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# SR&ED Capital Expenditures Policy

Date: December 18, 2014

## Changes to the SR&ED Capital Expenditures Policy

### Reasons for revision

This revision accommodates the legislative changes that have been announced.

### Revision overview

Scientific research and experimental development (SR&ED (scientific research and experimental development)) capital expenditures made after December 31, 2013 do not qualify for SR&ED (scientific research and experimental development) tax incentives. The rules applicable to claiming SR&ED (scientific research and experimental development) capital expenditures contained in this policy document are applicable to those expenditures made before 2014.

The text of this document has been revised to reflect these changes, see [Appendix C.1 Explanation of changes](#).

## **Table of contents**

### 1.0 Purpose

### 2.0 Overview

#### 2.1 Capital expenditures made after 2013

#### 2.2 Capital expenditures made before 2014

##### 2.2.1 SR&ED capital expenditures as an income deduction

##### 2.2.2 Introduction to shared-use-equipment

##### 2.2.3 SR&ED capital expenditures as qualified SR&ED expenditures

### 3.0 Legislation

#### 3.1 Capital expenditures made after 2013 cannot be claimed

##### 3.1.1 Expenditures of a current nature

##### 3.1.2 Capital look-through rule and the reporting of certain payments

#### 3.2 Capital expenditures made before 2014 can be claimed

##### 3.2.1 Criteria for SR&ED capital expenditures – Traditional method

##### 3.2.2 Criteria for SR&ED capital expenditures – Proxy method

##### 3.2.3 Additional criteria for SR&ED capital expenditures for both traditional and proxy methods

##### 3.2.4 SR&ED capital expenditure deduction deemed capital cost allowance

#### 3.3 Available for use

### 4.0 Terms

#### 4.1 All or substantially all

#### 4.2 Operating time

#### 4.3 General purpose office equipment or furniture

### 5.0 Depreciable property.

#### 5.1 Capital cost allowance

##### 5.1.1 Ownership of capital property.

##### 5.1.2 No ownership of capital property.

### 5.1.3 Deemed ownership of leased property

## 5.2 Capital cost of property

## 6.0 Intent

### 6.1 Reason for purchase

### 6.2 Potential use of property

### 6.3 Actual use of property

### 6.4 Type of SR&ED

### 6.5 SR&ED environment

### 6.6 Length of SR&ED project

### 6.7 Claimants past practices

### 6.8 Planning documents

## 7.0 Expenditures not allowed as SR&ED capital expenditures

### 7.1 Non-depreciable property

### 7.2 Expenditures for buildings

#### 7.2.1 Meaning of "building"

#### 7.2.2 Exception – Third-party payments concerning buildings may be allowed

### 7.3 Expenditures for capital property that is used outside Canada

## 8.0 SR&ED capital expenditures that are not allowed as qualified SR&ED expenditures

### 8.1 SR&ED capital expenditures prescribed by the Income Tax Regulations

#### 8.1.1 Acquisition of used property

#### 8.1.2 Refurbishment of used property

### 8.2 Expenditures for purchases of SR&ED capital property from non-arm's length parties

## 9.0 Sale of SR&ED capital property or change in use of SR&ED capital property

## 9.1 Recapture of capital cost allowance for claimed and unclaimed SR&ED capital expenditures

## 9.2 Recapture of SR&ED investment tax credit

## 10.0 Related topics to SR&ED capital expenditures

### 10.1 Development of an asset

### 10.2 Criteria in determining whether an expenditure is on account of capital or a current expense

### 10.3 Expenditures for software and software licenses before 2014 may be capital or current expenditures

### 10.4 Related current costs

## 11.0 Documentation and other evidence

### 11.1 Examples of documentation and other evidence

## Appendix A – Special-purpose building

## Appendix B – Consolidated policy references

### Appendix B.1 Legislative references

### Appendix B.2 Jurisprudence

## Appendix C – Revisions

### C.1 Explanation of changes

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# 1.0 Purpose

This policy document deals with capital expenditures made by a claimant for the prosecution of scientific research and experimental development (SR&ED (scientific research and experimental development)) carried on in Canada. This document clarifies the position of the Canada Revenue Agency (CRA (Canada Revenue Agency)) regarding capital expenditures



when administering the SR&ED (scientific research and experimental development) legislation under the federal *Income Tax Act* and the *Income Tax Regulations*.

