R&D Tax Incentives: Canada, 2020

Design of R&D tax relief provisions

Canada provides R&D tax relief through a volume-based tax credit.

Table 1. Main design features of R&D tax incentives in Canada, 2020

		Federal Scientific research and experimental development (SR&ED) tax credit
Tax incentive		Tax credit
Type of instrument		Volume-based
Eligible expenditures†		Current
Headline rates (%)		15 (35 for CCPCs*)
Refund		Immediate (CCPCs)
Carry-over (years)		20 (carry-forward), 3 (carry-back)
Thresholds & ceilings	Threshold (R&D expenditure)	35% credits are available to CCPCs up to a baseline expenditure limit of CAD 3 million** (excess expenditure is eligible for 15% tax credit)
	Refund-specific	Full refund at 35% rate up to expenditure limit of CAD 3 million (CCPC)***

* CCPC: Canadian-controlled Private Corporation.** Before March 2019, the baseline limit of CAD 3 million was reduced as a function of taxable income and taxable capital and was fully phased out once a CCPC reaches a prior year taxable income of CAD 0.8 million or a prior year taxable capital of CAD 50 million. As of March 2019, the use of previous year taxable income is removed as a factor in determining a CCPC's annual expenditure limit. The latter is a function of taxable capital only.

Note: For more details, see OECD R&D Tax Incentive Compendium and Eligibility of current and capital expenditure for R&D tax relief
Source: OECD, R&D Tax Incentives Database, http://oe.cd/rdtax, March 2021.

Key features:

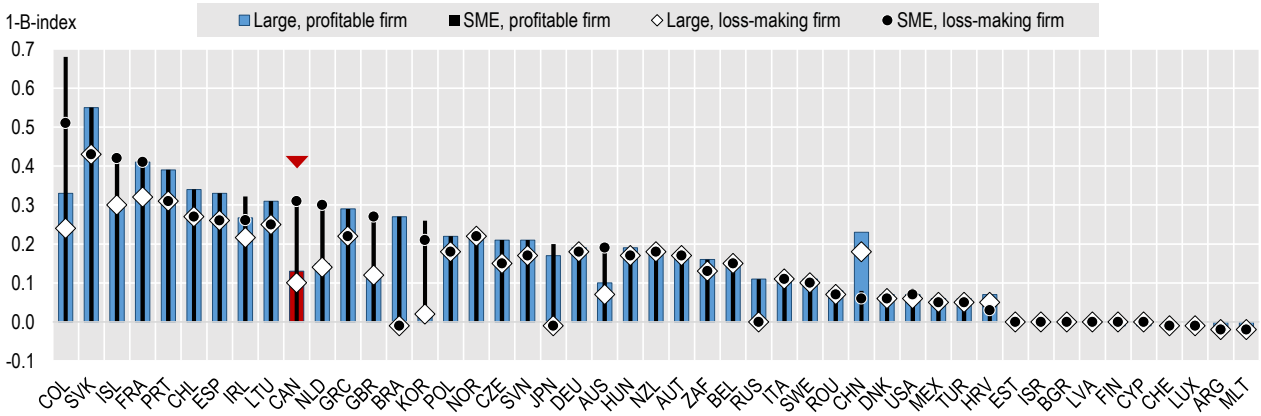
- In case of insufficient tax liability, unused credits can be carried-forward (back) for 20 (three) years.
- R&D tax credit is fully refundable for Canadian-controlled Private Corporations (CCPCs) at an enhanced rate of 35% on expenditures up to a limit of CAD 3 million (1 CAD= 0.642 EUR, Q3 2020).
- R&D expenses in excess of this threshold qualify for a tax credit at a reduced rate of 15% that is 40% refundable if its prior-year taxable income does not exceed its qualifying income limit for the business group. The qualifying income limit starts at CAD 500 000 and is reduced when prior-year taxable capital is between CAD 10 million and CAD 50 million.
- The expenditure limit of CAD 3 million is reduced as a function of the taxable capital in the previous tax year and fully phased out once a CCPC reaches a prior year taxable capital of CAD 50 million.
- In addition to Federal tax support, Canada offers provincial R&D tax credits that range from 3.5% (Ontario) to 30% (Quebec). Many provinces provide refundable credits.

