

Connecting Vision to Reality*

2008 Report on Emerging Canadian Software Companies:
The CEO Perspective

SR&ED

Mel Machado

May 13, 2008



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Agenda / Contents

SR&ED Legislative Changes

Single Administration of Ontario Corporate Tax



SR&ED Legislative Changes Federal Budget February, 2008

Expenditure Limit Increased From \$2M to \$3M

- Prior Year Taxable Income phase out range (upper limit) increased from \$600,000 to \$700,000
- Prior Year Taxable Capital phase out range (upper limit) from \$15M to \$50M



SR&ED Legislative Changes (Continued)

SR&ED Carried on Outside Canada

- Salary and wages incurred for SR&ED outside Canada qualifies
- Conditions for eligibility:
 - Salary and wages of claimant's employees
 - Work must be directly undertaken by the claimant
 - SR&ED must be related to the business of the claimant
 - Work must be solely in support of SR&ED carried on in Canada
- Expenditure limited to 10% of total salary and wages incurred in respect SR&ED carried on in Canada



SR&ED Legislative Changes – Ontario

Expenditure limit increased to \$3M from \$2M

Taxable income same as the revised Federal limits

Taxable capital phase out range remains at \$25M to \$50M

Single Administration of Ontario Corporate Tax – Strengthening Business through a Simpler Tax System Act, 2007



CRA will Administer:

- Corporate Income Tax
- Corporate Minimum Tax
- Capital Tax
- Ontario Special Additional Tax (OSAT)

Ontario will continue to administer:

- Mining Tax Act
- Insurance premium taxes
- Electricity Act payments-in-lieu of corporate taxes



Single Administration of Ontario Corporate Tax – Harmonized Return

- Ontario taxpayers will be required to file a harmonized T2 Corporations Income Tax Return for taxation years ending after December 31, 2008
- Ontario Research and Development Tax Credit (ORDTC) is a 4.5% non-refundable tax credit on eligible expenditures incurred in a taxation year that ends after 2008



Harmonized Return (continued)

- Tax pools will assume the Federal value resulting in a tax credit or additional Ontario tax (tax debit)
- For Ontario purposes, SR&ED Claimants may have used their Ontario SR&ED pool to reduce their Ontario Taxes
- Federal SR&ED pool balance could exceed its Ontario SR&ED pool balance, making it liable for a transitional debit (tax debit)
- For SR&ED Performers there is an opportunity to defer the payment of the tax debit for 7 years

Thank you

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Greg McIntosh
May 13, 2008



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About Cyence

Privately held, venture capital funded

Provide commercial software to the financial services industry

Technology stack is Microsoft – top to bottom

License software behind the client's firewall and through an ASP model

Annual product R&D budget of \$.5 – 1.0 million

All development and ancillary activities is performed in Canada



Our Experience with SRED

Overview

- Claimed since 2002 – 2005; received refunds for > 90%

Submission

- Used external support

Technical Reviews

- CRA uses experts with reasonable skepticism

Financial Reviews

- Relatively straight forward if your records are adequate



Issues in running an R&D operation

Identifying research that is eligible for credits by CRA definition

“Did we advance our understanding of something technical because the information/expertise was not freely available on the web or elsewhere.”



Issues in running an R&D operation

Advancement

- difficult to identify activities that are a pursuit in innovation or present unusual technical roadblocks where solutions don't already exist
- overruns resulting from technical issues are a good indicator
- may not be 'seen' in the end product (i.e. tools, performance enhancements)



Issues in running an R&D operation

Uncertainty

- Just because 'you' are uncertain doesn't make it research
- Eligibility may exist when alternative solutions are present or when the outcome is in doubt altogether
- Documenting the technical uncertainties appropriately
 - Alternative assessment, actions taken, costs incurred
- Advancement may not be new but uncertainty may still exist because of lack of public information (e.g. business rules engine)
- Porting to or development on new technologies is not enough
- Tracking the time spent from the time of uncertainty to the time the uncertainty is resolved



Issues in running an R&D operation

Content

- Content must be technical in nature
- Show IP ownership is retained in the contract
- Need to show that people performing the work are experienced or qualified
- Limited work outside Canada could qualify



Key Operational Learnings for SRED

- Educate yourself
- Don't wait until the 'big year'; develop experience / reputation
- Identify projects that may be eligible upfront and identify them (time system, code management tools)
- Documentation, documentation, documentation
- Develop templates for submissions
- Be diligent in submissions – **pride matters**
- Make the CRA reviewer's job easy
- Make improvements to your process after each submission
- Be compliant on all tax filings
- Use outside assistance

Thank you.

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