
Draft Amendments to the Income Tax Act With Respect to Research and Development

Issued by
The Honourable Marc Lalonde
Minister of Finance

October 1983

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Foreword

A discussion paper entitled *Research and Development Tax Policies* was released at the time of the April 19, 1983 Budget. Since that date, consultations have proceeded with industry. This draft legislation is now being released as a result of that consultative process.

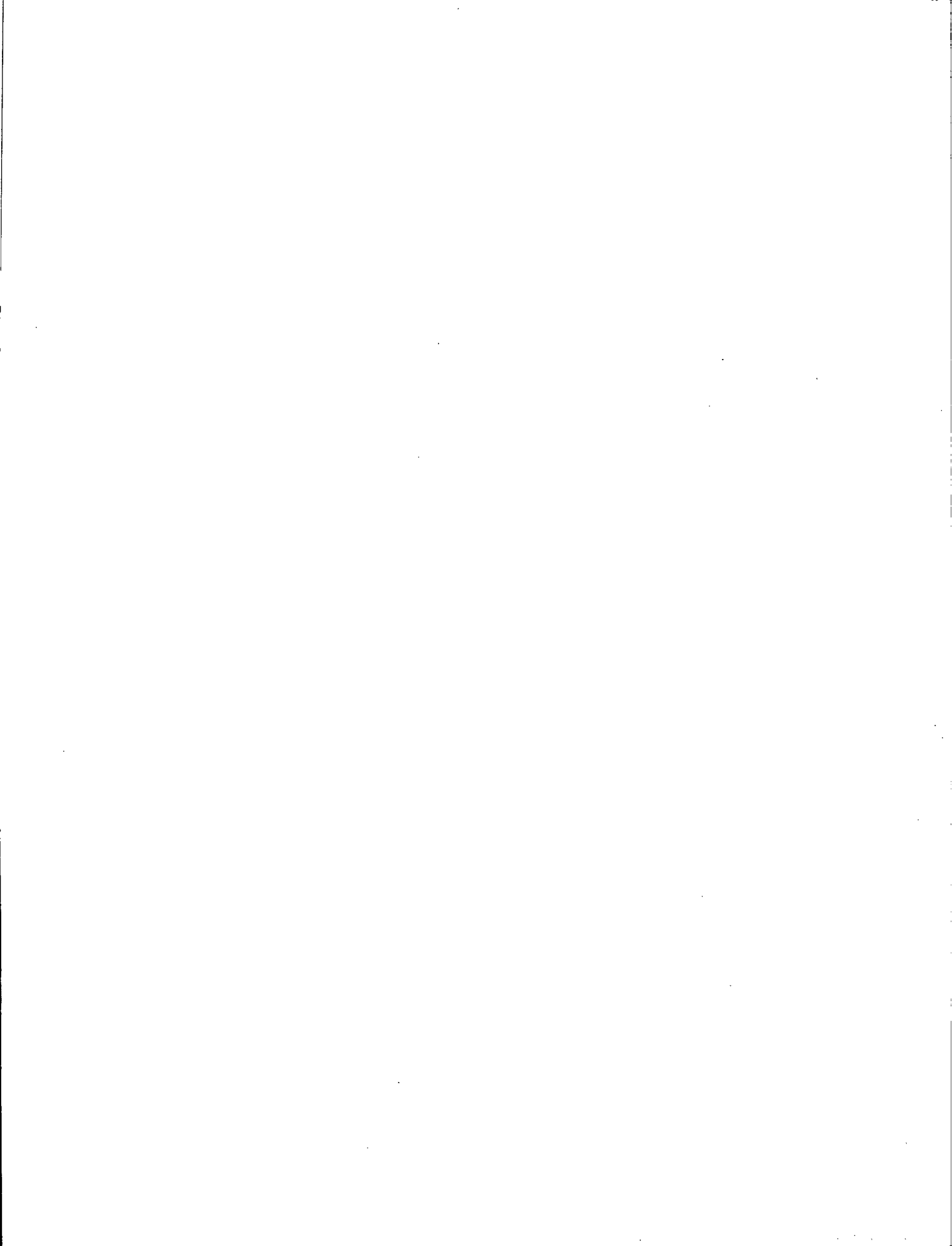
Publication of this draft will allow further comments to be made prior to the introduction of final legislation in the House. The draft legislation provides details of the changes that were proposed at the time of the Budget to enable firms and individuals affected to make appropriate plans in the current taxation year. As indicated in the consultative paper, the new tax provisions may apply to R&D investments in the current taxation year, at the taxpayer's option.

I would like to thank all those who offered valuable commentary to my officials both prior to and after the release of the April 19 paper.

The Honourable Marc Lalonde
Minister of Finance



Explanatory Notes



**Scientific Research
Deduction**
ITA
37(1)

Clause 1

Subsection 37(1) of the Act allows a taxpayer to deduct an amount for scientific research expenditures made in the current taxation year or previous taxation years to the extent that they have not previously been deducted.

New paragraph 37(1)(g) is added to the Act in consequence of the new scientific research tax credit financing mechanism, which is described in the commentary on new section 127.3 of the Act. Where this financing mechanism is used, the corporation is required to pay a special tax under Part VIII. However, this Part VIII tax may be refunded to the corporation when it renounces its right to deduct certain scientific research expenditures; \$1 of Part VIII tax is refunded for each \$2 of renounced expenditures. Paragraph 37(1)(g) is the provision which denies the deduction for these renounced expenditures. A corresponding amendment is also made to paragraph 127(10.1)(c) of the Act which prevents these renounced expenditures from qualifying for the investment tax credit. The new paragraph applies to the 1983 and subsequent taxation years.

**Additional Allowance
for Scientific Research**
ITA
37.1

Clause 2

Section 37.1 allows a corporation to deduct in a taxation year an amount equal to 50% of its incremental scientific research expenditures for the year. Subject to certain transitional provisions, this additional allowance is being eliminated for taxation years ending after October 1983. This additional allowance is replaced with an enhanced investment tax credit which is described in the commentary on new paragraph 127(11.1)(c) of the Act.

Clause 2 provides a transitional rule for taxation years that include November 1, 1983 and for grandfathered expenditures described in subparagraphs (b)(i) and (ii) of Clause 2. Where a corporation's taxation year includes November 1, 1983, it may elect to have section 37.1 apply in respect of all of its scientific research expenditures for the year. A separate rule applies in respect of grandfathered expenditures to allow only a proportion of the additional allowance otherwise determined – the proportion being the ratio of grandfathered expenditures to total scientific research expenditures in the year.