The purpose of this document is to:

- explain that capital expenditures made after December 31, 2013 no longer qualify for SR&ED (scientific research and experimental development) tax incentives;
- explain expenditures of a current nature after 2013;
- explain that capital expenditures made before 2014 may be claimed for SR&ED (scientific research and experimental development) purposes;
- provide guidelines for determining the intent of a claimant that acquired capital property for the prosecution of SR&ED (scientific research and experimental development) carried on in Canada (SR&ED (scientific research and experimental development) capital property) before 2014;
- explain the nature of SR&ED (scientific research and experimental development) capital property as depreciable property; and
- identify issues surrounding the sale of SR&ED (scientific research and experimental development) capital property.

### **Legislative References *Income Tax Act***

Paragraph 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

Subclause 37(8)(a)(ii)(A)(III) SR&ED (scientific research and experimental development) expenditures in Canada under the traditional method – ASA (all or substantially all) capital expenditures [Repealed]

Subclause 37(8)(a)(ii)(B)(III) SR&ED (scientific research and experimental development) expenditures in Canada under the proxy method – ASA (all or substantially all) capital expenditures [Repealed]

Paragraph 37(8)(d) SR&ED (scientific research and experimental development)

expenditures specifically excluded

Former paragraph 37(8)(d) SR&ED (scientific research and experimental development)

expenditures specifically excluded

Subsection 127(9) Definition of "qualified expenditure"

## 2.0 Overview

### 2.1 Capital expenditures made after 2013

The 2012 federal budget announced that expenditures of a capital nature made after 2013, will no longer qualify for SR&ED (scientific research and experimental development) tax incentives. This includes capital expenditures made **before** 2014 (see section 3.2) for property that became available for use (see section 3.3) after 2013. Further, for SR&ED (scientific research and experimental development) purposes, expenditures of a current nature made after 2013 exclude expenditures for capital property or the right to use capital property (see section 3.1.1).

The distinction between a current and a capital expenditure is ever more important now that capital expenditures no longer qualify for any SR&ED (scientific research and experimental development) tax incentives. Thus, the comments in section 10.2 may provide some assistance in making this distinction.

Further, contract expenditures and third-party payments incurred after December 31, 2013 must be reduced by the amount of any related expenditure of the SR&ED (scientific research and experimental development) performer that is not an expenditure of a current nature (see section 3.1.2).

The following sections of this policy document may be relevant to expenditures for capital property made after 2013:

- [Section 3.0](#) Legislation
- [Section 3.3](#) Available for use
- [Section 9.0](#) Sale of capital property
- [Section 10.2](#) Current vs capital expenditures
- [Section 10.4](#) Related current costs

### **Legislative References *Income Tax Act***

Paragraph 37(1)(b) Pool of deductible ~~SR&ED (scientific research and experimental development)~~ expenditures – capital expenditures [Repealed]

Subsection 37(1.2) Available for use

Paragraph 37(8)(d)(i) ~~SR&ED (scientific research and experimental development)~~ expenditures specifically excluded – capital property

Subsection 37(14) Look-through rule

## **2.2 Capital expenditures made before 2014**

Generally, a claimant carrying on a business in Canada in a tax year may, in calculating income from the business for the year, deduct expenditures for the prosecution of ~~SR&ED (scientific research and experimental development)~~ carried on in Canada that relates to a business of the claimant.

The first step to claiming an ~~SR&ED (scientific research and experimental development)~~ capital expenditure made before 2014 is to determine whether the ~~SR&ED (scientific research and experimental development)~~ expenditure is current or capital in nature. The distinction between current and capital is important because of the difference in investment tax credit (ITC (investment tax credit)) refundability rates for certain corporations. The distinction is also important because some expenses that would

normally be capital for accounting and tax purposes which would be deducted over many years, are fully deductible in the year as SR&ED (scientific research and experimental development) expenditures.

For more information on rates of refundable ITC (investment tax credit), please refer to the SR&ED (scientific research and experimental development) Investment Tax Credit Policy.

**Current** expenditures made before 2014 on or in respect of SR&ED (scientific research and experimental development) are considered to be those expenditures that do not result in the acquisition of land, a leasehold interest in land, or property that would otherwise be **depreciable property** (see section 5.0) to the claimant.

