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DEPARTMENT OF INDUSTRY, OTTAWA

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# DOING BUSINESS IN CANADA

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FEDERAL  
INCENTIVES  
TO INDUSTRY

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# FEDERAL INCENTIVES TO INDUSTRY

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This booklet deals with major federal government incentives available to Canadian manufacturers. It is intended as a guide in this field and, as such, refers only to the basic provisions. It is not intended as a manual for factors proposing to take advantage of any of these incentive measures. It is intended to provide the appropriate authorities referred to in the text.

Every effort has been made to accurately reflect the legislation in force at the time of preparation of this material.

Other publications available from the "Doing Business in Canada" series are:

## DOING BUSINESS IN CANADA

Forms of Business Organization (IRDA) (AIDIA)

Canadian (PAR) (IRDA) (AIDIA)

## FEDERAL INCENTIVES

Income Tax (IRDA) (AIDIA)

Income Tax (IRDA) (AIDIA)

## TO INDUSTRY

Income Tax (IRDA) (AIDIA)

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## PREPARED BY

## DEPARTMENT OF INDUSTRY

## O T T A W A

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F O R E W O R D

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Other publications available from the "Doing Business in Canada" series are:

The Canadian Environment

Forms of Business Organization

Canadian Customs Duties

Taxation - Income, Business, Property

Taxation - Sales, Excise, Commodity

Labour Legislation

Construction and Equipment Standards

Patents, Copyrights and Trade Marks

Tariff Preferences for Canadian Goods Abroad

Other publications available upon request are:

Financing Canadian Industries

Federal Services for Business

Revised: November, 1967

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## FEDERAL INCENTIVES TO INDUSTRY

### Introduction

The Canadian economy is becoming increasingly characterized by a broad population base, expansion of the domestic market, urbanization and diversified production facilities. In effect, Canada has undergone a modern industrial revolution in which advanced technology, modern transportation facilities and a highly skilled and flexible labour force are combined in an expanding market with a factory-based system of specialized production to serve it. These basic structural changes have decisively committed the Canadian economy to an industrial future.

The encouragement of industrial expansion has always been of major concern to Canada. In its effort to ensure continued sound industrial growth, the Canadian government is aware that an attractive investment climate must, in some areas, be complemented by positive incentive measures geared to the needs of industry and to the requirements for a maximum rate of growth on the basis of available resources.

This chapter of the "Doing Business in Canada" series is intended only to highlight the major industrial development incentives available at the federal level.

### INCENTIVES FOR AREA DEVELOPMENT

Despite the favorable developments which have characterized the Canadian economy over the years, there remains a number of regions which have experienced long-term high unemployment and which have lagged behind the national rate of economic growth. The Area Development Agency was established within the Department of Industry to stimulate economic and industrial expansion within such regions. The Agency administers a program of grants and special depreciation allowances.

#### Area Development Grants

Capital grants are available for new manufacturing and processing facilities establishing in designated areas as well as to firms already located in these areas which undertake significant expansions there. The areas which have been designated are listed in Appendix "A". Grants are available only in respect of projects not committed prior to July 1, 1965, and which commence commercial operations before expiry of the program on March 31, 1971.

The amounts of the grants are related to the total investment by these firms in new buildings and equipment. The development grants are exempt from federal income tax and do not reduce the amount of capital cost which may be used for tax purposes. A firm which qualifies for a grant may choose to take an equivalent amount in the form of a credit against its income tax liabilities.

Two of the major conditions for eligibility under the program are as follows:

- (1) at least 95% of the value of all machinery and equipment must be unused prior to use in the facility, and
- (2) at least 95% of the value of machinery, equipment, buildings and other fixed assets used in the facility must be located in the designated area.

Formulas for grants for new and expanding facilities are outlined in Appendix "B".

Assuming the applicant has sufficient equity in the project, payment of grants is as follows: 60% paid on the date of commencement of commercial production, 20% paid 12 months from that date, and the final 20% paid at the end of the following 12 month period.

