

Tax memo

Canadian tax updates



Ontario's Interactive Digital Media Tax Credit: Are you benefitting?

Provides details on
Ontario's
Interactive Digital
Media Tax Credit.

November 8, 2012

Ontario remains committed to the development of digital media in the province. It has provided ongoing support to the Emerging Technologies Fund and initiatives aimed at fostering a strong business environment for the Entertainment and Creative Cluster.

Recent studies (including the Canadian Interactive Alliances report "New Directions in the Financing of Digital Media") have noted that Canadian companies excel in creative and technological development but find it difficult to capitalize on their efforts. Firms that create digital media products and services have struggled to get the financial resources they need for growth.

To help companies develop digital media products, Ontario offers the Ontario Interactive Digital Media Tax Credit (OIDMTC) – a refundable tax credit. This *Tax memo* discusses in detail how the OIDMTC program works.

Background

Many provinces, including Ontario, have tax incentives to help companies develop digital media products. The following table outlines the history of OIDMTC refundable tax credit rates. As the bottom row shows, current rates for qualifying corporations are:

- 40% if they develop their own product; and
- 35% if they develop eligible products under a fee-for-service arrangement or are digital media game developers.

Qualifying expenditures incurred:		Products			
		1. Non-specified		2. Specified	3. Eligible digital games
		Qualifying corporation is:			
After	Before	Small	Other		
March 23, 2006	March 26, 2008	30%	20%		n/a
March 25, 2008	March 27, 2009		25%		
March 26, 2009	n/a	40%		35%	

Refundability is particularly important in the current economic environment, because the credit reduces the cost of development, so the company can enjoy the benefits even if it is not taxable.

Eligible claim periods

Applications can be made for current and previous tax year(s). However, the applicant may have to make a request to the Canada Revenue Agency (CRA) to amend a previously filed tax return. Requests must be made within the normal reassessment period:

	Normal reassessment period ¹
Canadian-controlled private corporations (CCPCs)	3 years
Other corporations	4 years

1. From date the CRA mailed the original notice of assessment for the tax year.

Administration

The OIDMTC program is jointly administered by the CRA and the Ontario Media Development Corporation (OMDC). The program provides refundable tax credits for eligible Ontario labour expenditures and eligible marketing and distribution expenditures incurred by Canadian taxable corporations (Canadian or foreign-controlled) with a permanent establishment in Ontario that develop interactive digital media products.

Upon receipt of an application and a fee equal to 0.1% of eligible expenditures (maximum \$2,000 fee), the OMDC will review the taxpayer's application and issue a certificate of eligibility if the various criteria are met. The refundability of the tax credits is handled through Ontario's corporate tax system, which is administered by the CRA.

Products eligible for the OIDMTC

This section discusses the types of products (see the table on page 1) that can be claimed under the OIDMTC. As mentioned, the OIDMTC is available in respect of the development of interactive digital media products. To be eligible, the product must:

- educate, inform or entertain; and
- present information using at least two of text, sound and images.

Eligible products include (but are not restricted to) games, and educational and informational products.

1. Non-specified products

For qualifying corporations that develop and market their own non-specified products, the credit is 40%.

Non-specified products are interactive products that are:

- developed all or substantially all by a qualifying corporation in Ontario;
- developed for sale or licensing by the qualifying corporation to one or more arm's length parties who have not previously entered into an arrangement with the qualifying corporation for the development of the product; and
- not used primarily for interpersonal communication, to present or promote the qualifying corporation or to present, promote or sell its products and services.

2. Specified products

For corporations that develop specified products the tax credit is 35%.

Specified products are interactive digital media products developed:

- all or substantially all by a qualifying corporation in Ontario;
- under a fee-for-service arrangement between the qualifying corporation and an arm's length purchaser;
- for the purpose of sale or license by the purchaser to one or more persons, each of whom deals at arm's length with the purchaser; and
- not to be used primarily for interpersonal communication, to present or promote the qualifying corporation or to present, promote or sell its products and services.

3. Eligible digital games

Games developed by qualifying developers

The credit is also 35% for qualifying digital game corporations that incur a minimum of \$1 million of directly attributable Ontario labour costs over a three-year period to develop an eligible digital game under a fee-for-service arrangement.

A qualifying digital game corporation is not required to develop 90% or more of the eligible digital game.

Games developed by specialized developers

The OITMC is 35% for specialized digital game corporations that:

- incur a minimum of \$1 million of Ontario labour expenditures in the taxation year of development; and
- have either 80% of Ontario payroll or 90% of annual revenues attributable to interactive digital game development.

A specialized digital game corporation is not required to develop 90% or more of the eligible digital game.

Eligible expenditures

The OITMTC can be claimed on the following types of expenditures:

	Expenditure ¹	
	Eligible labour ² (no maximum)	Eligible marketing and distribution expenditures (maximum of \$100,000 per eligible product)
Non-specified products		
All other		n/a

1. The expenditure must be paid in the taxation year or within 60 days thereafter.
2. Salaries and wages must be for employees resident in Ontario. Residency is determined by where the employee resided on December 31 of the previous year.

Eligible labour

Eligible labour expenditures must be directly attributable to the development of the product and paid for services rendered at a permanent establishment in Ontario. They are 100% of:

- salaries and wages for employees; and
- remuneration paid to arm's length persons who are not employees.

For specified and non-specified products, "persons" can include individuals, partnerships and corporations. For eligible digital games developed by qualifying digital game corporations and specialized digital game corporations, remuneration does not include amounts paid to another taxable

Canadian corporation for the services of its employees.

Eligible marketing and distribution expenses

Eligible marketing and distribution expenditures must be directly attributable to advertising or promoting the non-specified product or distributing it to customers or potential customers.

Timing of expenditures

The following table shows when expenditures must be incurred to be eligible for the OITMTC.

	Timing of expenditures from completion of product	
	Before	After
Ontario labour	Within 37 months	n/a
Marketing and distribution (non-specified products)	Within 24 months	Within 12 months

Other provinces

British Columbia and Manitoba also offer interactive digital media tax credits.

British Columbia

The Interactive Digital Media Tax Credit (IDMTC) program provides a refundable 17.5% tax credit on eligible qualified B.C. labour directly attributable to interactive digital media activity.

Manitoba

Manitoba offers a 40% refundable tax credit on eligible labour (maximum credit: \$500,000 for each project) for prototyping and product development.

For information on other programs for digital media, please refer to PwC's *The big table – Digital media and animation incentives in Canada* at www.pwc.com/ca/bigtable.

Effective use of the OIDMTC program

The high rates of refundable tax credits make the OIDMTC program extremely attractive and valuable to any company developing interactive digital media products.

The potential to reduce your after-tax cost of developing products or providing services should not be ignored. Every effort should be made to identify qualifying products and track associated costs to ensure that your tax credits are maximized. Claims can be submitted retroactively for all open Ontario tax years.

For more help

If you would like more information or to discuss how your company can take advantage of its full OIDMTC entitlement, please contact your PwC adviser or any of the following individuals.

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