**Capital** expenditures made before 2014 for the prosecution of SR&ED (scientific research and experimental development) carried on in Canada are **only** those expenditures that result in the acquisition of property that would be the claimant's depreciable property, other than a building or a leasehold interest in a building (see section 7.2). Expenditures for non-depreciable property such as the acquisition of land, property that is described in a claimant's inventory, or eligible capital property (such as goodwill) **cannot** be included in the pool of deductible SR&ED (scientific research and experimental development) expenditures as an SR&ED (scientific research and experimental development) capital expenditure (see section 7.1).

Expenditures on capital property made before 2014 that is intended (see section 6.0) to be used during all or substantially all (ASA (all or substantially all)) (see section 4.1) of its **operating time** (see section 4.2) in the prosecution of SR&ED (scientific research and experimental development) carried on in Canada, or ASA (all or substantially all) of its **value** would be consumed in the prosecution of SR&ED (scientific research

and experimental development) carried on in Canada may qualify as SR&ED (scientific research and experimental development) capital expenditures (see [section 3.0](#)).

The next steps to claiming an SR&ED (scientific research and experimental development) capital expenditure are to determine whether the capital expenditures made before 2014 are for SR&ED (scientific research and experimental development) carried on in or outside Canada (see [section 7.3](#)) and when the property became available for use (see [section 3.3](#)).

When a claimant sells their SR&ED (scientific research and experimental development) capital property, the tax treatment of the proceeds may vary depending on whether a deduction for the property has previously been claimed (see [section 9.0](#)).

If an expenditure was not claimed on [Form T661, Scientific Research and Experimental Development \(SR&ED \(scientific research and experimental development\)\) Expenditures Claim](#) by the reporting deadline, this will cause the expenditure to be classified as a normal business expense or outlay in accordance with the Act. For example, an expenditure to acquire depreciable property, which would have been an SR&ED (scientific research and experimental development) capital expenditure deductible in the year had the filing requirements been met, would generally be treated as an acquisition of depreciable property.

For more information on the reporting deadline, please refer to the [SR&ED \(scientific research and experimental development\) Filing Requirements Policy](#).

### **Legislative References *Income Tax Act***

Subsection 13(21) Definition of "depreciable property"

Subsection 37(1) Pool of deductible SR&ED (scientific research and experimental

~~development) expenditures~~

~~Paragraph 37(1)(a) Pool of deductible SR&ED (scientific research and experimental development) expenditures – current expenditures~~

~~Paragraph 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]~~

~~Subsection 37(2) Research outside Canada~~

~~Subclause 37(8)(a)(ii)(A)(III) SR&ED (scientific research and experimental development) expenditures in Canada under the traditional method – ASA (all or substantially all) capital expenditures [Repealed]~~

~~Subclause 37(8)(a)(ii)(B)(III) SR&ED (scientific research and experimental development) expenditures in Canada under the proxy method – ASA (all or substantially all) capital expenditures [Repealed]~~

~~Subsection 37(11) Filing requirement~~

## **2.2.1 SR&ED (scientific research and experimental development) capital expenditures as an income deduction**

For expenditures made before 2014, a claimant may fully deduct its ~~SR&ED (scientific research and experimental development)~~ capital expenditures (see [section 3.2](#)) incurred in the tax year when determining their income for tax purposes in the tax year. A claimant may also, to the extent that those ~~SR&ED (scientific research and experimental development)~~ capital expenditures have not been deducted in the tax year, carry these expenditures forward to reduce their income for tax purposes in future tax years. The carry forward amount will be subject to certain limits if the claimant is a corporation whose control has been acquired by a person or group of persons.

For more information on deducting ~~SR&ED (scientific research and experimental development)~~ expenditures, please refer to the [Pool of Deductible SR&ED \(scientific research and experimental development\)](#)

Expenditures Policy. For more information on acquisition of control, please refer to section 5.1 of the SR&ED (scientific research and experimental development) Investment Tax Credit Policy.

