&ED related tax forms, assuming the client prepares the technical (project) descriptions.

3) **Related liability** - Worse yet I have seen lawsuits for millions of dollars against CA's for failure to adequately:

- plan or complete the SR&ED forms
- within required deadlines.

### Analysis

My experiences on billing methods is at each has its own pros & cons however, it is ultimately the claimant who should be empowered with choice..

The majority (approximately 80%) of first time claimants, under \$100,000 of ITC's prefer to use the % recovery in the first year.

The % fees for this work range from 2-20% of recovery dependent on the nature of the work and range of services provided.

I have some flat fee clients who's fees (including costs to plan & complete the project descriptions & income tax forms) are <2% of total credits.

Fees at the higher end of this fee range tend to be paid by clients with weaknesses in the SR&ED documentation systems.

Most clients will not pay aggressive fees for services which they believe they can perform on their own.

If the free market willing to pay high fees for product or service it is because they perceive high value.

### Related Recommendations

The free market is likely the best mechanism to determine the fair price of any service commodity.

It should be the client's choice which method of billing & payment best meets their business needs.

As a result the government should not attempt to regulate the fee or service providers other than as to quality of work.

The Jenkins and other current SR&ED reports recommend, “streamlining the SR&ED claim system.”

If the government policy makers & CRA wish to reduce the fees consultants charge all they need do is simplify the current complexity of the program.

## **C) SR&ED issues & recommendations on CRA administration**

### **1) Ombudsman report<sup>5</sup>**

In December 2011 the CRA Ombudsman released its report on

[Issues of service & fairness within the SR&ED Program](#)

#### **Select excerpts:**

Although our Office heard criticisms and comments through consultations with claimants about the perception of regional discrepancies,

“we did not receive any actual complaints that we could substantiate. On one hand, there may indeed be some inconsistencies in the way the program is administered.”

In some of the reports the RTAs<sup>6</sup> simply stated that,

“the claim did not meet the criteria of the Income Tax Act”

without explaining in a clear and complete manner how the decision was arrived at.

This is an excerpt from one such Technical Review Report:

“Designing a XYZ is not considered an attempted technological advancement.

The work is not considered to be performed for the purpose of achieving technological advancement and therefore it does not meet subsection 248(1)(c) of the Income Tax Act.”

#### **Author’s commentary**

It should be noted that the report was premised on 5 main questions for claimant & preparer feedback, regarding post Feb. 21/07 SR&ED claims:

- Did CRA adequately inform taxpayers about the recent changes to the T661 form?
- Has the cost of filing and defending an SR&ED claim changed?
- Did CRA accept your request for a "second opinion"?
- Did CRA review and audit your claim in a professional and courteous manner?
- Has any CRA person ever attempted to dissuade you from retaining professional advice?

The report was silent as to the responses to these specific questions.

The report otherwise speaks for itself: no on provided evidence to back up their complaints.

#### **Related Recommendations**

We suggest the best solution to this issue would be for;

- One or more claimants to
- post relevant complaints publicly
- for SR&ED stakeholder review & input since

This should to remove the “secretive” nature of the

- current process & provide
- required accountability based on specific facts.

<sup>5</sup> This publication is available in electronic format at [www.oto-boc.gc.ca](http://www.oto-boc.gc.ca).

<sup>6</sup> CRA “Research & Technology Advisors”

## 2) Related - Administration of the SR&ED program by the CRA

### CRA SR&ED Directorate - top 5 program problems (Jan 11, 2012)

The CRA's SR&ED Directorate held its annual practitioners meeting in Burlington, Ontario on January 11, 2012.

The CRA's new Director General for SR&ED, Susan Betts, listed the **top five concerns of industry and CRA about SR&ED.**

For industry:

- 1) RTA's not qualified to correctly assess claims
- 2) Narrowing eligibility criteria
- 3) Complexity of process and forms
- 4) Requirement for supporting documents too onerous
- 5) Outcomes uncertain year to year and lack of consistency

For CRA:

- 1) Personal attacks against CRA staff
- 2) Incomplete claims / information not sufficient to allow desk review processing
- 3) Success fee billings "unfairly" divert benefits from taxpayers to consultants
- 4) Increasingly aggressive claims
- 5) Claims withdrawn if challenged by CRA
  - including penalties for unjustified claims &
  - prosecution of claimants & tax advisors

### Authors Recommendations

#### Technological eligibility recommendations – 2 steps

We propose that the CRA management could consider 2 steps to improve the current system:

##### 1) 1 complete project example / industry

- based on existing [CRA SR&ED examples](#) &
- compliant with all
  - a. technology & tax reporting expected of claimants & related
  - b. [precedence set by the Tax Court of Canada](#)

##### 2) Dispute resolution mechanism

- objective,
- third party, 2nd review system to
- Arbitrate /settle disputes
- In a timely manner (30 day objective)

#### Financial eligibility recommendations – 1 step

We propose that SR&ED policy makers can assist CRA management by

- moving to a labour based system
- with simplified calculations.

## **D) Commercialization – new focus & options**

### **SME and large firm – collaboration for commercialization**

#### Facts:

Several of the reports acknowledge that

- "large, multi-national" co's have
- strong commercialization infrastructures &
- prefer to have SR&ED funding vs.
- SME's who need commercialization assistance.

A [Feb.28, 2012 report from CATA](#) acknowledges,

“53 per cent of surveyed companies compete in the market without collaborating with industry peers.”