#### Special Depreciation Allowances

Firms eligible for the Development Grant may also take special depreciation tax allowances for machinery, equipment and buildings in the following manner:

- a) Most new machinery and equipment can be written-off at an annual rate of up to 50% on a straight-line basis..
- b) New buildings and significant extensions can be written-off at an annual rate of up to 20% on a straight-line basis.

The foregoing is only an outline of the area development incentive measures. Firms proposing to take advantage of the program are advised to contact the Area Development Agency, Department of Industry, Ottawa.



## INDUSTRIAL RESEARCH AND DEVELOPMENT

### Introduction

Industrial research and development is encouraged generally with income tax allowance incentives, and by the Industrial Research and Development Incentives Act (IRDIA). Further assistance for worthy projects is offered for research by the Industrial Research Assistance Program (IRAP), and for research leading to commercial development by the Program for the Advancement of Industrial Technology (PAIT). In the area of defence, research projects are aided by the Defence Industrial Research Program (DIR), administered by the Defence Research Board, while the Defence Development Sharing Program of the Department of Industry encourages developments which have commercial defence export potential. The latter four incentive programs are designed to supplement the first two general incentives, and to ensure, insofar as it is practicable to do so, that no worthwhile research and development projects are abandoned for lack of financial support.

### Income Tax Allowances

Under Section 72 of the federal Income Tax Act a corporation may deduct from its income all expenditures of a current nature made in Canada for scientific research, and all expenditures of a capital nature made in Canada (for the acquisition of property other than land) for scientific research, in the year in which they were incurred.

For purposes of this measure, "scientific research" means a systematic investigation or search by means of experimentation or analysis in the field of science to acquire new knowledge, to devise and develop new products and processes and/or to apply newly acquired knowledge in making improvements to existing products or processes. In some cases, expenditures to develop, test and evaluate a prototype are considered as scientific research expenditures. However, expenditures for purposes such as market research, sales promotion, quality control or preparation of specifications are not recognized as eligible expenditures.

### Industrial Research and Development Incentives Act (IRDIA)

The Industrial Research and Development Incentives Act was enacted in March, 1967 to provide general incentives to industry for the expansion of scientific research and development in Canada. The Act is administered by the Department of Industry.

The new Act provides that taxable Canadian corporations may make application for cash grants, or credits against federal income tax liabilities, equal to 25% of:

- a) all capital expenditures (other than for land) incurred in the past fiscal year on research and development carried out in Canada; and
- b) the increase in current expenditures in Canada for scientific research and development over the average of such expenditures in the preceding five years.

For the purposes of the Act "scientific research and development" means systematic investigation or search carried out in a field of science or technology by means of experiment or analysis. It includes basic research, applied research and development which is defined as using the results of basic or applied research for the purpose of creating new or improving existing materials, devices, products or processes. Market research, sales promotion, quality control, prospecting, exploring or drilling for or producing minerals, petroleum or natural gas, commercial production, style changes and routine data collection are excluded from the definition of scientific research and development.

To qualify for a grant, expenditures must be for scientific research and development likely to benefit Canada. To this end, corporations must undertake to exploit the results of their research and development work in Canada, unless according to sound business judgment it would be uneconomic to do so. Furthermore, corporations must normally be free to exploit the results of their research and development in all export markets.

Grants made under the Act are not subject to federal income tax and are in addition to the normal 100% deduction of all expenditures for scientific research under the Income Tax Act.

Additional information may be obtained by writing to IRDIA, Department of Industry, Ottawa 4, Ontario.

#### Industrial Research Assistance Program (IRAP)

This program was established by the National Research Council in 1962 to encourage scientific research by Canadian industry. Assistance is in the form of grants and is intended



primarily for applied research and development up to, but not including, pre-engineering preparation for production.

Financial assistance under this program is concentrated mainly on relatively long-term applied research through the establishment of new industrial research teams or the expansion of existing research groups. It excludes fields such as quality control, testing of products and production techniques, market research and sales operations. Minor improvement of existing machines and processes, development of new applications of a product, and other similar work do not receive prime consideration under the program.

