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An Introduction to the Scientific Research and Experimental Development Program

Your opinion counts!

We review our income tax guides and pamphlets each year. If you have any comments or suggestions to help us improve our publications, we would like to hear from you.

Please send your comments to:

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Introduction

The Government of Canada has established a tax incentive program to encourage Canadian businesses of all sizes to conduct research and development that will lead to new or improved technologically advanced products or processes. This program is called the Scientific Research and Experimental Development (SR&ED) Program. It is the largest single source of federal government support for industrial research and development.

Canada Revenue Agency (CRA) administers the program through its offices in all provinces. The objectives of the CRA are to promote the program and to stimulate Canadian SR&ED by quickly and consistently delivering these incentives to all companies that carry out eligible work.

The SR&ED Program gives claimants cash refunds and/or tax credits for their expenditures on eligible research and development work done in Canada. This brochure provides general information on the program, outlines eligibility requirements, filing requirements, and services available and clarifies those areas of research and development that qualify for the SR&ED incentives.

For more information, visit our Web site at www.cra.gc.ca/sred.

What work is eligible?

To be eligible for SR&ED incentives, work must meet the legislative definition of “scientific research and experimental development.” The work must fall into one of the following categories:

- **Experimental development** – This is the work done to achieve technological advancement to create, or improve, new materials, devices, products, or processes. Most SR&ED claims involve experimental development.
- **Applied research** – This is work done to advance scientific knowledge with a specific practical application in view.
- **Basic research** – This is work done to advance scientific knowledge without a specific practical application in view.
- **Support work** – This is work that directly supports and is commensurate with the needs of experimental development, applied research, and basic research. This includes only the following 8 specific types of work:
 - engineering;
 - design;
 - operations research;
 - mathematical analysis;
 - computer programming;

- data collection;
- testing; and
- psychological research.

Eligible work may be done either by you, or on your behalf.

Only SR&ED done in Canada qualifies under the program. When work is carried on both inside and outside Canada, only expenditures for work done in Canada that meets the definition of SR&ED will be eligible for the incentives.

What are the eligibility criteria?

While there are definitions of “research and development” outside the scope of the SR&ED Program, only work that meets the previous definition and the following three criteria qualifies as SR&ED.

1. **Scientific or technological advancement** – The work must generate information that advances the understanding of scientific relations or technologies.
2. **Scientific or technological uncertainty** – Whether a given result or objective can be achieved, or how to achieve it, is unknown or cannot be determined based on generally available scientific or technological knowledge or experience.
3. **Scientific and technical content** – There must be evidence that qualified personnel with relevant experience in science, technology, or engineering have conducted a systematic investigation through experiment or analysis.

What work is not eligible?

Certain work is not eligible for benefits under the SR&ED Program, including:

- research in the social sciences or the humanities;
- commercial production of a new or improved material, device, or product, or the commercial use of a new or improved process;
- style changes;
- market research or sales promotion;
- quality control or routine testing of materials, devices, products, or processes;
- routine data collection; and
- prospecting, exploring, or drilling for or producing minerals, petroleum, or natural gas.

What does the SR&ED Program offer?

The SR&ED Program provides the following incentives:

- You can deduct current and capital SR&ED expenditures to reduce your tax liability in the current year or carry these expenditures forward indefinitely to reduce your tax liability in future years.
- You can receive investment tax credits on qualifying expenditures through a cash refund, a reduction of taxes payable, or both. The unused investment tax credits can be carried back 3 years, or forward 10 years if the investment tax credits were earned prior to 2006, 20 years if they were earned after 2005.

The businesses that benefit from the SR&ED Program fall into three groups:

1. qualifying Canadian-controlled private corporations (refundable and/or non-refundable tax credits);
2. other Canadian corporations (non-refundable tax credits); and
3. Proprietorships, Partnerships, and Trusts (refundable and/or non-refundable tax credits).

Expenditures for SR&ED conducted in Canada may include wages, materials, equipment, some overheads, SR&ED contracts, and third party payments.