### **Legislative Reference *Income Tax Act***

Paragraph 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

## **2.2.2 Introduction to shared-use equipment**

Expenditures for capital property made before 2014 that **do not** meet the ASA (all or substantially all) criteria (see sections 3.2.1 and 3.2.2) do not qualify as an SR&ED (scientific research and experimental development) capital expenditure. However, where claimants perform SR&ED (scientific research and experimental development) in an environment where their capital property is used for both SR&ED (scientific research and experimental development) and commercial work, their capital property may qualify as shared-use-equipment (SUE (shared-use-equipment)) and be included in qualified SR&ED (scientific research and experimental development) expenditures. An expenditure on capital property that is used primarily during its operating time in SR&ED (scientific research and experimental development) may meet the requirements of SUE (shared-use-equipment) provided requirements for first term and second term shared-use-equipment are met.

For more information on first term and second term shared-use equipment, please refer to the SR&ED (scientific research and experimental development) Shared-Use-Equipment Policy. For more information on qualified SR&ED (scientific research and experimental development)

expenditures, please refer to the Total Qualified SR&ED (scientific research and experimental development) Expenditures for Investment Tax Credit Purposes Policy.

### **Legislative References *Income Tax Act***

Subsection 37(1) Pool of deductible SR&ED (scientific research and experimental development) expenditures

Subsection 37(2) Research outside Canada

Subclause 37(8)(a)(ii)(A)(III) SR&ED (scientific research and experimental development) expenditures in Canada under the traditional method – ASA (all or substantially all) capital expenditures [Repealed]

Subclause 37(8)(a)(ii)(B)(III) SR&ED (scientific research and experimental development) expenditures in Canada under the proxy method – ASA (all or substantially all) capital expenditures [Repealed]

Subsection 127(9) Definition of "first term shared-use-equipment"

Subsection 127(9) Definition of "second term shared-use-equipment"

### **2.2.3 SR&ED (scientific research and experimental development) capital expenditures as qualified SR&ED (scientific research and experimental development) expenditures**

A claimant may earn ITC (investment tax credit)s on **SR&ED (scientific research and experimental development) capital expenditures** made before 2014 that meet the rules for qualified SR&ED (scientific research and experimental development) expenditures. For an expenditure to be a qualified SR&ED (scientific research and experimental development) expenditure, the expenditure must first meet the criteria as a deductible SR&ED (scientific research and experimental development) capital expenditure (see sections 3.2 to 3.3). For more information on deductible



SR&ED (scientific research and experimental development) expenditures, please refer to the Pool of Deductible SR&ED (scientific research and experimental development) Expenditures Policy.

An SR&ED (scientific research and experimental development) capital expenditure made before 2014 that is included in the pool of deductible SR&ED (scientific research and experimental development) expenditures may not necessarily be a qualified SR&ED (scientific research and experimental development) expenditure for ITC (investment tax credit) purposes. For example, a qualified expenditure does not include prescribed expenditures such as used equipment (see sections 8.0 to 8.2).

In addition, when a claimant purchases goods or services (other than where SR&ED (scientific research and experimental development) work is performed on behalf of the claimant) from a person with whom the claimant **does not** deal at arm's length at the time of the transaction, the amount of qualified SR&ED (scientific research and experimental development) expenditures for ITC (investment tax credit) purposes may be restricted (see section 8.2).

For more information on qualified SR&ED (scientific research and experimental development) expenditures, please refer to the Total Qualified SR&ED (scientific research and experimental development) Expenditures for Investment Tax Credit Purposes Policy.

### **Legislative References *Income Tax Act***

Paragraph 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

Subsection 127(9) Definition of "qualified expenditure"

## Legislative Reference *Income Tax Regulations*

Former paragraph 2902(b) Prescribed capital expenditures for purposes of qualified expenditures

# 3.0 Legislation

## 3.1 Capital expenditures made after 2013 cannot be claimed

Capital expenditures made after December 31, 2013 can no longer be claimed for SR&ED (scientific research and experimental development) purposes. This is also applicable to capital expenditures (see section 3.2) deemed to have been made after 2013 due to the available for use rules (see section 3.3).

## Legislative References *Income Tax Act*

Paragraph 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

Subsection (37(1.2) Available for use

### 3.1.1 Expenditures of a current nature

For SR&ED (scientific research and experimental development) purposes, **expenditures of a current nature** include **any** expenditures made by the claimant **other than** an expenditure for:

- the acquisition of capital property of the claimant, or
- the use of, or the right to use, property that would be capital property of the claimant if it were owned by the claimant.