The initiative in project selection rests entirely with the firm and the N.R.C. Committee on Industrial Research Assistance assesses the program on its scientific merits and the capabilities of the company and its staff. The cost of an approved project is usually shared on the basis of approximately equal contributions by the National Research Council and industry. In practice, the division of costs generally provides for the payment of salaries and wages of scientific and technical staff by the government with payment for equipment and overhead by industry. Commercial security of industrial projects is maintained and all titles and rights to research results are retained by industry.

For further information, interested firms should contact the Secretary, N.R.C. Committee on Industrial Research Assistance, National Research Council, Ottawa.

#### Program for the Advancement of Industrial Technology (PAIT)

This is a program of direct financial assistance, administered by the Department of Industry, to stimulate sound industrial growth through the application of science and technology. The basic aim of the program is to help industry upgrade its technology and its innovation activity by underwriting specific development projects which involve a significant advance in technology and which, if successful, offer good prospects for commercial exploitation.

Assistance under the program is available to individual Canadian companies for development projects to be carried out in Canada. Under the program, the Department of Industry can share up to 50% of the cost of special equipment and prototypes. However, it is not the purpose of the program to finance the establishment of a business, or the acquisition of general purpose capital facilities, or to cover the cost of setting up production.

Choice of development projects and responsibility for their direction and execution rest with industry. Applications will be assessed on the basis of the technical and commercial feasibility of the project. Companies will normally be expected to have the means to undertake the development work and also to provide for the manufacture and marketing of the end product or for the use of the resulting process. However, where necessary companies may subcontract portions of the work to other companies, research institutes, universities or consultants within Canada.

In the event a project is technically successful and the results are put into commercial use, the company will be required to repay the Department's contribution with interest. The rate of repayment will be negotiated with the company and will be related to the commercial utilization of the product or process. However, it is foreseen that the repayment period should not exceed ten years from the date of first commercial use or sale by the company. If the project results are not put into commercial use, the company will not be required to repay the Department's contribution.

Title to patents, designs, information and equipment resulting from the project will be held by the company. However, the company will be required to give an undertaking to exploit the successful results of a project in Canada within a reasonable period of time.

For further details on the Program for the Advancement of Industrial Technology, interested companies should write to:

PAIT Program Office  
Department of Industry  
OTTAWA

FEDERAL SALES TAX - EXEMPTION/REDUCTION

1. Effective March 30, 1966, the following are exempt from federal sales tax when for use by manufacturers or producers directly in the manufacture or production of goods -
  - (a) dies, jigs, fixtures and moulds,
  - (b) patterns for dies, jigs, fixtures and moulds,  
and

- (c) tools for use in or attachment to production machinery that are for working materials by turning, milling, grinding, polishing, drilling, punching, boring, shaping, shearing, pressing or planing.
- 2. Effective June 2, 1967, the federal sales tax was removed on machinery and apparatus sold to or imported by manufacturers or producers for use by them directly in the manufacture or production of goods.

### CUSTOMS INCENTIVES

Canadian customs legislation contains a number of concessions favourable to domestic manufacturing activity. It should be noted, however, that duty concessions are not granted strictly on the basis that a firm is becoming established in Canada or is undertaking new manufacturing activity.

Outlined below are some of the major customs incentives of interest to manufacturers. For details on any of these measures, interested firms should get in touch with the Customs and Excise Division, Department of National Revenue, Ottawa.

#### Tariff Relief - Manufacturers

The Customs Tariff contains a number of items providing for the duty-free entry of articles and materials to be used exclusively in the manufacture of certain merchandise in Canada. These items are intended to encourage processing operations in Canada. Also, the Minister of Finance can authorize certain reductions in duty by the establishment of temporary tariff items. They remain temporary for varying periods of time and, if warranted, can become statutory. It should be stressed that materials imported under such duty free conditions, or at reduced rates of duty, are to be used exclusively in the manufacture of specified products.

