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R&D tax update

CRA releases draft examples to clarify SR&ED guidance

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On September 18, 2013, the Canada Revenue Agency (CRA) issued a new scientific research and experimental development (SR&ED) document for public consultation on the eligibility of work for the SR&ED program, with responses due by November 18, 2013. In this document, CRA has proposed **ten example cases** to illustrate key concepts of the CRA's policy as it relates to eligibility of SR&ED activities. The examples are intended to complement the policy documents relating to eligibility released in December 2012 as part of the SR&ED Policy Review Project. Prior to this time, the CRA's policy and related guidance documents contained a much larger and more specific set of examples, including industry specific examples that had been developed with the direct input of affected industries. Attempting to provide a similar level of clarity with a much smaller example set may be an optimistic objective. Taxpayers should carefully consider these changes to understand if and how these changes may affect their claims, and whether the examples provide sufficient clarity in relation to their SR&ED claims.

Deloitte is committed to fostering the development of clear, useful policy guidance that is consistent with the provisions of the Income Tax Act and the historical intentions of the SR&ED program. We welcome this consultation initiative and hope that it results in strong renewed engagement with industry to ensure that the proposed guidance reflect a taxpayer's need for clarity and relevance. We will be providing feedback to the CRA, and encourage taxpayers affected by this new policy guidance to do the same. We believe that it is important that affected parties engage with the CRA on this matter; examples are a key method by which the public can develop an understanding of SR&ED eligibility, and by which the CRA reviewers will apply the policy.

In our view, it is particularly important to ensure that the examples accurately reflect the intent of the SR&ED program, while clarifying the applicable requirements and boundaries. It is equally important that the examples be universally applicable given the removal of industry specific guidance, without prejudice towards any industry or type of research. Furthermore, it is also essential that these examples be pertinent to real-world applications, and not over-simplified for the convenience of a small number of examples. In other words, they must reflect the natural complexities of work undertaken by Canadian industry, and not simply idealized situations. To this end, we have identified a number of potential issues for SR&ED claimants in these examples and will be corresponding accordingly with the CRA.

In providing your own feedback, we suggest that you take into consideration the following:

- Which examples provide clear distinction of eligible and ineligible activities in relation to your business and your research? Which do not?
- In its 2012 policy release, the CRA introduced an extensive lexicon that provides specific definitions to certain commonly used terms that may not reflect the common definition of these terms as used in industry (e.g. technical vs. technological). The current examples reinforce these definitions. Does the terminology used reflect your understanding of the related terms, and how do you anticipate that the use of this terminology will impact the ability of your technical staff to convey the eligibility of the work undertaken by your organization upon review? Does the terminology aid or detract from your understanding of the underlying issues, i.e. the existence or not of a logical, systematic link between the activities and an attempt to resolve technological uncertainty; and whether or not the work develops new, or enhances the understanding of, the capabilities of the associated technology?
- When creating examples such as these, it is important to be as simple and clear as possible. However, too much simplification can render the example unusable in real-world situations. Do the examples adequately simplify the question without loss of relevance to the complexity of your real-world projects? Some elements to consider when addressing this question might include:
 - Are any examples so obvious as to add little or no value to your understanding?
 - Are the examples balanced so as to assist the taxpayer in drawing the line between included and excluded activities, or does it simply exclude certain generalized types of activities?
 - Do the examples provide useful insight into more complex situations, i.e. where the work involves more than one technology, the integration of multiple technologies or other system-related challenges? Do they help to understand the technological level at which such projects should be claimed?
 - Do the examples provide useful insight to the segregation of eligible and non-eligible activities within an SR&ED project conducted as part of a larger company project (e.g. plant trials, custom products, etc.)?
- Do the examples adequately address eligibility in technology development situations versus scientific research situations?
- Do the examples adequately clarify the treatment of “support activities” and the distinction between such activities conducted independently from and regardless of the SR&ED project versus those undertaken as an integral part of an SR&ED project?
- Is there sufficient broad representation of different industries? We note, for example, that there are no software development examples.

We are interested in understanding your perspective on the proposed changes, and in understanding how these and other recent changes are affecting your SR&ED benefits. To this end, we would be pleased to help you formulate recommendations in association with your own submission, or to incorporate your perspective within our own responses.

We can also assist you with clear guidance on how to apply the provisions of the SR&ED program in your business and industry, and in interpreting published policy in your specific situation, including the proposed examples.

Should you wish to discuss these, or any other matters related to SR&ED, please contact any of the Deloitte practitioners noted or your local Deloitte SR&ED consultant.

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