These rules apply to expenditures made after 2013. For more information on the use or right to use capital property, please refer to the SR&ED (scientific research and experimental development) Lease Expenditures Policy.

## **Legislative References *Income Tax Act***

Paragraph 37(8)(d) SR&ED (scientific research and experimental development) expenditures specifically excluded

Section 54 Definition of “capital property”

### **3.1.2 Capital look-through rule and the reporting of certain payments**

The look-through rule—a claimant’s particular expenditure made to a person or partnership (the performer) to be used in SR&ED (scientific research and experimental development) purposes must be reduced by the amount of any related expenditure of the person or partnership to whom the particular expenditure is made that is **not** an expenditure of a current nature of the person or partnership (see [section 3.1.1](#)). In other words, any contract expenditure and third-party payment of the claimant made to an SR&ED (scientific research and experimental development) performer must be reduced by any related expenditure of the SR&ED (scientific research and experimental development) performer that is for capital property, or the use of, or the right to use, capital property (if the capital property were owned by the SR&ED (scientific research and experimental development) performer).

When a claimant is required to reduce their expenditure because of the look-through rule, the SR&ED (scientific research and experimental development) performer is required to inform the claimant in writing of the amount of the reduction. This information is to be provided without delay if requested by the claimant and in any other case no later than 90 days after the end of the calendar year in which the expenditure (of the claimant) was made.

## **Legislative References *Income Tax Act***

Subsection 37(14) Look-through rule

Subsection 37(15) Reporting of certain payments

## 3.2 Capital expenditures made before 2014 can be claimed

### 3.2.1 Criteria for SR&ED (scientific research and experimental development) capital expenditures – Traditional method

If a claimant elects to use the traditional method, an SR&ED (scientific research and experimental development) capital expenditure **made before 2014 means** an expenditure that, at the time it was incurred, was for the provision of premises, facilities, or equipment, when at that time it was **intended** that:

- the capital property would be used during **all or substantially all** (see section 4.1) of its **operating time** (see section 4.2) in its expected useful life for the prosecution of SR&ED (scientific research and experimental development) carried on in Canada; or
- all or substantially all of its **value** would be consumed in the prosecution of SR&ED (scientific research and experimental development) carried on in Canada.

When claiming an SR&ED (scientific research and experimental development) capital expenditure, a claimant should not only consider whether the capital property will be used in SR&ED (scientific research and experimental development) in the year the expenditure was made but should also consider the intended use over the lifetime of the capital property (see section 6.0).

Only those expenditures of a capital nature for the provision of premises, facilities or equipment for the prosecution of SR&ED (scientific research and experimental development) carried on in Canada that meet these criteria may be claimed as an SR&ED (scientific research and experimental development) capital expenditure.

For more information on the traditional method, please refer to the [Traditional and Proxy Methods Policy](#).

### **Legislative References *Income Tax Act***

Paragraph 37(1)(b) Pool of deductible ~~SR&ED (scientific research and experimental development)~~ expenditures – capital expenditures [Repealed]

Subclause 37(8)(a)(ii)(A)(III) ~~SR&ED (scientific research and experimental development)~~ expenditures in Canada under the traditional method – ~~ASA (all or substantially all)~~ capital expenditures [Repealed]

### **3.2.2 Criteria for ~~SR&ED (scientific research and experimental development)~~ capital expenditures – Proxy method**

If a claimant elects to use the [proxy method](#), an expenditure of a capital nature on or in respect of ~~SR&ED (scientific research and experimental development)~~ made before 2014 means the same as it does in [section 3.2.1](#) for the [traditional method](#), except that it does not include general purpose office equipment or furniture (~~GPOEF (general purpose office equipment or furniture)~~) (see [section 4.3](#)).

For more information on the proxy method, please refer to the [Traditional and Proxy Methods Policy](#).