Example

Total R&D Expenditures	\$500
Incremental R&D Expenditures	\$300
Grandfathered R&D Expenditures	\$250
Additional Allowance otherwise determined – 50% of \$300 =	\$150
Additional Allowance $\frac{250 \times 150}{500}$ =	\$ 75

Capital Loss in Respect
of Unused Scientific
Research Tax Credit
ITA
39(8)

Clause 3

Subsection 39(8) of the Act has been added as a consequence of the introduction of the scientific research tax credit as provided in new section 127.3 and Part VIII of the Act. Where a taxpayer is unable to utilize any portion of his scientific research tax credit for a year, the unused portion of the credit is treated under this subsection as a capital loss for that year. This subsection applies to the 1983 and subsequent taxation years.

Capital Properties Cost
Base Adjustments

Clause 4

Subclause 4(1)

ITA
53(2)(c)(viii)

Paragraph 53(2)(c) of the Act provides for certain deductions in computing the adjusted cost base of a partnership interest. New subparagraph (viii) is added to require a member of a partnership to reduce the adjusted cost base of his partnership interest by the amount of any scientific research tax credit that flows through the partnership to him. This would occur where the partnership acquires a share, debt obligation or right to which the scientific research tax credit attaches. This amendment applies to the 1983 and subsequent taxation years.

Subclause 4(2)

ITA
53(2)(h)(iv)

Paragraph 53(2)(h) of the Act provides for certain deductions in computing the adjusted cost base of a beneficiary's capital interest in a trust or a unit of a unit trust. New subparagraph (iv) has been added to require the beneficiary to reduce the adjusted cost base of his interest in the trust by the amount of any scientific research tax credit that flows through the trust to him. This would occur where the trust acquires a share, debt obligation or right to which the scientific research tax credit attaches. This amendment applies to the 1983 and subsequent taxation years.

Subclause 4(3)

This sets out the effective dates for the amendments to subsection 53(2) of the Act relating to adjustments to cost base.

Amalgamations

Clause 5

ITA
87(2)(oo)

Subsection 87(2) of the Act provides rules which apply on the amalgamation of two or more taxable Canadian corporations. The amalgamated corporation is generally treated as a continuation of its predecessor corporations for the purposes of the Act. New paragraph 87(2)(oo) is added as a consequence of the introduction of the new Part VIII tax relating to the scientific research tax credit. This paragraph provides that any Part VIII tax paid by a predecessor corporation which has not been refunded to it will enter into the calculation of the refundable Part VIII tax on hand of the amalgamated corporation. Thus a new corporation formed on an amalgamation will be entitled to offset the Part VIII tax paid by a predecessor corporation by any scientific research tax credit earned by the new corporation and by 50% of eligible scientific research expenditures made by it. This amendment applies to the 1983 and subsequent taxation years.

Winding-up of a
Corporation
ITA
88(1)(e.2),
88(1)(e.2)(xix) and
(xx)

Subclauses 6(1) and (2)

Subsection 88 (1) of the Act sets out detailed rules that apply on the winding-up of a subsidiary into a parent corporation that owns at least 90% of its shares. Under paragraph 88(1)(e.2) many of these detailed rules are adopted by way of cross refer-

ence to the corresponding provisions in section 87 relating to amalgamations. The amendments to paragraph 88(1)(e.2) make reference to new paragraph 87(2)(oo) and are consequential on the introduction of this provision in the Act. Thus a parent corporation will be entitled to offset the Part VIII tax paid by its subsidiary before the winding-up by any scientific research tax credit earned by the parent and by 50% of eligible scientific research expenditures made by it. These amendments apply to the 1983 and subsequent taxation years.

Forward Averaging

Clause 7

ITA
120.1(2)(b)

Paragraph 120.1(2)(b) provides for a special calculation of the tax payable on a taxpayer's accumulated forward averaging amount in the year in which the taxpayer dies. In these cases the tax on the accumulated forward averaging amount is computed as the amount that his tax for the three years preceding the year of his death would have increased had 1/3 of the accumulated forward averaging amount been included in his income for each of those years. To simplify this calculation, tax payable for this purpose is computed without regard to various tax credits. The amendment to paragraph 120.1(2)(b) ensures that the scientific research tax credit provided in section 127.3 is also to be ignored in making this calculation. The amendment applies to the 1983 and subsequent taxation years.

**Overseas Employment
Tax Credit**

Clause 8

ITA
122.3(2)(b)

Paragraph 122.3(2)(b) of the Act defines "tax otherwise payable under this Part for the year" for the purposes of calculating the overseas employment tax credit. Paragraph 122.3(2)(b) of the Act is amended to include a reference to section 127.3 of the Act relating to the scientific research tax credit. Since the overseas employment tax credit is based on taxes payable before other tax credits are deducted, the amendment ensures that the scientific research tax credit is not deducted before calculation of the overseas employment tax credit. This amendment applies to the 1984 and subsequent taxation years.

Corporation Surtax

Clauses 9 and 10

ITA
123.4(a) and
123.5(a)

Section 123.4 of the Act imposes a 5% corporate surtax for the 1982 calendar year and section 123.5 imposes a 2½% corporate surtax for 1983. Paragraphs 123.4(a) and 123.5(a) are amended to provide that the amount of the surtax is calculated by reference to a corporation's federal tax otherwise payable before any deduction of scientific research tax credits to which it is entitled. The amendments to sections 123.4 and 123.5 apply to the 1983 and subsequent taxation years.

Foreign Tax Credit

Clause 11

ITA
126(7)(d)

Paragraph 126(7)(d) of the Act defines Canadian tax otherwise payable for the purposes of determining the foreign tax credit limitation. Subparagraphs (i) to (iii) are amended as a result of the new scientific research tax credit. The effect is to exclude this credit in determining the Canadian tax otherwise payable in paragraph 126(7)(d). These changes apply to the 1983 and subsequent taxation years.

Investment Tax Credit

Clause 12

Subclause 12(1)

ITA
127(10.1)(c)

Paragraph 127(10.1)(c) of the Act defines those scientific research expenditures which qualify for the investment tax credit. This amendment removes from that defi-

dition those expenditures which a corporation has renounced under the new scientific research financing mechanism. Thus, those expenditures specified by a corporation under new clause 194(2)(a)(ii)(A) in order to obtain a refund of the new Part VIII tax will not qualify for the investment tax credit. These expenditures also reduce the scientific research expenditures that are deductible as an expense under subsection 37(1) of the Act. This amendment applies to expenditures made after April 19, 1983.

Subclauses 12(2) and (3)

ITA
127(11.1)(b) and (c)

Paragraph 127(11.1)(b) of the Act sets out the existing investment tax credit rates of 10%, 20% and 25% earned on qualifying scientific research expenditures. Under new paragraph 127(11.1)(c) of the Act, these rates are being increased to 20%, 30% and 35% for expenditures made in taxation years ending after October 31, 1983. These higher tax credits compensate for the withdrawal of the special research allowance under section 37.1 of the Act, effective for taxation years ending after October 31, 1983.

