



SR&ED: CHANGES TAKE AIM AT SME'S

Elliot Schiller, Ph.D, C.M.C.



The Scientific Research and Experimental Development Program (SR&ED) is the primary means by which the Harper Government supports domestic manufacturing. In its latest budget, the government estimated that the value of the program to Canadian manufacturers is approximately \$6 billion per year. Like most tax incentive programs, this one is extremely nuanced as the actual tax act (subsection 248(1) of the Income Tax Act) is less than 300 words, and leaves Canada's Revenue Agency (CRA) lots of room for interpretation.

What CRA Expects

When the taxpayer disagrees with CRA's interpretation, the courts eventually decide on what is the proper interpretation, and that precedent carries on until a contradictory court challenge. In the most recent high profile case, Airmax Technologies won its case against CRA, but, in its ruling, the courts reaffirmed the requirement for the taxpayer needing to maintain "relevant record keeping" during the experimental process. CRA has used this ruling to examine and reject many otherwise valid SR&ED claims ever since.

This ruling gives CRA the right to reject any claims where the documentation during the experimentation is not sufficiently detailed, and in so doing, takes aim at the small to medium sized enterprises (SME's) who often have only one or two SR&ED participants who use verbal analysis to carry on the experimental development, either to improve products or processes, but often do not put each step, finding, and next step hypothesis' in writing.

Forewarned is forearmed. If the taxpayer wants to receive the extremely lucrative often refundable tax credits that could represent almost 70% of the experimental costs, they will need to start documenting the process better, during the process, not after the fact.

Relevant Record Keeping

The scientific method is a method of procedures that characterizes how to conduct effective experimentation. It begins with the formulation of a question. (i.e. What if we alter this section of the assembly line, can we then increase production by 10%?). Next, it requires the gathering of information as to how to answer the question, or to see it has already been thought of and answered in the past, and the answer is readily available in the public domain (what CRA calls due diligence). Once the taxpayer is armed with knowledge, they then are expected to develop a hypothesis to solve the problem. By definition, a hypothesis is a proposed explanation that can be either verified or proved wrong by experimentation. Once experimentation begins, often, so does eligible SR&ED tax credit gathering begin. Whether the actual experimentation results in SR&ED eligible work or turns out to simply involves routine engineering, CRA has

the expectation that the original formulation of the question, the due diligence results, and the initial hypothesis are documented. Then, the results of each test to prove the hypothesis, the new formulation of a hypothesis based on these findings, and the new tests, and so on and so on are all documented.

In a large corporation perhaps there are enough personnel to stop and write down each experimental finding, but often, in an SME shop, the results of an experiment lead to an obvious follow up experiment and the experimental team is so lean and the work is so time sensitive, as to not have the luxury of a documenter. Therein lies the CRA "gotcha".

To solve this problem, as painlessly as possible, the taxpayer needs to instill some new disciplines onto the shop floor. There is lots of technology that can help. Who today doesn't have a phone that can take pictures or movies? Aren't there lots of computers close and if you don't want to type, isn't there lots of inexpensive dictation software available to help? For example our firm provides a structured software program to each of our clients that is cloud based that enables our clients to summarize the days' work simply and easily in a format that time and date stamps each entry and can even be made available to CRA to view the relevant record keeping from their offices via the cloud. Pictures and movies can easily be referenced as part of the documentation.

Summary

If you are still manufacturing in Canada, then you are innovating. That's a fact. And, another fact is that much of your innovation involves SR&ED eligible activities. While it was once acceptable to look back on the year and document your SR&ED activity after the fact, based on memory recollection, those days are gone. If you want to participate in the SR&ED program and take advantage of the close to 70% recovery of SR&ED costs, you need to provide CRA with evidence that you were documenting your work during the year on an ongoing basis. It sounds like a win-win situation to this writer. ■

Elliot Schiller, Ph.D, C.M.C. is a director at Teeger Schiller Inc. Teeger Schiller Inc. specializes in SR&ED Technical Submission Development, Systems Consulting and Change Management, and I.T./Policy Governance Consulting. Our clients include manufacturers, importers, wholesales', distributors, and retailers throughout North America. Teeger Schiller advises and works with our clients to ensure that companies achieve their goals.

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David Teeger

Director

David Teeger C.A., C.A. (S.A.) graduated as a Chartered Accountant in South Africa, and upon arrival in Canada he obtained his Canadian C.A. designation and joined Richter & Associates, a management consulting firm, where he concentrated his practice on various business sectors including household goods, fashion, automotive parts, public associations, and retail chains. He performed many roles in his 15 years at Richter, including managing the professional services organization in North America and all business operations throughout Europe.

David's professional capabilities include computer audits, feasibility studies, system analyses and assistance in the selection, negotiation and implementation of computerized solutions.

As a founding partner of Teeger Schiller Inc., he has focused his practice on consulting to management. His team of professionals has helped businesses select and successfully install a variety of ERP business solutions and add-on systems including business intelligence solutions to give new life to existing computer systems. David's clients not only rely on him to successfully manage the implementation of their new systems, but to manage the change that occurs in their organizations as a result of the use of these new tools.



Elliot Schiller

Director

Elliot Schiller, Ph.D., C.M.C. began his career as a Chemical Engineer working for Grumman Aircraft, in Long Island, New York. He obtained his Ph.D. at the University of Pittsburgh with funding from the U.S. Atomic Energy Commission, and, after being awarded a Presidential Fellowship, he went on to perform research and development activities at Brookhaven National Laboratory.

Since coming to Canada, he has primarily assisted consumer products and retail organizations in a variety of strategic management initiatives, traveling around the globe on behalf of his clients. In 1987, Elliot joined Richter & Associates, and it is here that he first met David Teeger.

As a founding partner of Teeger Schiller Inc., he has focused the SR&ED / Grant Division on obtaining grants and tax incentives for over 100 companies in the small to medium sized business sector. His team has provided services to the discrete / processing manufacturing, material development, textiles, apparel, automotive and computer sciences sectors. Annually, Teeger Schiller Inc. secures more than \$5 million in government funding to assist its clients in having their business initiatives supported by government funding.



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