The report then recommends that,

“To compete and survive, small companies need to collaborate among themselves, as well as with large anchor companies that have built-in channels to the market. Canada does not have a culture of collaboration,”

“The government must encourage collaboration among Canadian industry companies on a much larger scale than at present, where most of the incentives were focused on collaboration between government labs and industry and on ways to get more academic institutions to license their inventions to industry,”

#### **Group Recommendations**

Consider incentive for;

- "large co's" to act as "ANCHORS" for
- development, mentoring & commercialization with
- SME's on SR&ED projects.

This could be implemented;

- based on previously approved SR&ED projects &
- as a basis to implement the proposed &/or
- refundable SR&ED ITC treatments.

As noted in the section on US collaboration the

- Canadian SR&ED form already contemplates
- Collaborative claims for SR&ED projects

As a result we recommend the:

- existing SR&ED claim information can be used to
- identify “collaborative” SR&ED work, allowing;
  - a single project description for multiple claimants (reduced compliance costs),
  - additional incentives to large Canadian firms who work with Canadian SME's &
  - perhaps even joint incentives for work with
    - Canadian & US companies,
    - jointly administered by the CRA & IRS.

*See example on next page*

## SR&ED claim form – method to claim “collaborative work”

### Part 2 – Project information

Complete a separate Part 2 for each project claimed this year.

CRA Internal form Identifier 060  
Code 1101

Section A – Project Identification																										
<b>200</b> Project title (and identification code if applicable)																										
<b>202</b> Project start date <div style="text-align: center; margin-top: 5px;"> <table style="margin: auto; border: none;"> <tr> <td style="border: none;"> </td><td style="border: none;"> </td> </tr> <tr> <td style="border: none; text-align: center;">Year</td><td style="border: none; text-align: center;">Month</td><td colspan="4" style="border: none;"></td> </tr> </table> </div>							Year	Month					<b>204</b> Completion or expected completion date <div style="text-align: center; margin-top: 5px;"> <table style="margin: auto; border: none;"> <tr> <td style="border: none;"> </td><td style="border: none;"> </td> </tr> <tr> <td style="border: none; text-align: center;">Year</td><td style="border: none; text-align: center;">Month</td><td colspan="4" style="border: none;"></td> </tr> </table> </div>							Year	Month					<b>206</b> Field of science or technology code (See guide for list of codes)
Year	Month																									
Year	Month																									
Project claim history																										
<b>208</b> 1 <input type="checkbox"/> Continuation of a previously claimed project		<b>210</b> 1 <input type="checkbox"/> First claim for the project																								
<b>218</b> Was any of the work done jointly or in collaboration with other businesses? ..... 1 <input type="checkbox"/> Yes 2 <input type="checkbox"/> No																										
<b>If you answered yes to line 218, complete lines 220 and 221.</b>																										
<b>220</b> Names of the businesses	<b>221</b> BN																									
1																										
2																										
3																										

The work was carried out (Check any that apply)

### Collaboration – stage 1 (Large & Small companies)

Consider “refundable credit” incentive for;

- "large co's" to act as "ANCHORS" for
- development, mentoring & commercialization with
- SME's on SR&ED projects
- Including a single project description for multiple claimants (reduced compliance costs),

### Collaboration – stage 2 (Canada–US SR&ED)

Consider extending SR&ED 1 “collaboration”;

- To include joint incentives for work between
- Canadian & US companies,
- Jointly administered by the CRA & IRS

## **Crowd funding for SME's – follow US model?**

The Entrepreneurs Access to Capital Act, recently passed in the U.S House of Representatives with overwhelming support. It is now being reviewed by the U.S. Senate.

In Canada, CATA and other technology policy groups have launched advocacy campaigns to encourage provincial securities legislators to adopt similar approaches.

Peter Andrews, CATA Director stated,

“the crowd funding model is like a bake sale, where people pitch in a small amount of money to get a project off the ground.”

Key features of the new U.S. crowd funding legislation include:

- \$1,000,000/year limit on the amount an issuer can raise (\$2,000,000 if audited financial statements);
- limits on the amount sold to any investor in any year

lesser of ;

(a) \$10,000

(b) 10% of the investor's annual income).

A recent issue of Small Business Report provides additional insights [Crowd Funding and Start up Capital](#).

### **Group Recommendations**

Most parties agree that this appears to be a promising incentive for;

- "small companies" to "raise private capital"
- Development & Commercialization of SR&ED
- Without the use of taxpayer funds.

As a result most parties support recommendations to speed the passing of this legislation in Canada.

### **Notable quote:**

“Give a man a match, and he'll be warm for a minute, but set him on fire, and he'll be warm for the rest of his life.”

- Anonymous

## Questions or feedback

We welcome your questions or feedback on any issues raised in this letter.

We also encourage interested parties to examine:

- past SR&ED newsletters
- SR&ED tax guide [the Guide to RDBASE.NET],
- “RDBASE.NET” online SR&ED tracking software &
- additional tutorials re. eligible SR&ED activities at

## Terms of use

Although we endeavor to ensure accurate & timely information throughout this letter, it is not intended to be a definitive analysis of the legislation, nor a substitute for professional advice.

Before implementing decisions based on this information, readers are encouraged to seek professional advice, in order to clarify how any issues discussed herein, may relate to their specific situations.

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