However, as set out in the commentary at Clause 2, there are some transitional cases where section 37.1 will continue to apply in later years. New paragraph 127(11.1)(c) of the Act provides that the new higher rates will not apply to scientific research expenditures made by a corporation in any taxation year in which it deducts the special incremental research allowance under section 37.1 of the Act.

Subclause 12(4)

This sets out the effective date for the proposed amendment to section 127 of the Act dealing with the definition of qualified expenditure for the purposes of the investment tax credit.

Scientific Research Tax
Credit

Clause 13

Subclause 13(1)

ITA
127.3

New section 127.3 of the Act, taken together with new Part VIII, provides the new financing mechanism proposed in the consultation paper *Research and Development Tax Policies* which was released with the April 19, 1983 budget. This mechanism will enable a corporation to renounce the tax benefit of deductions and related investment tax credits for scientific research expenditures and, by so doing, allow new investors to qualify for the new scientific research tax credit (SRTC). The rates of this tax credit are described in new subsection 127.3(2).

The SRTC is deductible by investors in calculating their liability for tax under Part I of the Act. To be eligible for the credit the investments must be in the form of shares, debt obligations or certain rights acquired after September, 1983. These investments are further described below. Where the investor is a corporation the credit is deductible either from its tax under Part I or against any liability that may arise under new Part VIII of the Act.

ITA
127.3(1)

New subsection 127.3(1) of the Act permits a taxpayer to deduct his SRTC from his Part I tax otherwise payable for the year. The amount of the credit is determined under subsection 127.3(2).

ITA
127.3(2)

New subsection 127.3(2) defines a taxpayer's scientific research tax credit for a taxation year. Where the investor is an individual, the credit is 34% of the amount designated in respect of a qualifying investment made by him. In the case of a corpo-

rate investor, the credit is 50% of the amount designated in respect of a qualifying investment made by it. The computation of provincial individual income taxes under federal-provincial tax collection agreements means that the 34% SRTC rate for individuals will provide a total effective rate of credit for individuals of approximately 50%, depending on the province.

Qualifying investments are shares or debt obligations issued, or rights granted under a scientific research financing contract, by a corporation after September 1983 where the investor is the first person (other than a broker or dealer in securities) to have acquired the share, debt obligation or right. For the purpose of this section, a debt obligation is a bond, debenture, bill, note, mortgage, hypothec or similar indebtedness. A scientific research financing contract, as defined in new subsection 194(6) of the Act, is a royalty agreement or other contract under which the investor becomes entitled to receive income other than interest or dividends.

ITA
127.3(3)

New subsection 127.3(3) sets out the rules for the allocation of the SRTC by a trust to its beneficiaries. A trust cannot itself claim the credit but under this new subsection may allocate SRTC to its beneficiaries. Where the taxation years of the trust and its beneficiaries do not coincide, the allocation is made as at the end of the trust's taxation year and the beneficiary obtains the credit for his taxation year then in progress.

ITA
127.3(4)

New subsection 127.3(4) sets out the rules for the allocation of the SRTC by a partnership to the members of the partnership. A partnership cannot itself claim the credit. However, under this subsection the members of the partnership are deemed to have earned the SRTC in their taxation year that includes the end of the fiscal period of the partnership in which it acquired the qualifying investment.

ITA
127.3(5)

New subsection 127.3(5) deals with the SRTC of a co-operative corporation. Often these corporations have little or no taxable income because they have distributed or allocated their income by way of patronage dividends to members. To ensure that such a corporation benefits from SRTC, this subsection permits it to apply the credit, as at the date of the payment of the patronage dividends, against its withholding tax liability in respect of such dividends. Any balance of the credit that is not applied against the withholding tax liability may be claimed by the co-operative corporation in the normal fashion as a tax credit against its Part I income tax liability.

ITA
127.3(6)

New subsection 127.3(6) requires the cost to an investor of a qualifying investment that earns the SRTC to be reduced by 50% of the designated amount. This cost reduction applies at the time of acquisition whether or not the SRTC is claimed. This ensures that if the qualifying investment is sold before the credit is claimed, the reduced cost will be used in determining any gain or loss.

ITA
127.3(7)

New subsection 127.3(7) provides that, although a partnership is not a person, it shall be treated as a person in determining whether it is the first person to acquire a qualifying investment and in determining the cost thereof.

ITA
127.3(8)

New subsection 127.3(8) provides that SRTC cannot be used to reduce the additional tax payable as a result of an election by an individual to forward average. The credit may, however, be claimed against tax payable arising as a result of an election to include in income amounts previously forward averaged. The SRTC is to be applied against such tax before the special deduction allowed under section 120.1 of the Act in respect of the tax paid at the time of forward averaging.

Subclause 13(2)

This sets out the effective date for new section 127.3 dealing with the scientific research tax credit.

Refundable Tax on Corporation in Respect of Scientific Research Tax Credit

Part VIII

Clause 14

New Part VIII of the Act is an integral part of the new financing mechanism described in the commentary under section 127.3 of the Act. Part VIII, consisting of sections 194 and 195, provides for a refundable tax payable annually by a corporation in an amount equal to the scientific research tax credit that it makes available to investors through the issue of its shares, debt obligations or rights after September, 1983. However, the Part VIII tax liability may be satisfied by renouncing the benefit of the deduction and investment tax credit in respect of scientific research (R&D) expenditures made by it in the year or the immediately preceding year. For each \$2 of expenditures renounced, \$1 of the Part VIII tax liability is eliminated. In addition, the corporation may offset its Part VIII tax liability by any scientific research tax credit it earns through investments it has made in other corporations. The corporation is required to pay the remaining Part VIII tax liability but the amount so paid is refundable in subsequent taxation years when R&D expenditures are made or scientific research tax credits are earned. This mechanism enables a corporation to issue shares or debt obligations, or grant rights, that carry rights to the SRTC even though it has not at the time of issue made the necessary qualifying expenditures.

Subclause 14(1)

ITA
194(1)

New subsection 194(1) of the Act imposes the Part VIII tax liability on a corporation that has issued shares or debt obligations, or granted rights, entitling the purchaser to SRTC. The corporation's liability for the Part VIII tax in a year is equal to 50% of all amounts designated by it under new subsection 194(4) in respect of such shares, debt obligations or rights issued or granted by it in the year.

ITA
194(2)

New subsection 194(2) of the Act defines the "Part VIII refund". This refund is the lesser of two amounts:

The first amount is the sum of:

- the corporation's scientific research tax credit for the year that was not deducted from its Part I tax, and
- such amount as a corporation chooses to claim, not exceeding 50% of its R&D expenditures in the year or the previous year, provided the expenditures did not give rise to a Part VIII refund for the preceding year, a deduction under section 37 or 37.1 of the Act or an investment tax credit claim.

