



## **KEEPING CANADA COMPETITIVE: ENHANCING THE SCIENTIFIC RESEARCH AND EXPERIMENTAL DEVELOPMENT (SR&ED) TAX CREDIT**

### **THE ISSUE**

The Scientific Research and Experimental Development (SR&ED) tax credit program has long been heralded as one of the world's most generous R&D tax credit programs. The program's competitiveness has largely diminished due to measures of reigning in R&D dollars in difficult economic times. Over the last three years, a variety of countries, including economically comparable nations such as France and Australia, have made impressive changes to their respective R&D tax credit regimes.

As domestic capital from the private markets has slowed since the economic recession, junior biotechnology companies are increasingly looking at foreign markets as sources for risk capital. However, as these companies raise foreign capital, they become less likely to receive refundable SR&ED tax credits due to the Canadian-controlled private company (CCPC) restriction. In turn this makes it harder for companies to maintain or expand their development operations here in Canada.

As opposed to other technology industries, junior biotechnology companies going public is not an indication of reaching a mature stage of development; it is simply a method to help finance R&D operations in Canada. Consequently, the CCPC restriction against refundable tax credits not only discourages companies from seeking risk capital from foreign investors, but also the public markets. These refundable credits need to be available to all SME's irrespective of ownership to keep research operations in Canada.

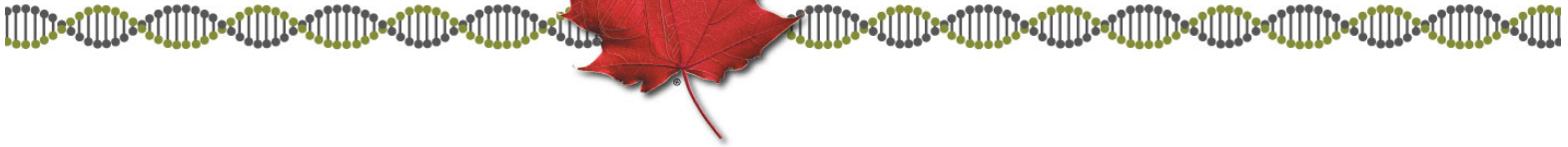
We have a growing concern around new interpretive changes being implemented within CRA regarding the eligibility of clinical trial expenditures. This results in SR&ED becoming misaligned with the realities and expectations of Health Canada regulations for acceptable therapeutic drug research and development in Canada, as well as out of step with the expectations of provincial governments to increase clinical trial work domestically.

### **RECOMMENDATIONS**

*Keep the SR&ED program valuing clinical trial work being done in Canada and enable companies to grow their operations in Canada with foreign investment:*

The Government of Canada should remove the current CCPC restriction against refundable SR&ED tax credits in order to encourage companies to seek foreign and public sources of capital, and enhance business expenditures on research and development (BERD). BIOTECCanada estimates that removing the CCPC restriction would cost an additional \$75 million per year (2% of the value of the program), but would create close to \$1 billion in new wealth and economic gains. \*





## BACKGROUND

- The value of the SR&ED program has been proven in numerous government, industry, and academic reports. The Department of Finance has estimated the SR&ED program has a positive return on investment - \$1.11 returned for every dollar spent on the program.
- The SR&ED program was established in 1985 before international free-trade agreements, and has not been updated to reflect today's global business environment.
- If a company is a CCPC, it is eligible for a refundable tax credit of 35% on up to \$3 million of annual R&D spending. If the company is not a CCPC, it receives tax credits of only 20% on its R&D expenditures and these are not refundable.
- Non-refundable tax credits are not useful to junior biotech companies as they are in a loss position, do not have taxable income and are years away from reaching profitability.
- When a Canadian company successfully attracts international investment or relies on public markets for financing, it loses its valuable refundable tax credits even though jobs, research and innovation are still conducted in Canada. This can, and has, lead companies to relocate activities and jobs outside of Canada. Removal of Section 116C of the Income Tax Act was a positive step in attracting foreign risk capital, but more needs to be done to keep building innovative companies in Canada.
- It is important to note removal of the CCPC restriction is intended to benefit small, research-intensive companies within the taxable income and taxable capital thresholds. This recommendation will not benefit large technology companies outside of the taxable income and taxable capital thresholds.
- Canada's vital tool, the SR&ED program, can be a competitive advantage if all junior, research-intensive companies can use it. Increasing the expenditure limit will ensure access to much needed capital and leverage financing from outside sources, ensuring more Canadian business success stories.
- BIOTECanada has written to Minister Shea on the matter of CRA clinical trial interpretations and we are currently awaiting an opportunity to meet with her and her officials.

\*Source: Pellerin, W. Canada's missing billion dollars: Quantifying costs and benefits of modifications to the SR&ED tax credit program – the biotech industry example, September 2008, BIOTECanada.