### **Legislative References *Income Tax Act***

Paragraph 37(1)(b) Pool of deductible ~~SR&ED (scientific research and experimental development)~~ expenditures – capital expenditures [Repealed]

Subclause 37(8)(a)(ii)(A)(III) ~~SR&ED (scientific research and experimental development)~~ expenditures in Canada under the traditional method – ~~ASA (all or substantially all)~~ capital expenditures [Repealed]

Subclause 37(8)(a)(ii)(B)(III) ~~SR&ED (scientific research and experimental development)~~ expenditures in Canada under the proxy method – ~~ASA (all or substantially all)~~ capital expenditures [Repealed]

### **3.2.3 Additional criteria for SR&ED (scientific research and experimental development) capital expenditures for both traditional and proxy methods**

In order to include an SR&ED (scientific research and experimental development) capital expenditure in the pool of deductible SR&ED (scientific research and experimental development) expenditures:

- the expenditure must be made before January 1, 2014;
- the capital property must be a new or used property that would otherwise be considered depreciable property (see sections 5.0 to 5.2 for further explanations regarding depreciable property, capital cost of property, capital cost allowance (CCA (capital cost allowance)), and undepreciated capital cost (UCC (undepreciated capital cost)));
- the expenditure must be made by a claimant for the prosecution of SR&ED (scientific research and experimental development) carried on in Canada that is directly undertaken by, or on behalf of, the claimant and that is related to a business of the claimant; and
- the capital property must be available for use before January 1, 2014 (see section 3.3).

These criteria must be met in order for a capital expenditure to be included in the pool of deductible SR&ED (scientific research and experimental development) expenditures when claimants use either the traditional method (see section 3.2.1) or the proxy method (see section 3.2.2) to determine their SR&ED (scientific research and experimental development) expenditures.

#### **Legislative References *Income Tax Act***

Paragraph 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

Subsection 37(1.2) Available for use

### **3.2.4 SR&ED (scientific research and experimental development) capital expenditure deduction deemed capital cost allowance**

If the pool of deductible SR&ED (scientific research and experimental development) expenditures includes an expenditure for capital property, the same property cannot also be claimed for CCA (capital cost allowance). Therefore, a claimant is prevented from duplicating deductions for capital expenditures by claiming CCA (capital cost allowance) on such expenditures as well as deducting the SR&ED (scientific research and experimental development) capital expenditure in determining their income for tax purposes in the year.

For the purposes of the rules concerning depreciable property (definition of depreciable property, recapture rules, etc. (and so forth)), an SR&ED (scientific research and experimental development) capital expenditure deducted by the claimant in determining their income for tax purposes in the year will be deemed to be an amount that has been allowed to the claimant as CCA (capital cost allowance). The SR&ED (scientific research and experimental development) capital expenditure deducted by the claimant in the year is deemed to be claimed as CCA (capital cost allowance) in order to satisfy other rules of the *Income Tax Act*. The treatment of the sale of SR&ED (scientific research and experimental development) capital property is an example of these rules (see section 9.1).

SR&ED (scientific research and experimental development) capital property is also deemed to be of a separate prescribed class for CCA (capital cost allowance). As such, an amount may be required to be included in the claimant's income as recapture of CCA (capital cost allowance) if the property is disposed of (see section 9.1). For more information, please refer to the Recapture of SR&ED (scientific research and experimental development) Investment Tax Credit Policy.

## **Legislative References *Income Tax Act***

Section 13 Rules concerning depreciable property

Subsection 13(1) Recaptured depreciation

Paragraph 20(1)(a) Deduction for capital cost of a property

Subsection 37(1) Pool of deductible SR&ED (scientific research and experimental development) expenditures

Paragraph 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

Subsection 37(6) Expenditures of a capital nature

## **Legislative Reference *Income Tax Regulations***

Paragraph 1102(1)(d) SR&ED (scientific research and experimental development) deduction deemed not allowed for capital cost allowance

## **3.3 Available for use**

A capital property must be available for use before 2014 in order for a capital expenditure for that property to be included in the pool of deductible SR&ED (scientific research and experimental development) expenditures.

Generally, a property is considered to become available for use, for inclusion in the pool of deductible SR&ED (scientific research and experimental development) expenditures and for ITC (investment tax credit) purposes as determined by the available for use rules concerning depreciable property.

Generally, an SR&ED (scientific research and experimental development) capital property is considered to become available for use at the earliest of:

- the time at which the property is first used by the claimant, for the purpose of earning income. For the purpose of determining when a property is first used, SR&ED (scientific research and experimental



development) activities are considered to be for the purpose of earning income.

or

- the time the property is delivered or is made available to the claimant or to another person (or partnership) that will use the property for the benefit of the claimant, **and** is capable of producing or performing a commercially saleable **product or service**. **Product or service** includes an intermediate product or service that is, or will be, used or consumed by or for the benefit of the claimant or the other person (or partnership) in producing or performing any such product or service.