The second amount is the corporation's "refundable Part VIII tax on hand" at the end of the year as defined in new subsection 194(3).

ITA
194(3)

New subsection 194(3) of the Act defines a corporation's "refundable Part VIII tax on hand" at the end of a taxation year. This amount represents the maximum refund of the Part VIII tax to which a corporation is entitled in a year. It consists of the total of the Part VIII taxes payable by the corporation in the year and in all preceding years minus the total of its Part VIII refunds for all preceding years.

Example

Corporation issues shares and designates \$1,000 in respect of the shares.

Part VIII tax liability under subsection 194(1): 50% of \$1,000 = \$500

Corporation spends \$800 on scientific research expenditures which it renounces under subsection 194(2)

Part VIII refund under 194(2): 50% of \$800 = \$400

If corporation has paid the \$500 Part VIII tax as required by subsection 195(2), it will get a refund of \$400.

Under subsection 194(3) the corporation's refundable Part VIII tax on hand at the end of the following year is \$500 minus \$400 = \$100

ITA
194(4)

A corporation that wishes to designate scientific research tax credits on the issue of a share or debt obligation, or on the grant of a right, is required under new subsection 194(4) of the Act to designate an amount in respect thereof. The amount so designated cannot exceed the amount of the consideration for which the corporation issued the share or debt obligation or granted the right. Where the purchaser of a share is entitled to receive an amount from a provincial government in respect of his purchase of the share, the consideration for which it was issued shall, for the purpose of this section, be reduced by that amount. The corporation must make the designation by filing certain prescribed information before the end of the month following the month in which the share or debt obligation is issued, or the right is granted, or within 90 days following Royal Assent to the enacting bill. In respect of a share it issues, a corporation cannot make designations under both this subsection and subsection 192(4) of the Act dealing with the share-purchase tax credit.

ITA
194(5)

New subsection 194(5) of the Act provides that a corporation's Part VIII refund for a taxation year will be considered to have been paid as an amount on account of its Part VIII tax liability for the year on the last day of the second month following the end of the year. This treatment effectively ensures the recovery of Part VIII tax actually paid by the corporation.

ITA
194(6)

New subsection 194(6) defines the term "scientific research financing contract" for the purposes of the SRTC and the Part VIII refundable tax. A scientific research financing contract is defined as a contract between an investor and a corporation under which the investor is granted the right under the contract to receive a royalty or similar payment.

ITA
194(7)

New subsection 194(7) of the Act permits a corporation to designate an amount in respect of a share, debt obligation or right for the purposes of the SRTC even though the designation has not been made within the time period specified in subsection 194(4). A late designation may be made if the corporation has made the prescribed information return in respect of the share, debt obligation or right as and when

required and has paid to the Receiver General a reasonable estimate of the penalty for filing a late designation. A late designation cannot be more than three years late and in any event must be made within 90 days after notification by the Minister of National Revenue that the required designation was not made.

ITA
194(8)

New subsection 194(8) of the Act determines the amount of the penalty which must be paid under subsection 194(7) in respect of a late designation. The penalty is normally equal to 1% of the amount designated in respect of the share, debt obligation or right for each month or part thereof in the period beginning on the last day of the month following the month in which the share or debt obligation was issued or the right was granted, and ending on the day the late designation is made. Under subsection 194(4) this period will not commence until 90 days after the implementing legislation is enacted. The maximum penalty for a month is \$500.

ITA
194(9)

New subsection 194(9) prevents a corporation from designating more than one amount in respect of the same share, debt obligation or right.

ITA
195(1)

New subsection 195(1) of the Act requires a corporation liable for Part VIII tax to file a return under that Part by the date on which it is required to file its annual corporate tax return under Part I of the Act and to pay the balance of any tax owing on or before the last day of the second month following the end of the taxation year of the corporation. For corporations, a return is required to be filed within six months from the end of its taxation year.

ITA
195(2)

New subsection 195(2) requires a corporation which has designated an amount under new subsection 194(4) in respect of shares or debt obligations issued by it or rights granted by it to pay 50% of that amount – i.e., its liability for the Part VIII tax – by the end of the month following the month in which the shares or debt obligations were issued or the rights were granted. The tax equals the amount of the SRTC that an investor will earn in respect of those shares, debt obligations or rights.

ITA
195(3) and (4)

New subsection 195(3) provides that corporations which do not pay their Part VIII tax by the date required under subsection 195(2) must pay interest from that date. However, new subsection 195(4) provides that, in determining the interest payable, the amount of Part VIII tax payable is reduced by any Part VIII refund to which the corporation is entitled for the year. In determining the month-end tax liability on which interest is calculated, the amount of the corporation's Part VIII tax for the year minus its Part VIII refund for the year is multiplied by a fraction that has as its numerator the total of the amounts designated by it in respect of all shares or debt obligations issued, or rights granted, in the preceding month and as its denominator the total of the amounts designated by it in respect of all shares or debt obligations issued, or rights granted, in the year.

Example

Corporation designates \$200 in February
in respect of shares issued in January
and does not pay tax.

Total designated by corporation in respect of all shares issued in the year	\$1,000
Part VIII tax liability for the year: 50% of \$1,000 =	\$500
Part VIII refund (assumed)	\$350
Net Part VIII tax payable	\$150

Interest will be computed from end of
February on unpaid tax of \$30, arrived
at as follows:

$$\begin{array}{r} \$150 \times \$200 = \\ \quad \quad \quad \$1,000 \end{array} \qquad \qquad \qquad \$30$$

ITA
195(5)

New subsection 195(5) is an anti-avoidance provision. It denies the SRTC to a purchaser of a share, debt obligation or right in circumstances where he acquired the share, debt obligation or right when he knew or ought to have known that the corporation issuing the share or debt obligation or granting the right would evade or attempt to evade payment of its Part VIII tax liability.

ITA
195(6)

New subsection 195(6) is an anti-avoidance provision designed to preclude a corporation from avoiding interest on Part VIII tax through the acquisition of shares, debt obligations or rights issued or granted by a corporation that it controls. Where it is reasonable to consider that one of the main purposes for acquiring a share, debt obligation or right was to avoid the payment of interest on Part VIII tax for a period, the share, debt obligation or right shall be deemed not to have been acquired or issued or granted until after the end of the period for the purposes of calculating the corporation's SRTC and its Part VIII refund.

For example, a company with a December 31 year-end owes Part VIII tax and late in the year it acquires a share of a subsidiary with a November 30 year-end for the purpose of generating sufficient scientific research tax credits to offset its Part VIII tax liability. In the absence of subsection 195(6), the liability for the Part VIII tax would be transferred to the subsidiary and postponed for 11 months. Indeed, the subsidiary could in turn acquire shares of a sub-subsiary and by this means the corporate group could effectively postpone the tax indefinitely.