Generosity of R&D tax support in 2020

Differences in the design of R&D tax incentives drive significant variation in the expected generosity of tax relief per additional unit of R&D investment. In 2020, the marginal tax subsidy rate for profit-making (loss-making) SMEs in **Canada** is estimated at 0.31 (0.31), well above the OECD median of 0.20 (0.18). The implied tax subsidy rate for large enterprises is 0.13 (0.10) in the profit (loss)-making scenario, close (equal) to the OECD median of 0.17 (0.15).

Figure 1. Implied tax subsidy rates on R&D expenditures: Canada, 2020

1-B-Index, by firm size and profit scenario



Note: Implied marginal tax subsidy rates, presented for different firm size and profitability scenarios, are calculated based on headline tax credit/allowance rates (see methodology and country-specific notes), providing an upper bound value of the generosity of R&D tax support, not reflecting the effect of thresholds and ceilings that may limit the amount of qualifying R&D expenditure or value of tax relief.
Source: OECD, R&D Tax Incentives Database, http://oe.cd/rdtax, March 2021.

Only Federal tax incentives are modelled – the SR&ED tax credit and accelerated depreciation for machinery and equipment used in the process of R&D (immediate write-off), available from 2000 to 2014. According to SR&ED eligibility purposes, SMEs correspond to CCPCs.

Recent developments in R&D tax relief provisions

Regular reforms of R&D tax incentives lead to continuous changes in the availability, scope and generosity of R&D tax incentives. Such reforms relate to the launch of new tax incentives, the R&D definition adopted for tax purposes, changes in tax credit and allowance rates, adjustments of thresholds or upper ceilings on qualifying R&D expenditure or tax relief amounts, or changes in the terms and availability of refunds.

In 2020, changes in the availability and scope of R&D tax incentives represented the most frequent type of policy reform (OECD, 2020), along with adjustments to the headline R&D tax credit/allowance rates and adjustments of thresholds or upper ceilings on qualifying R&D expenditure or tax relief amounts. In response to the COVID-19 pandemic, several countries increased the generosity of R&D tax relief or introduced modifications to the administration of R&D tax incentives to facilitate and accelerate R&D funding.

In 2020, **Canada** undertook **three changes** in its R&D tax relief provisions:

- Most refundable claims are to be processed as soon as possible with minimal burden on the claimants. Claims accepted at this time may be subject to review/audit at a future date to ensure eligibility. Small or medium businesses will generally not be contacted to initiate any SR&ED claim reviews.
- For claims due March 13, 2020 or later, the deadline to claim certain tax credits, including the SR&ED tax credit, has been extended to six months from the original due date or to December 31, 2020, whichever is earlier.
- The tax legislation was amended to grant Revenu Québec discretion to extend the time limit for filing applications for certain tax incentives, including the SR&ED tax credit, for up to one year following the otherwise applicable deadline.

All of these policy changes are related to the **COVID-19 outbreak**.

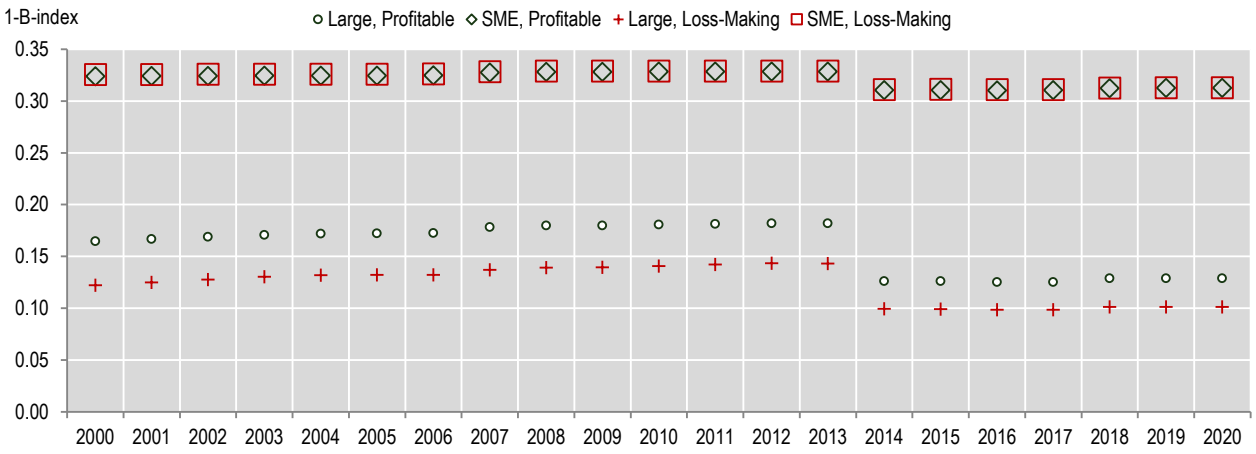
Trends in the generosity of R&D tax support