Investment tax credit rates

The investment tax credit rates and the percentage that you can have refunded vary according to the type of business you conduct. For more information on this subject, see Appendix.

Qualifying Canadian-controlled private corporations (CCPC)

If you are a qualifying CCPC, you may receive a refundable investment tax credit of 35% of your qualified SR&ED expenditures. This is called a refundable claim and may entitle you to a cash refund. You must first apply these investment tax credits against taxes payable in the year of the claim. The 35% rate and refundability are subject to an expenditure limit of \$2 million.

After applying the tax credits against taxes payable, you can receive a cash refund on the balance of tax credits as follows:

- a full cash refund on tax credits calculated on qualified current SR&ED expenditures; and
- a 40% cash refund on tax credits calculated on qualified capital SR&ED expenditures.

Other Canadian corporations

For Canadian corporations other than qualifying Canadian-controlled private corporations, the investment tax credit rate for qualified SR&ED expenditures is 20% for both current and capital expenditures. While these credits are non-refundable, they may be carried back 3 years, or carried forward 10 years if earned before 2006, 20 years if earned after 2005, to reduce tax liability.

Proprietorships, Partnerships, and Trusts

If you fall into one of these categories, you can earn investment tax credits at the rate of 20% of qualified current and capital SR&ED expenditures. After applying these credits against taxes payable, you can get a cash refund on 40% of the balance of the tax credits.

What services are available to claimants?

First Time Claimant Service

The First Time Claimant Service is designed to help companies new to the SR&ED Program. You can visit the SR&ED Web site at www.cra.gc.ca/sred to view SR&ED publications, or request an information kit from a tax services office in your area. In addition, SR&ED staff can be contacted to answer questions and are also available to visit your business to explain the program and its requirements in more detail. You can also attend one of the public information seminars that the CRA regularly holds at locations across Canada. Please contact your local tax services office for more information.

Preclaim Project Review Service (PCPR)

PCPR is an optional service that provides an “up-front” review and preliminary opinion on the eligibility of work for SR&ED tax credits. The service is provided before SR&ED is claimed or even before the work is undertaken.

The PCPR service was developed as part of the CRA’s on-going efforts to make the SR&ED Program more responsive to your business needs. Through this service, you will learn which of your company’s research and development (R&D) projects are eligible for SR&ED tax credits. You also receive valuable guidance from an SR&ED Program expert about the proper way to substantiate your company’s SR&ED claim.

Account Executive Service

The Account Executive Service is optional, and provides your company with a designated contact person from the SR&ED Program. Called an Account Executive, this contact acts as your company’s single point of contact for any questions you may have or any guidance you may need about the SR&ED

Program. Ideally, the Account Executive Service provides your company with continuity from year to year, enabling you to more fully understand the SR&ED Program, its requirements for technical eligibility and substantiation, and the claim review process. This service also provides:

- briefings for your staff about the program and its requirements;
- help in identifying your company's eligible work;
- advice on substantiation requirements, claim preparation and submission, as well as on the review process; and
- assistance to help you take advantage of other SR&ED advisory services, such as Preclaim Project Review.

Applying for SR&ED incentives

To claim benefits under the SR&ED program, you must complete the following forms: Form T661, *Claim for Scientific Research and Experimental Development Expenditures (SR&ED) Carried on in Canada*; and Form T2 SCH 31, *Investment Tax Credit – Corporations* or Form T2038 (IND) *Investment Tax Credits (Individuals)*.

You should file the appropriate forms with your tax return. If that is not possible, you must file the form no later than 12 months after the filing due date of your tax return. Generally, as a corporation, you have 6 months after the end of your fiscal year to file your tax return, so you will have a total of 18 months from the end of the taxation year in which you incurred the expenditures to file the forms.

To make it simpler to prepare your claim, we recommend the person in charge of research and development in your organization be responsible for the technical information for your submission and the person responsible for financial matters provide the expenditure details. You need to determine what research and development work in your company qualifies as SR&ED, to describe that work, and to identify the associated costs.