ITA
195(7)

New subsection 195(7) sets out the rules relating to the payment of tax and various other procedural and administrative matters with respect to the Part VIII tax.

Subclause 14(2)

This sets out the effective date for the new Part VIII dealing with the refundable tax on corporations in respect of the scientific research tax credit.

Clause 15

Liabilities of Directors
ITA
227.1

Section 227.1 of the Act relates to the liability of the directors of a corporation for the withholding tax obligations imposed on the corporation under sections 135, 153 and 215 of the Act. The liability is imposed on persons who were directors at the time the corporation failed to deduct or withhold or remit the required tax. The liability also extends to any related interest or penalty. This amendment to subsection 227.1 (1) extends the liability where the corporation has failed to pay its Part VIII tax liability, related to the scientific research tax credit, for a taxation year. This amendment applies to the 1983 and subsequent taxation years.

Clause 16

Mailing Date
ITA
244(14)

Subsection 244(14) of the Act provides that the day of mailing of a notice of assessment or other notification shall, in the absence of any evidence to the contrary, be the date appearing thereon. This subsection is amended to add a reference to new

subsection 194(7) which provides that a corporation has 90 days to respond to a notice by the Minister of National Revenue that it has not filed a designation as required by new subsection 194(4). This amendment applies to the 1983 and subsequent taxation years.

Draft Amendments to the Income Tax Act

1. (1) Subsection 37(1) of the *Income Tax Act* is amended by striking out the word "and" at the end of paragraph (e) thereof, by adding the word "and" at the end of paragraph (f) thereof and by adding thereto the following paragraph: 5

"(g) the aggregate of all amounts each of which is an amount equal to twice the amount claimed under subparagraph 194(2)(a)(ii) by the taxpayer for the 10 year or any preceding taxation year."

(2) Subsection (1) is applicable to the 1983 and subsequent taxation years.

Application of
subsections
37.1(1) and (2)

2. Notwithstanding subsection 6(2) of An Act to amend the statute law relating to 15 income tax and to authorize payments related to provincial sales tax reductions, chapter 32 of the Statutes of Canada, 1977-78, subsections 37.1(1) and (2) of the *Income Tax Act* do not apply to a taxation year of a 20 corporation that ends after October, 1983 unless

(a) in the case of a particular taxation year that includes November 1, 1983, the corporation elects in its return of income 25 under Part I of the *Income Tax Act* for the year to have those subsections apply, in which case each corporation that was associated with the corporation in the year shall be deemed to have so elected in 30 respect of its taxation year that ended in the calendar year in which the particular taxation year ended, or

(b) the qualified expenditure (within the meaning of paragraph 37.1(5)(c) of the 35 *Income Tax Act*) made by the corporation in the year includes

(i) an expenditure that the corporation was obligated to make pursuant to an agreement in writing entered into by the corporation before April 20, 1983, or

(ii) an expenditure that the corporation 5 was obligated to make in respect of a project pursuant to an agreement in writing entered into by the corporation before November 2, 1983, where the project commenced before 1984 and 10 proceeded without undue delay, and arrangements, evidenced by writing, respecting the project were substantially advanced before April 20, 1983,

and the corporation elects in its return of 15 income under Part I of the *Income Tax Act* for the taxation year to have those subsections apply, in which case the amount that may be deducted under section 37.1 of the *Income Tax Act* in com- 20 puting the income of the corporation for the year shall be that proportion of the amount thereof that could, but for this section, have been so deducted by the corporation (on the assumption that it is not 25 associated in the year with any other corporation) that

(iii) an amount equal to the aggregate of expenditures made by the corporation in the year each of which is an expendi- 30 ture described in paragraph 37.1(5)(c) of the *Income Tax Act* and is made pursuant to an agreement referred to in subparagraph (i) or (ii) of this para- 35 graph

is of

(iv) the qualified expenditure (within the meaning of paragraph 37.1(5)(c) of

the *Income Tax Act*) made by the corporation in the year.

3. (1) Section 39 of the said Act is amended by adding thereto the following subsection:

“(8) The amount, if any, by which the scientific research tax credit of a taxpayer for a taxation year exceeds the aggregate of

(a) the amount deducted under subsection 127.3(1) from his tax otherwise payable under this Part for the year, and

(b) his refundable Part VIII tax on hand at the end of the year

shall be deemed to be a capital loss of the taxpayer from a disposition of property in the year.”

(2) Subsection (1) is applicable to the 1983 and subsequent taxation years.

4. (1) Paragraph 53(2)(c) of the said Act is amended by striking out the word “and” at the end of subparagraph (vi) thereof, by adding the word “and” at the end of subparagraph (vii) thereof and by adding there- to the following subparagraph:

“(viii) an amount equal to 50% of the amount deemed to be designated pursuant to subsection 127.3(4) before that time in respect of each share, debt obligation or right acquired by the partnership and deemed to have been acquired by the taxpayer under that subsection.”

(2) Paragraph 53(2)(h) of the said Act is amended by striking out the word “and” at the end of subparagraph (ii) thereof, by adding the word “and” at the end of subparagraph (iii) thereof and by adding thereto the following subparagraph:

“(iv) an amount equal to 50% of the amount deemed to be designated pursuant to subsection 127.3(3) before that time in respect of each share, debt obligation or right acquired by the trust and deemed to have been acquired by the taxpayer under that subsection.”

(3) Subsections (1) and (2) are applicable to the 1983 and subsequent taxation years.

5. (1) Subsection 87(2) of the said Act is amended by striking out the word “and” at the end of paragraph (mm) thereof, by adding the word “and” at the end of paragraph (nn) thereof and by adding thereto the following paragraph:

“(oo) for the purpose of computing the refundable Part VIII tax on hand of the new corporation at the end of any taxation year, there shall be added to the aggregate determined under paragraph 194(3)(a) the aggregate of all amounts each of which is the amount, if any, by which

(i) a predecessor corporation’s refundable Part VIII tax on hand at the end of its last taxation year

exceeds

(ii) the predecessor corporation’s Part VIII refund for its last taxation year.”

(2) Subsection (1) is applicable to the 1983 and subsequent taxation years.

6. (1) All that portion of paragraph 88(1)(e.2) of the said Act preceding subparagraph (i) thereof is repealed and the following substituted therefor:

“(e.2) the provisions of paragraphs 87(2)(c), (d.1), (g) to (l), (l.3) to (s), (t), (u), (x), (y.1) to (z.1), (cc), (ee) and (ll) to (oo), subsection 87(6) and, subject to section 78, subsection 87(7) apply to the winding-up as if the references therein to”

(2) Paragraph 88(1)(e.2) of the said Act is further amended by striking out the word “and” at the end of subparagraph (xvii) thereof and by adding thereto the following subparagraphs:

“(xix) “predecessor corporation’s refundable Part VIII tax on hand” were read as “subsidiary’s refundable Part VIII tax on hand”, and

(xx) “predecessor corporation’s Part VIII refund” were read as “subsidiary’s Part VIII refund”;

Unused scientific research tax credit

(3) Subsections (1) and (2) are applicable to the 1983 and subsequent taxation years.