The generosity of federal R&D tax incentives has remained fairly stable in **Canada** over the 2000-20 period, with a reduction in implied R&D tax subsidy rates in 2014. In this year, the accelerated depreciation provision for machinery and equipment used in the process of R&D (immediate write-off) was abolished, capital expenditures and lease costs ceased to qualify for tax support under the SR&ED investment tax credit; and the general rate of the SR&ED investment tax credit was reduced from 20% to 15%.

This change in the rate of the tax credit did not affect SMEs which benefited from a fully refundable tax credit at an enhanced rate of 35% throughout the time period considered. If the SR&ED threshold applicable to SMEs is considered in the modelling of R&D tax subsidy rates, the rate for profitable (loss-making) SMEs slightly changes from 0.31 (0.31) to 0.31 (0.29).

Figure 2. Implied tax subsidy rates on R&D expenditures: Canada, 2000-20

1-B-Index, by firm size and profit scenario



Note: Implied marginal tax subsidy rates, presented for different firm size and profitability scenarios, are calculated based on headline tax credit/allowance rates (see methodology and country-specific notes), providing an upper bound value of the generosity of R&D tax support, not reflecting the effect of thresholds and ceilings that may limit the amount of qualifying R&D expenditure or value of tax relief.

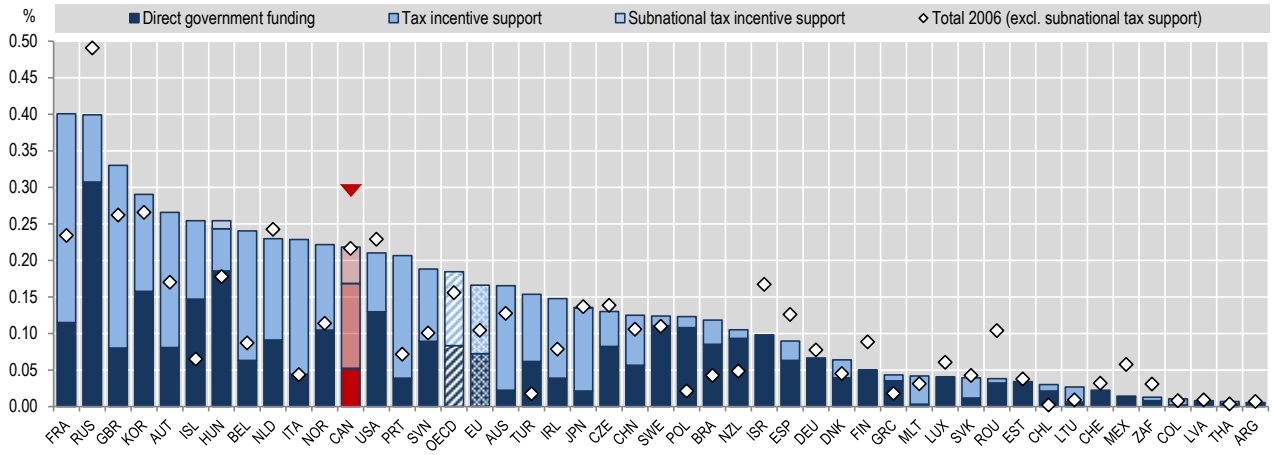
Source: OECD, R&D Tax Incentives Database, http://oe.cd/rdtax, March 2021.