Processing targets

All claims are subject to a review to determine if a complete claim can be processed as filed or if further review is necessary.

For refundable claims, our goal is to complete the review process within 120 days of receiving a complete claim.

For non-refundable claims, our goal is to complete the review within 365 days of receiving a complete claim.

For refundable claims related to adjustments requested to income tax returns that have been previously filed, our goal is to complete the review process within 240 days of receiving a complete claim.

For non-refundable claims related to adjustments requested to income tax returns that have been previously filed, our goal is to complete the review process within 365 days of receiving a complete claim.

The above standards apply in those situations where a complete claim has been filed and any requests for additional information have been addressed.

The CRA relies on your co-operation to meet these objectives. To ensure the review process goes smoothly, the CRA asks that you:

- maintain the technical and financial documents needed to substantiate the claim;
- submit your claim with your income tax return; and
- respond in a timely manner to CRA requests for more information.

Review procedures

The CRA's technical and financial review staff delivers the SR&ED Program. They work as a team to review claims and ensure that you receive the tax credits to which you are entitled in a timely manner.

The technical reviewer evaluates the work to determine whether it meets the SR&ED eligibility criteria. The financial reviewer looks at the costs associated with your projects to ensure they are SR&ED expenditures. These reviews may involve a site visit.

All information provided to the technical and financial review staff is held in strictest confidence. Legislative provisions and stringent rules protect the confidentiality of all claimants' records.

To expedite your claim and deliver your tax credits as quickly as possible, it helps if you provide CRA's reviewers with the technical and financial information that substantiates your claim at the beginning of their review. That is why the CRA encourages you to maintain all your evidence, documentation, and records for each of the projects you are claiming. This information could include project records, such as notebooks, project progress reports, draftings, and lab test results that verify the technical aspects of your SR&ED work, as well as financial records that verify SR&ED costs.

For detailed information on the review process, please see the *Guide to Conducting a Scientific Research and Experimental Development Review*, which is available on our Web site at www.cra.gc.ca/sred.

What are your responsibilities and entitlements?

To qualify for SR&ED tax incentives, you have to file the claim within 18 months from the end of the taxation year in which you incurred the expenditures. In processing and reviewing the claim, CRA staff are committed to:

- treating you fairly through due process;
- providing service in the official language of your choice;
- protecting your confidential information; and
- providing access to impartial redress if there is a dispute.

Guidelines for resolving claimants' SR&ED concerns

If a dispute arises during the review process, the SR&ED Program management will work with you to address all concerns. You may refer to the latest version of the Application Policy SR&ED 2000-02, *Guidelines for resolving claimants' SR&ED concerns*, for more information.

Appeals

If you disagree with the decision on your SR&ED claim, the *Income Tax Act* gives you the right to file a Notice of Objection. You will find details on objection and appeal procedures in the latest version of *Your Appeal Rights Under the Income Tax Act*. Once you file your objection, the case is referred to an appeals officer in the CRA's Appeals Division, who will give your objection a fair and impartial review.

Legislative references

The SR&ED Program is governed by sections 37, 127, 127.1, 164, and 248 of the *Income Tax Act* and sections 2900, 2902, and 2903 of the *Income Tax Regulations*.

Additional SR&ED reference material

General information on filing your claim can be found in the *Guide to Form T661, Claiming Scientific Research and Experimental Development Expenditures*.

Information on the eligibility criteria for SR&ED technical work and related expenditures are outlined in detail in the latest versions of the CRA's Information Circular 86-4, *Scientific Research and Experimental Development* and Interpretation Bulletin IT-151, *Scientific Research and Experimental Development Expenditures* respectively. You can obtain copies of these publications through your CRA tax services office. You can also obtain program information, policies, and publications on the SR&ED Web site at www.cra.gc.ca/sred.