7. (1) Paragraph 120.1(2)(b) of the said Act is repealed and the following substituted therefor:

“(b) where he died in the year and was resident in Canada at the time of his death, the amount, if any, by which

(i) the aggregate of the taxes that would, if this Part were read without reference to sections 118 to 127.3, have been payable by him under this Part for the three immediately preceding taxation years if he had specified for each of those years in elections under subsection 110.4(2) 1/3 of his accumulated averaging amount at the end of the year in which he died

exceeds

(ii) the aggregate of his taxes that would, if this Part were read without reference to sections 118 to 127.3, have been payable under this Part for the three immediately preceding taxation years.”

(2) Subsection (1) is applicable to the 1983 and subsequent taxation years.

8. (1) Paragraph 122.3(2)(b) of the said Act is repealed and the following substituted therefor:

“(b) “tax otherwise payable under this Part for the year” means the amount, if any, by which the tax payable under this Part for the taxation year (before making any addition under section 120.1 or any deduction under section 120.1, 121, 126, 127, 127.2 or 127.3) exceeds the amount, if any, deemed by subsection 120(2) to have been paid on account of tax under this Part for the year.”

(2) Subsection (1) is applicable to the 1984 and subsequent taxation years.

9. (1) Paragraph 123.4(a) of the said Act is repealed and the following substituted therefor:

“(a) the tax otherwise payable under this Part by the corporation for the year determined without reference to this section, sections 123.3, 123.5 and 126 (except for the purposes of section 125.1 and subsections 125(1) and (1.1)), subsections 127(3), (5), (13), 127.2(1) and 127.3(1) and as if subsection 124(1) were read without reference to the words “in a province” therein”

(2) Subsection (1) is applicable to the 1983 and subsequent taxation years.

10. (1) Paragraph 123.5(a) of the said Act is repealed and the following substituted therefor:

“(a) the tax otherwise payable under this Part by the corporation for the year determined without reference to this section, sections 123.4 and 126 (except for the purposes of section 125.1 and subsections 125(1) and (1.1)), subsections 127(3), (5), (13), 127.2(1) and 127.3(1) and as if subsection 124(1) were read without reference to the words “in a province” therein”

(2) Subsection (1) is applicable to the 1983 and subsequent taxation years.

11. (1) Paragraph 126(7)(d) of the said Act is repealed and the following substituted therefor:

“(d) “tax for the year otherwise payable under this Part” means

(i) in paragraphs (1)(b) and (3)(b), the amount, if any, by which the tax for the taxation year otherwise payable under this Part before making any addition under section 120.1 and any deduction under any of sections 120.1, 121, 122.3, 125 to 127, 127.2 and 127.3 exceeds the amount, if any, deemed by subsection 120(2) to have been paid on account of tax under this Part for the year,

(ii) in subparagraph (2)(c)(i) and paragraph (2.2)(b), the tax for the taxation year otherwise payable under this Part before making any addition under section 120.1 and any deduction under any of sections 120.1, 121,

“Tax otherwise payable under this Part for the year”

“tax for the year otherwise payable under this Part”

122.3, 124 to 127, 127.2 and 127.3, and

(iii) in subsection (2.1), the tax for the taxation year otherwise payable under this Part before making any addition under subsection 120(1) or section 120.1 and any deduction under any of sections 120.1, 121, 122.3, 124 to 127, 127.2 and 127.3.”

(2) Subsection (1) is applicable to the 1983 and subsequent taxation years.

12. (1) Paragraph 127(10.1)(c) of the said Act is repealed and the following substituted therefor:

“(c) “qualified expenditure” means an expenditure in respect of scientific research made by a taxpayer after March 31, 1977 that qualifies as an expenditure described in paragraph 37(1)(a) or subparagraph 37(1)(b)(i), but does not include

- (i) a prescribed expenditure, and
- (ii) in the case of a taxpayer that is a corporation, an expenditure specified by the taxpayer for the purposes of clause 194(2)(a)(ii)(A);”

(2) All that portion of paragraph 127(11.1)(b) of the said Act preceding subparagraph (i) thereof is repealed and the following substituted therefor:

“(b) a qualified expenditure incurred by a taxpayer after November 16, 1978 and before his taxation year that includes November 1, 1983, or a qualified expenditure incurred by him in that taxation year or a subsequent taxation year if he deducted an amount under section 37.1 in computing his income for the year,”

(3) Subsection 127(11.1) of the said Act is further amended by striking out the word “and” at the end of paragraph (a) thereof, by adding the word “and” at the end of paragraph (b) thereof and by adding thereto the following paragraph:

“(c) a qualified expenditure incurred by a taxpayer in his taxation year that includes November 1, 1983 or a subsequent taxation year, other than a quali-

fied expenditure referred to in paragraph (b),

(i) where the expenditure was incurred by a Canadian-controlled private corporation in a taxation year of the corporation in which it is or would, if it had sufficient taxable income for the year, be entitled to a deduction under section 125 in computing its tax payable under this Part for the year, the references in paragraphs (a) and (b) thereof to “5%” shall be read as references to “35%” and the references in paragraphs (a.1), (a.2), (b.1) and (b.2) thereof to “2 1/2%” or “5%”, as the case may be, shall be read as references to “0%”, and

(ii) in any other case, the references in paragraphs (a) and (b) thereof to “5%” shall be read as references to “20%”, the references in paragraphs (a.1) and (b.1) thereof to “5%” shall be read as references to “10%” and the references in paragraphs (a.2) and (b.2) thereof to “2 1/2%” shall be read as references to “0%”.”

(4) Subsection (1) is applicable with respect to expenditures made after April 19, 1983.

13. (1) The said Act is further amended by adding thereto, immediately after section 127.2 thereof, the following section:

“**127.3** (1) There may be deducted from the tax otherwise payable under this Part by a taxpayer for a taxation year an amount not exceeding his scientific research tax credit for the year.”

Scientific research tax credit

(2) For the purposes of this Act, “scientific research tax credit” of a taxpayer for a taxation year means the aggregate of all amounts each of which is an amount equal to

Calculation of scientific research tax credit

- (a) where the taxpayer is a corporation, 50%, or
- (b) where the taxpayer is an individual other than a trust, 34%

of an amount designated by a corporation under subsection 194(4) in respect of

(c) a share acquired by the taxpayer in the year where the taxpayer is the first person, other than a broker or dealer in securities, to be a registered holder thereof,

(d) a bond, debenture, bill, note, mortgage, hypothec or similar obligation (in this section and in Part VIII referred to as a "debt obligation") acquired by the taxpayer in the year where the taxpayer is the first person, other than a broker or dealer in securities, to be a registered holder thereof, or

(e) a right acquired by the taxpayer in the year where the taxpayer is the first person, other than a broker or dealer in securities, to have acquired that right.