Policy support for business R&D: the policy mix

In 2018, **Canada** is placed above the OECD average in terms of total government support to business R&D as a percentage of GDP, at a rate equivalent to 0.22% of GDP.

Figure 3. Direct government funding of business R&D and tax incentives for R&D, 2018 (nearest year)

As a percentage of GDP



Note: Data on subnational tax support are only available for a group of countries.

Source: OECD, R&D Tax Incentives Database, http://oe.cd/rdtax, March 2021.

Key points:

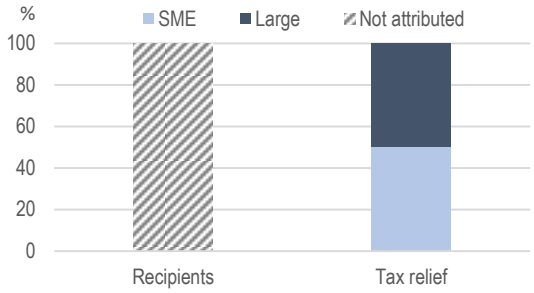
- From 2006 to 2018, government support for BERD (excluding subnational tax support) as a percentage of GDP decreased in **Canada** by 0.05 percentage point (pp), while the OECD average increased by 0.03 pp.
- During this period, business R&D intensity in **Canada** declined from 1.1% to 0.8%.
- In 2018, R&D tax incentives accounted for 76% of total government support for BERD in **Canada**.

Distribution of R&D tax relief recipients and government tax relief for R&D

The distribution of R&D tax relief recipients and government tax relief for R&D expenditures (GTARD) provide insights into what types of firms claim and benefit from tax relief.

Figure 4. Number of R&D tax relief recipients and value of government tax relief for R&D, 2017

By firm size*, share in percent



Note: Figures refer to the SR&ED tax credit. *SMEs are defined as Canadian Controlled Private Corporations (CCPCs).

Source: OECD, R&D Tax Incentives Database, http://oe.cd/rdtax, March 2021.

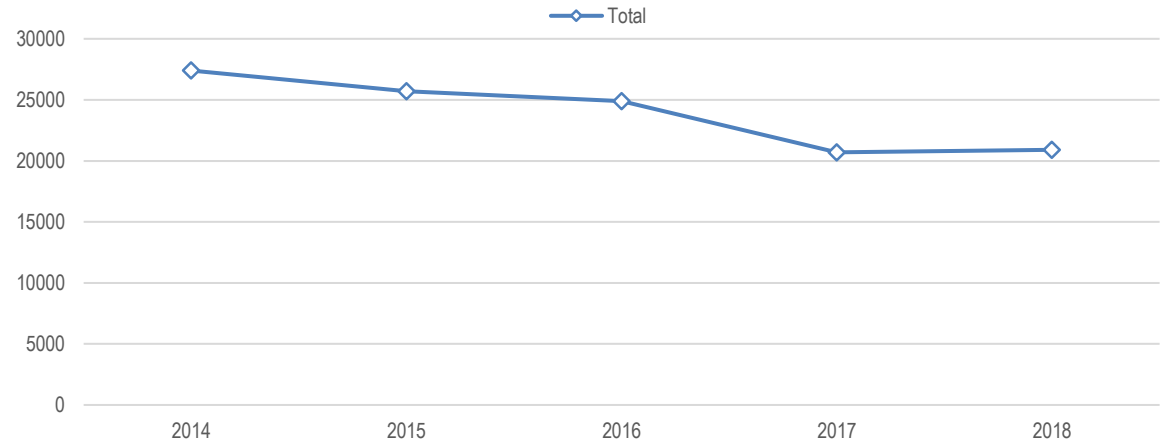
Key points:

- While data on the share of R&D tax relief recipients accounted for by SMEs vis-à-vis large firms are not available for **Canada**, the available breakdown for GTARD suggests that R&D tax support in **Canada** was evenly distributed between SMEs (CCPCs) and large firms, amounting to 50% each.

