R&D Tax Incentives: Canada

1. Public support for business R&D: the mix of direct funding and tax relief

Governments in many countries seek to promote R&D investment in the economy by granting a preferential tax treatment to eligible R&D expenditures, especially those incurred by firms. In 2016, 29 of the 35 OECD countries, 22 of 28 EU countries and a number of non-OECD economies offer R&D tax incentives.

Figure 1. Direct government funding of business R&D and tax incentives for R&D, 2014 (nearest year)
As a percentage of GDP


Main points:
- Canada ranks among the top third of OECD and other major economies in terms of the total volume of (central) government support for business R&D, equivalent to 0.18% of GDP.
- Tax incentives account for 83% of total public support for business R&D in Canada.
- From 2006 to 2014, R&D tax support as a percentage of GDP decreased in Canada by 0.04 percentage points, while the OECD median increased by 0.02 percentage points.

2. Trends in government support for business R&D

Over the last decade, several OECD countries have increased their reliance on R&D tax incentives. However, this trend has not been uniform. The relative importance of tax incentives declined briefly following the global financial crisis, reflecting the demand-led nature of tax relief and its dependence on profits.

Figure 2. Direct funding of business R&D and tax incentives for R&D, Canada, 2000-14
As a percentage of GDP, 2010 prices (right-hand scale)


Main points:
- In Canada, R&D tax support increased slightly from CAD 2.6 billion in 2000 to CAD 2.8 billion in 2014.
- As percentage of GDP, tax support remained fairly stable between 2000 and 2007 following which it steadily declined from 0.21% of GDP in 2007 to 0.15% in 2014.
- Direct funding of BERD increased from 0.026% to 0.034% of GDP during this period.

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1 This document and any map included herein are without prejudice to the status of or sovereignty over any territory, to the delimitation of international frontiers and boundaries and to the name of any territory, city or area. The statistical data for Israel are supplied by and under the responsibility of the relevant Israeli authorities or third party. The use of such data by the OECD is without prejudice to the status of the Golan Heights, East Jerusalem and Israeli settlements in the West Bank under the terms of international law.
2 The estimates for Canada presented in this note exclude the cost of provincial tax credits for research and innovation, worth in excess of CAD 1.5 billion in 2014.
3. Design of R&D tax incentive support

Countries differ in the extent to which they rely on tax measures to support R&D, and those that do design tax relief measures in substantially different ways. Key design features relate to the type of tax instrument, eligible R&D costs, provisions for firms with insufficient tax liability, ceilings and thresholds among others.

### Table 1. Main design features of R&D tax incentives

<table>
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<tr>
<th>Tax incentive</th>
<th>Scientific research and experimental development (SR&amp;ED) tax credit</th>
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<tbody>
<tr>
<td>Type of instrument</td>
<td>Volume-based</td>
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<td>Eligible expenditures†</td>
<td>Current</td>
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<td>Headline rates (%)</td>
<td>15 (35 CCPCs)</td>
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<td>Refund</td>
<td>Immediate (only CCPCs*)</td>
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<td>Carry-over (years)</td>
<td>20 (carry-forward), 3 (carry-back)</td>
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<td>Thresholds &amp; ceilings</td>
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<tr>
<td>Base amount</td>
<td>CAD 3 million (CCPCs: excess expenditure eligible for 15% tax credit)</td>
</tr>
<tr>
<td>Refund-specific</td>
<td>CAD 3 million (CCPC)*</td>
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CCPC: Canadian Controlled Private Corporation; †: In excess of CAD 3 million, expenditure is eligible for a 15% tax credit that is 40% refundable for CCPCs below phase-out range (below CAD 500k in prior year taxable income and below CAD10m in prior year capital); else no refund.

1For additional information: OECD R&D Tax Incentive Compendium and Eligibility of current and capital expenditure for R&D tax relief


**Main points:**
- Canada’s Federal Government provides R&D tax relief through a volume-based R&D tax credit.
- 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 CCPCs at an enhanced rate of 35% up to a CAD 3 million expenditure limit. R&D expenses in excess of this threshold qualify for a credit at reduced rate of 15% that is 40% refundable for CCPCs below the phase-out range.
- The expenditure limit of CAD 3 million is fully phased out once the CCPC reaches a prior year taxable income of CAD 0.8 million or a prior year taxable capital of CAD 50 million.

4. Generosity of R&D tax support

The design of R&D tax incentives influences the "expected" generosity of tax relief per additional unit of R&D investment. Across OECD and partner economies providing tax relief, there is a significant variation in tax subsidy rates for firms of different size and profitability.

![Figure 3. Implied tax subsidy rates on R&D expenditures, 2016](http://oe.cd/rdtax)

**Main points:**
- In Canada, the marginal R&D tax subsidy rate for SMEs is estimated at 0.30 (0.29) in the profit (loss-making) scenario; significantly above the OECD median of 0.18 (0.11) for profitable (loss-making) SMEs.
- The tax subsidy rate for profitable (loss-making) large enterprises in Canada is 0.13 (0.10); larger than (close to) the OECD median of 0.11 (0.09) for profitable (loss-making) large enterprises.