Contacts

The CRA delivers the SR&ED Program through 10 coordinating tax services offices.

Coordinating tax services offices:

Halifax 1557 Hollis Street, 10th floor
P.O. Box 638,
Halifax NS B3J 2T5
Telephone: (902) 426-2386
1 (866) 433-5986
Fax: (902) 426-4727

Québec 94 Dalhousie Road
P.O. Box 1787
Québec QC G1K 7L3
Telephone: (418) 648-7151,
1 (866) 204-0101
ext. 648-7151
Fax: (418) 648-5663

Laval 3400 Ave Jean-Béraud
Laval QC H7T 2Z2
Telephone: (514) 338-4198
1 (888) 784-8709
Fax: (514) 338-4564

Montréal 305 Blvd. René Lévesque W.
Montréal QC H2Z 1A6
Telephone: (514) 496-1317
Fax: (514) 496-6607

For tax service offices in:

Bathurst, Charlottetown,
Halifax, Moncton, Saint
John, St. John's, Sydney

Chicoutimi, Québec,
Rimouski, Sherbrooke,
Trois-Rivières

Laval, Rouyn-Noranda,
Outaouais

Montréal,
Montréal/Rive-Sud

Ottawa	333 Laurier Avenue W. Ottawa ON K1A 0L9 Telephone: (613) 598-2106 Fax: (613) 952-1856	Belleville, Kingston, Nunavut, Ottawa, Peterborough, Sudbury, Thunder Bay
Toronto-Centre	1 Front Street W. Toronto ON M5J 2X6 Telephone: (416) 973-2814 Fax: (416) 952-8334	Toronto Centre, Toronto East, Toronto North
Toronto West	3rd Floor 5800 Hurontario Street P.O. Box 6000 Mississauga ON L5A 4E9 Telephone: (905) 566-6010 Fax: (905) 566-6154	Toronto West
Hamilton	55 Bay Street N. P.O. Box 2220 Hamilton ON L8N 3E1 Telephone: (905) 572-2650 Fax: (905) 570-8247	Hamilton, Kitchener/Waterloo, London, St. Catharines, Windsor
Calgary	220-4th Avenue S.E. Calgary AB T2G 0L1 Telephone: (403) 691-5890 Fax: (403) 691-6625	Calgary, Edmonton, N.W.T., Regina, Saskatoon, Winnipeg
Vancouver	1166 West Pender Street Vancouver BC V6E 3H8 Telephone: 1 (866) 317-0473 Fax: (604) 691-3872	Burnaby, Northern B.C., Southern Interior, Vancouver, Vancouver Island, Yukon

Appendix – Summary of investment tax credit rates

The following table outlines the tax credit rates that apply to qualified SR&ED expenditures.

	Investment tax credit rate	Rate of refundability	
		Current	Capital
Qualifying Canadian-controlled private corporations*			
<i>Taxable income of previous year less than or equal to \$300,000: †</i>			
■ Up to \$2 million in expenditures	35%	100%	40%
■ Remaining expenditures	20%	40%	40%
Other Canadian-controlled private corporations			
<i>Taxable income of previous year between \$300,000 and \$500,000: †</i>			
■ Expenditures below the expenditure limit**	35%	100%	40%
■ Expenditures over the expenditure limit	20%	–	–
Other corporations	20%	–	–
Proprietorships, Partnerships, and Trusts	20%	40%	40%

* The limits are for the 2006 calendar year and are affected when the corporation is associated with another corporation and when the taxable capital the corporation employs in Canada is more than \$10 million.

** The maximum expenditure limit is \$2 million per year. This limit is reduced by \$10 for every \$1 of taxable income in the previous year above \$300,000. †

† Effective for taxation years that start in 2008 or if there is more than one taxation year in 2007, effective from the second taxation year in 2007, the references to \$300,000 and \$500,000 should be \$400,000 and \$600,000 respectively.

Note

A partnership earns investment tax credits at the rate of 20%. These credits are then allocated to the partners.