Trends in the uptake of R&D tax incentives

Over the period 2014-2018 (for which relevant data are available), the number of R&D tax relief recipients decreased in **Canada** by nearly 25%, from 27 400 in 2014 to 20 900 in 2018. Most of this decline is attributable to the year 2017 where this count reached 20 700, a decline of around 4 200 firms compared to 2016.

Figure 5. Number of R&D tax relief recipients, Canada, 2014-2018



Note: Figures refer to SR&ED investment tax credit.

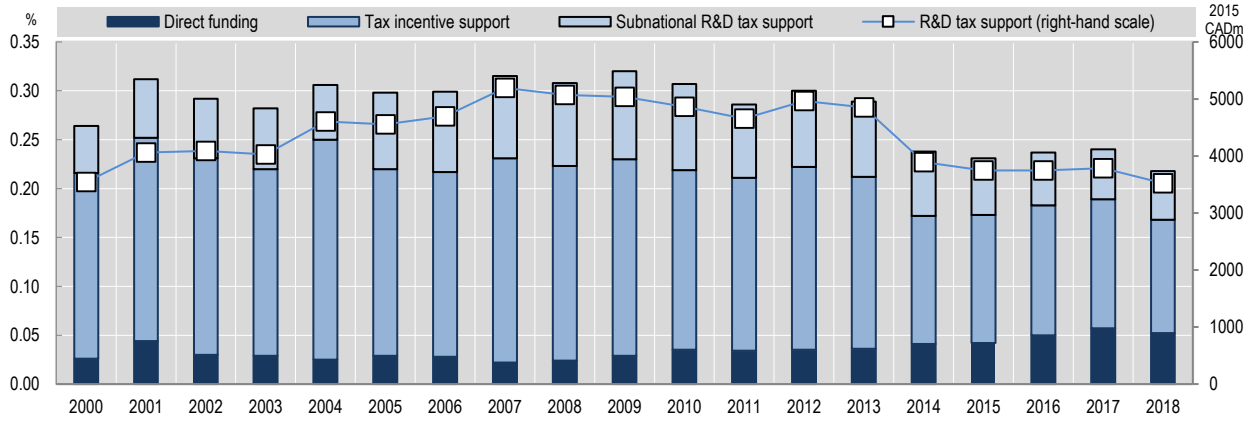
Source: OECD, R&D Tax Incentives Database, http://oe.cd/rdtax, March 2021.

Trends in government support for business R&D

Between 2000 and 2018, the importance of tax incentives has been very high in **Canada**, both in absolute and relative terms, with a rebalancing of the policy mix noticeable in more recent years.

Figure 6. Direct government funding of business R&D and tax incentives for R&D, Canada, 2000-18

As a percentage of GDP, 2015 prices (right-hand scale)



Source: OECD, R&D Tax Incentives Database, http://oe.cd/rdtax, March 2021.

- The cost of R&D tax relief declined (in 2015 prices) from CAD 4 695 million in 2000 to CAD 3 523 million in 2018. From January 2014, the base of eligible expenditures was narrowed by removing capital expenditures and lease costs. The SR&ED tax credit was also reduced from 20% to 15%.
- As a percentage of GDP, R&D tax support oscillated between 0.18% and 0.20% of GDP from 2008 to 2013, declined to 0.13% of GDP after the tax credit reform in 2014 to reach 0.116% of GDP in 2018.
- Direct funding of BERD increased from 0.03% to 0.05% of GDP between 2000 and 2018.
- The share of R&D tax incentives in total government support fluctuated between 88% and 92% over the 2008-13 period, dropping to 83% in 2014 and declining further to 76% in 2018. Subnational tax incentives accounted for 29-34% of total tax support for R&D during the 2008-18 period (30% in 2018).

Please cite this note as: OECD (2021). "R&D Tax Incentives: Canada, 2020", www.oecd.org/sti/rd-tax-stats-canada.pdf, Directorate for Science, Technology and Innovation, March 2021.