#### Dies, Moulds

Authority may be obtained to import into Canada, on a temporary basis for a maximum period of twelve months, plant equipment such as dies, moulds, patterns and related jigs and fixtures, paying duty on the basis of one-sixtieth



of the value of the goods for each month or part of a month they remain in Canada subject to a minimum payment of \$25. per entry. This measure is intended to alleviate the high cost of duplicating such equipment for limited production runs, and encourages higher Canadian content in the finished product. This concession has been well received by industry and is used extensively. The regulations governing such temporary entry allow Customs Collectors at ports of entry to authorize the temporary importation of such plant equipment rather than refer each case to Ottawa for approval.

### Duty Drawbacks

The Customs Tariff includes several drawback items which permit the return of duty to the importer when materials, machinery or equipment are applied to specified uses. In addition, drawback provisions also apply in the case of goods imported for further processing in Canada and re-exported either to the same country from which the goods were originally imported or to a third country. In such circumstances, a 99% duty drawback is normally available.

There is one drawback provision which may be of interest to manufacturers using both imported and domestic materials of the same class in the production of goods subsequently exported. In order to avoid the maintenance of segregated stocks of domestic and imported materials for duty drawback purposes, the manufacturer is allowed to claim recovery of duty paid on the imported portion on the basis of equivalent content in the exported goods. An example of this would be a stock of soda ash composed partly of Canadian soda ash and partly imported. The soda ash would be used in the refining of metal sold domestically and exported. The manufacturer could claim a 99% duty drawback on the imported soda ash in an amount equivalent to the quantity of soda ash used to refine the exported metal. "Equivalents" must be applied to exports within twelve (12) months of actual use of the imported material.

### Production Components

It can be stated generally that a manufacturer in Canada who must use imported production components in his manufacturing operation can achieve savings on the basis of a lower value for duty. In such circumstances, a great deal depends on the extent of fabrication carried out in Canada.

If the components are imported for an assembly operation without the introduction of a reasonable Canadian content, it is likely that the only saving in valuation for duty would be the assembly and packaging costs transferred to Canada. However, in the case of a manufacturing operation, the imported production components can be valued for duty purposes on the basis of factory cost (material, labour and factory overhead only) in the country of export plus a percentage advance. The size of this advance would vary depending in part on the degree of Canadian content attained in the finished product. If the Canadian content is high, the saving can be worthwhile.

A more detailed outline of the provisions for establishing value for duty on production parts, as well as on finished articles, is contained in the chapter "Canadian Customs Duties" from this series. Manufacturers are well advised to obtain valuation rulings in advance of importation from the Customs and Excise Division, Department of National Revenue, Ottawa.

#### INCENTIVE FOR CANADIAN OWNERSHIP

##### Dividend Payments

Dividends paid or credited to a non-resident shareholder are subject to a 15% tax. However, this tax is reduced to 10% if the corporation declaring the dividends has a "degree of Canadian ownership". The term "dividend" includes all distributions of earnings or profits of a corporation. For details concerning the meaning of "degree of Canadian ownership", see Appendix "C".

#### OTHER PROGRAMS

Such programs as Automotive Adjustment Assistance Program, Defence Development Sharing Program, Industry Modernization for Defence Exports Program and the Shipbuilding Program, all of which are administered by the Department of Industry are not described in this booklet, as they are incentive programs of limited application, not designed to be general industrial development incentives.

Also beyond the scope of this booklet are the many general government services to industry, described in the Department of Industry publication "Federal Services for Business".