Trust

(3) For the purposes of this section and section 53, where a taxpayer, other than a broker or dealer in securities, is a beneficiary under a trust and an amount is designated by a corporation under subsection 194(4) in respect of a share, debt obligation or right acquired by the trust in a taxation year of the trust where the trust is the first person, other than a broker or dealer in securities, to be a registered holder of the share or debt obligation or to have acquired the right, as the case may be,

(a) the trust may, in its return of income for that year, specify such portion of that amount as may, having regard to all the circumstances (including the terms and conditions of the trust arrangement), reasonably be considered to be attributable to the taxpayer and as was not specified by the trust in respect of any other beneficiary under that trust; and

(b) the portion specified pursuant to paragraph (a) shall be deemed to be an amount designated on the last day of that year by the corporation under subsection 194(4) in respect of a share, debt obligation or right, as the case may be, acquired by the taxpayer on that day where the taxpayer is the first person, other than a broker or dealer in securities, to be a registered holder of the

share or debt obligation or to have acquired the right, as the case may be.

(4) For the purposes of this section and section 53, where a taxpayer, other than a broker or dealer in securities, is a member of a partnership and an amount is designated by a corporation under subsection 194(4) in respect of a share, debt obligation or right acquired by the partnership in a taxation year of the partnership where the partnership is the first person, other than a broker or dealer in securities, to be a registered holder of the share or debt obligation or to have acquired the right, as the case may be, such portion of that amount as may reasonably be considered to be the taxpayer's share thereof shall be deemed to be an amount designated on the last day of that year by the corporation under subsection 194(4) in respect of a share, debt obligation or right, as the case may be, acquired by the taxpayer on that day where the taxpayer is the first person, other than a broker or dealer in securities, to be a registered holder of the share or debt obligation or to have acquired the right, as the case may be.

Partnership

(5) Where, at any particular time in a taxation year, a taxpayer that is a cooperative corporation within the meaning assigned by subsection 136(2) has, as required by subsection 135(3), deducted or withheld an amount from a payment made by it to any person pursuant to an allocation in proportion to patronage, the taxpayer may deduct from the amount otherwise required by subsection 135(3) to be remitted to the Receiver General, an amount not exceeding the amount, if any, by which

Cooperative corporation

(a) the amount that would, but for this subsection, be its scientific research tax credit for the taxation year in which it made the payment if that year had ended immediately before the particular time

exceeds

(b) the aggregate of all amounts each of which is the amount deducted by virtue of this subsection from any amount

otherwise required by subsection 135(3) to be remitted in respect of payments made by the taxpayer before the particular time and in the taxation year, and the amount, if any, so deducted from the amount otherwise required by subsection 135(3) to be remitted shall be

(c) deducted in computing the scientific research tax credit of the taxpayer for the taxation year; and

(d) deemed to have been remitted by the taxpayer to the Receiver General on account of tax under this Part of the person to whom that payment was made.

(6) For the purposes of this Act, where a taxpayer has acquired a share, debt obligation or right and is the first registered holder of the share or debt obligation or the first person to have acquired the right, as the case may be, other than a broker or dealer in securities, and in respect of which an amount is, at any time, designated by a corporation under subsection 194(4), in determining the cost to the taxpayer of the share, debt obligation or right, there shall be deducted 50% of the amount so designated in respect of that share, debt obligation or right.

(7) For the purposes of this section and Part VIII, a partnership shall be considered to be a person and its taxation year shall be its fiscal period.

(8) In this section, "tax otherwise payable" by a taxpayer under this Part means the amount that would, but for section 120.1, be the tax payable by the taxpayer under this Part."

(2) Subsection (1) is applicable in respect of shares, debt obligations and rights acquired after September, 1983.

14. (1) The said Act is further amended by adding thereto, immediately after section 193 thereof, the following Part:

"PART VIII
REFUNDABLE TAX ON
CORPORATION IN RESPECT OF
SCIENTIFIC RESEARCH TAX CREDIT

194. (1) Every corporation shall pay a tax under this Part for a taxation year equal to 50% of the aggregate of all amounts each of which is an amount designated under subsection (4) in respect of a share or debt obligation issued by it in the year or a right granted by it in the year.

(2) In this Act, the "Part VIII refund" of a corporation for a taxation year means an amount equal to the lesser of

- (a) the aggregate of
 - (i) the amount, if any, by which the scientific research tax credit of the corporation for the year exceeds the amount, if any, deducted by it under subsection 127.3(1) from its tax otherwise payable under Part I for the year, and
 - (ii) such amount as the corporation may claim, not exceeding 50% of the amount, if any, by which

(A) the aggregate of all expenditures made by it after April 19, 1983 and in the year or the immediately preceding taxation year each of which is an expenditure, other than an expenditure prescribed for the purposes of paragraph 127(10.1)(c), claimed under paragraph 37(1)(a) or (b) to the extent that such expenditure is specified by the corporation in its return of income under Part I for the year

exceeds the aggregate of (B) the aggregate of all expenditures each of which is an expenditure made by it in the immediately preceding taxation year, to the extent that such expenditure was included in determining the aggregate under clause (A) and resulted in

(I) a refund to it under this Part for the immediately preceding taxation year,

Corporation to pay tax

"Part VIII refund" defined

Deduction from cost

Partnership

"Tax otherwise payable" defined

(II) a deduction by it under subsection 37(1) for the immediately preceding taxation year, or (III) a deduction by it under subsection 127(5) for any taxation year, and

(C) twice the portion of the aggregate of amounts each of which is an amount deducted by it in computing its income for the year or the immediately preceding taxation year under section 37.1 that can reasonably be considered to relate to expenditures that were included in determining the aggregate under clause (A), and

(b) the refundable Part VIII tax on hand of the corporation at the end of the year.

(3) In this Act, "refundable Part VIII tax on hand" of a corporation at the end of a taxation year means the amount, if any, by which

(a) the aggregate of the taxes payable by it under this Part for the year and all preceding taxation years exceeds

(b) the aggregate of its Part VIII refunds for all preceding taxation years.

(4) Every taxable Canadian corporation may, by filing a prescribed form with the Minister at any time on or before the last day of the month immediately following a month in which it issued a share (other than a share in respect of which the corporation has, on or before that day, designated an amount under subsection 192(4)) or debt obligation or granted a right under a scientific research financing contract, designate, for the purposes of this Part and Part I, an amount in respect of that share, debt obligation or right not exceeding the amount by which

(a) the amount of the consideration for which it was issued or granted, as the case may be, exceeds

(b) in the case of a share, the amount of any prescribed assistance provided in respect of that share.