# APPENDIX "A"

## CANADA MANPOWER CENTRE AREAS DESIGNATED UNDER THE AREA DEVELOPMENT INCENTIVES ACT

| <u>Newfoundland</u>     | <u>New Brunswick</u> | <u>Quebec</u>               |
|-------------------------|----------------------|-----------------------------|
| Corner Brook            | Bathurst             | Alma                        |
| Grand Falls             | Campbellton          | Baie Comeau                 |
| St. John's (Labrador *) | Edmundston           | Buckingham                  |
|                         | Minto                | Causapsal                   |
| <u>Nova Scotia</u>      | Moncton              | Chandler                    |
| Amherst                 | Newcastle            | Chicoutimi                  |
| Bridgewater             | St. Stephen          | Dolbeau                     |
| Inverness               | Sussex               | Forestville                 |
| Kentville               | Woodstock            | Gaspé                       |
| Liverpool               |                      | Jonquière                   |
| New Glasgow             | <u>Ontario</u>       | Lachute                     |
| Springhill              | Bracebridge          | La Malbaie                  |
| Sydney                  | Elliot Lake          | La Tuque                    |
| Sydney Mines            | Hawkesbury           | Louiseville                 |
| Truro                   | Kirkland Lake        | Maniwaki                    |
| Yarmouth                | New Liskeard         | Mantane                     |
|                         | North Bay            | Mégantic                    |
| <u>British Columbia</u> | Parry Sound          | Mont Laurier                |
| Kelowna                 | Sturgeon Falls       | Montmagny                   |
| Penticton               | Timmins              | New Richmond                |
| Vernon                  |                      | Port Alfred                 |
|                         | <u>Manitoba</u>      | Rimouski                    |
| <u>Saskatchewan</u>     | Brandon              | Rivière du Loup             |
| Lloydminster            | Dauphin              | Roberval                    |
| North Battleford        | The Pas              | Shawinigan                  |
| Prince Albert           | Selkirk              | St. Jérôme                  |
| Yorkton                 |                      | Ste. Agathe                 |
|                         |                      | Sept-Isles                  |
|                         |                      | Ville St. Georges           |
|                         |                      | <u>Prince Edward Island</u> |
|                         |                      | Charlottetown               |
|                         |                      | Summerside                  |

### Countries and Census Divisions that Qualify for Designation:

|                         |                           |
|-------------------------|---------------------------|
| Queen's, N.B.           | Census Division 3, Man.   |
| Beauce, P.Q.            | Census Division 10, Man.  |
| Berthier, P.Q.          | Census Division 18, Man.  |
| Labelle, P.Q.           | Census Division 19, Man.  |
| Pontiac, P.Q.           | Census Division 5, Sask.  |
| Haliburton, Ont.        | Census Division 10, Sask. |
| Parry Sound, Ont.       | Census Division 13, Sask. |
| Manitoulin Island, Ont. | Census Division 12, Alta. |
| Census Division 2, Man. | Census Division 13, Alta. |

\* to include Lake Melville district and coastal settlements south of the 55th Parallel.



APPENDIX "B"

FORMULAS FOR GRANTS TO NEW AND EXPANDING FACILITIES  
UNDER THE ADA PROGRAM

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Formula No. 1. For establishment of new facility:

1. Where the approved capital costs do not exceed \$250,000, the amount of the development grant shall not exceed an amount equal to  $\frac{1}{3}$  of the approved capital costs.
2. Where the approved capital costs exceed \$250,000 but do not exceed \$1,000,000, the amount of the development grant shall not exceed the aggregate of
  - (a)  $\frac{1}{3}$  of \$250,000, and
  - (b)  $\frac{1}{4}$  of the amount of the approved capital costs in excess of \$250,000.
3. Where the approved capital costs exceed \$1,000,000, the amount of the development grant shall not exceed the lesser of
  - (a) the aggregate of
    - (i)  $\frac{1}{3}$  of \$250,000,
    - (ii)  $\frac{1}{4}$  of \$750,000, and
    - (iii)  $\frac{1}{5}$  of the amount of the approved capital costs in excess of \$1,000,000, or
  - (b) \$5,000,000.

Formula No. 2. For expansion of existing facility:

The amount of a development grant for the expansion of an existing facility shall not exceed the lesser of

- (a) the amount obtained when formula No. 1 is applied to the amount remaining after subtracting from the approved capital costs the greater of 10% of the value as determined by the Minister of the existing facility being expanded or \$10,000; or
- (b) \$5,000,000.

"Canadian Ownership"

1. The company must be a resident of Canada.
2. (A) No less than 25% of the company's issued and outstanding voting shares and no less than 25% of the equity share capital of the company must be owned in Canada (by individuals and/or by Canadian controlled companies).

(B) A class or classes of voting shares and a class or classes of equity shares representing not less than 50% of the equity share capital of the company must be listed on a Canadian stock exchange and no more than 75% of the voting shares must be owned by one non-resident person or related persons.

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