(5) For the purposes of this Act, the Part VIII refund of a corporation for a taxation year shall be deemed to be an amount paid on account of its tax under this Part for the year on the last day of the second month following the end of the year.

(6) For the purposes of this Act, "scientific research financing contract" means a contract in writing pursuant to which an amount is paid by a person to a corporation as consideration for the granting by the corporation to that person of any right, either absolute or contingent, to receive income, other than interest or dividends.

(7) Where a taxable Canadian corporation that issued a share or debt obligation or granted a right under a scientific research financing contract does not designate an amount under subsection (4) in respect of the share, debt obligation or right on or before the day on or before which such designation was required by that subsection, the corporation shall be deemed to have made the designation on that day if, within three years after that day,

(a) the corporation has made the prescribed information return in respect of the share, debt obligation or right as and when required; and

(b) the corporation has (i) designated an amount in respect of the share, debt obligation or right by filing a prescribed form with the Minister, and (ii) paid to the Receiver General an amount that is a reasonable estimate of the amount of the penalty payable by the corporation for the late designation in respect of the share, debt obligation or right;

however, where the Minister has mailed a notice to the corporation that a designation has not been made in respect of the share, debt obligation or right under subsection (4), the designation and payment

Presumption

"Scientific research financing contract" defined

Late designation

"Refundable Part VIII tax on hand" defined

Designation

described in paragraph (b) must be made by the corporation on or before the day that is 90 days after the day of such mailing.

Penalty for late designation

(8) Where, pursuant to subsection (7), a corporation made a late designation in respect of a share or debt obligation issued, or a right granted, in a month, the corporation shall pay, for each month or part of a month that elapsed during the period commencing on the last day on or before which an amount could have been designated by the corporation under subsection (4) in respect of the share, debt obligation or right and ending on the day that the late designation is made, a penalty for the late designation in respect of the share, debt obligation or right in an amount equal to 1% of the amount designated in respect of the share, debt obligation or right, except that the maximum penalty payable under this subsection by the corporation for a month shall not exceed \$500.

Only one designation permitted

(9) Where at any time a corporation has designated an amount under subsection (4) in respect of a share, debt obligation or right, no amount may be designated by the corporation at any subsequent time in respect of that share, debt obligation or right.

Corporation to file and pay

195. (1) Every corporation that is liable to pay tax under this Part for a taxation year shall

(a) on or before the day on or before which it is required to file its return of income under Part I for the year, file with the Minister a return for the year under this Part in prescribed form; and

(b) on or before the last day of the second month following the end of the year, pay the tax to the Receiver General.

Corporation to make payment on account of tax

(2) Where, in a particular month in a taxation year, a corporation issues a share or debt obligation, or grants a right, in respect of which it designates an amount under section 194, the corporation shall, on or before the last day of the month

following the particular month, pay to the Receiver General on account of its tax payable under this Part for the year an amount equal to 50% of the aggregate of all amounts so designated.

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(3) Where a corporation is liable to pay tax under this Part and has failed to pay all or any part or instalment thereof on or before the day on or before which it was required to pay the tax, it shall, on payment of the amount in default, pay interest thereon at the prescribed rate for the period commencing on the day following the day on or before which it was required to make the payment and ending on the day of payment.

Interest on amount in default

(4) For the purposes of computing interest payable by a corporation under subsection (3) for any month or months in the fourteen month period ending two months after the end of a taxation year in which the corporation has designated an amount under section 194 in respect of a share or debt obligation issued, or right granted, by it in a particular month in the year, the corporation shall be deemed to have been liable to pay, on or before the last day of the month immediately following the particular month, a part or instalment of tax for the year equal to that proportion of the amount, if any, by which its tax payable under this Part for the year exceeds its Part VIII refund for the year that

Idem

(a) the aggregate of all amounts so designated by it under section 194 in respect of shares or debt obligations issued, or rights granted, by it in the particular month

is of

(b) the aggregate of all amounts so designated by it under section 194 in respect of shares or debt obligations issued, or rights granted, by it in the year.

(5) Where a corporation that is liable to pay tax under this Part in respect of a share or debt obligation issued, or a right granted, by it wilfully, in any manner whatever, evades or attempts to evade pay-

Evasion of tax

ment of the tax and a purchaser of the share, debt obligation or right or, where the purchaser is a partnership, a member thereof, knew or ought to have known, at the time the share, debt obligation or right was acquired, that the corporation would wilfully evade or attempt to evade the tax, for the purposes of section 127.3 the share, debt obligation or right shall be deemed not to have been acquired.

this section, may be made on or before the day that is 90 days after this Act is assented to.

5 **15.** (1) Subsection 227.1(1) of the said Act is repealed and the following substituted 5 therefor:

“**227.1** (1) Where a corporation has failed to deduct or withhold an amount as required by subsection 135(3) or section 153 or 215, has failed to remit such an amount or has failed to pay an amount of tax for a taxation year as required under Part VII or Part VIII, the directors of the corporation at the time the corporation was required to deduct, withhold, remit or pay the amount are jointly and severally liable, together with the corporation, to pay that amount and any interest or penalties related thereto.”

Liability of directors

(2) Subsection (1) is applicable to the 1983 and subsequent taxation years.

16. (1) Subsection 244(14) of the said Act is repealed and the following substituted therefor:

“(14) For the purposes of this Act, the day of mailing of any notice of assessment or notification described in subsection 152(4) or 194(7) shall, in the absence of any evidence to the contrary, be deemed to be the day appearing from such notice or notification to be the date thereof unless called in question by the Minister or by some person acting for him or Her Majesty.”

(2) Subsection (1) is applicable to the 1983 and subsequent taxation years.

Undue deferral

(6) Where, in a transaction or as part of a series of transactions, a taxpayer acquires a share or debt obligation of a corporation or a right granted by a corporation and the corporation is controlled (within the meaning assigned by subsection 186(2)) by him and it may reasonably be considered that one of the main purposes of the acquisition was to reduce for a period interest on his liability for tax under this Part, the share, debt obligation or right shall, for the purposes of section 127.3 and this Part (other than this subsection), be deemed not to have been acquired by the taxpayer and not to have been issued or granted, as the case may be, by the corporation until the end of that period.

(7) Sections 151, 152, 158, 159 and 162 to 167 and Division J of Part I are applicable to this Part, with such modifications as the circumstances require.”

(2) Subsection (1) is applicable in respect of shares and debt obligations issued, and rights granted, after September, 1983, except that a designation under subsection 194(4) of the said Act, as enacted by subsection (1) of

Provisions applicable to this Part