#### **Legislative References *Income Tax Act***

Subsections 13(26) to (32) Available for use

Subsection 37(1.2) Available for use

Subsection 127(11.2) Time of an expenditure and acquisition

Subsection 248(19) When property available for use

## **4.0 Terms**

### **4.1 All or substantially all**

All or substantially all (ASA (all or substantially all)) is generally accepted to mean 90% or more. Generally, where an expenditure is ASA (all or substantially all), the total amount of the expenditure is deductible.

For SR&ED (scientific research and experimental development) capital property, the ASA (all or substantially all) test will be met where it is determined that, the property's anticipated use for other purposes during its operating time in its expected useful life does not exceed 10%, or if it is intended that not less than 90% of the value of the property is to be

consumed in the prosecution of SR&ED (scientific research and experimental development) carried on in Canada (see sections 3.2.1 and 3.2.2).

The ASA (all or substantially all) test for SR&ED (scientific research and experimental development) capital property is based on intent as opposed to actual use even though the CRA (Canada Revenue Agency) may look at subsequent use to evaluate intent (see section 6.0).

### **Legislative References *Income Tax Act***

Subsection 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

Subclause 37(8)(a)(ii)(A)(III) SR&ED (scientific research and experimental development) expenditures in Canada under the traditional method – ASA (all or substantially all) capital expenditures [Repealed]

Subclause 37(8)(a)(ii)(B)(III) SR&ED (scientific research and experimental development) expenditures in Canada under the proxy method – ASA (all or substantially all) capital expenditures [Repealed]

## **4.2 Operating time**

SR&ED (scientific research and experimental development) use of SR&ED (scientific research and experimental development) capital property should be determined as a percentage of the total operating time on an annual basis. The term **operating time** is not defined in the *Income Tax Act* but generally means the time the equipment usually runs or functions during the tax year.

Time spent to set up equipment for SR&ED (scientific research and experimental development) activities and time spent to switch the equipment back to another use will usually be considered to be operating time in which the equipment is used for the prosecution of SR&ED

(scientific research and experimental development) carried on in Canada, as long as it is reasonable in the circumstances. The time that the machine is idle is not included in the calculation (is not considered operating time).

Whether equipment is used for the prosecution of SR&ED (scientific research and experimental development) carried on in Canada during its operating time is a question of fact that can only be determined on a case-by-case basis. The onus is on the claimant to maintain documentation, such as a logbook, which would support the SR&ED (scientific research and experimental development) use of the equipment for the period (see section 11.0).

### 4.3 General purpose office equipment or furniture

General purpose office equipment or furniture (GPOEF (general purpose office equipment or furniture)) includes all furniture, such as desks, chairs, lamps, filing cabinets, and bookshelves. It also includes photocopiers, fax machines, telephones, pagers, typewriters, word processors, teletypes and calculators.

Computers, including hardware, software, and ancillary equipment, are **not** considered to be general purpose office equipment or furniture.

The only difference in determining SR&ED (scientific research and experimental development) capital expenditures under the traditional method and the proxy method for expenditures made before 2014, is that expenditures for general purpose office equipment or furniture (GPOEF (general purpose office equipment or furniture)), must be excluded where the proxy method is used. If a claimant uses the proxy method, outlays to acquire GPOEF (general purpose office equipment or furniture) are included in a prescribed class and are eligible for capital cost allowance (CCA (capital cost allowance)) (see section 5.1) at the prescribed rate.

GPOEF (general purpose office equipment or furniture) is excluded from the definitions of first and second term shared-use-equipment. For more information, please refer to the SR&ED (scientific research and experimental development) Shared-Use-Equipment Policy.

### **Legislative References *Income Tax Act***

Paragraph 20(1)(a) Deduction for capital cost of a property

Paragraph 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

Subclause 37(8)(a)(ii)(B)(III) SR&ED (scientific research and experimental development) expenditures in Canada under the proxy method – ASA (all or substantially all) capital expenditures [Repealed]

## **5.0 Depreciable property**

Depreciable property is any property that has an expected useful life and / or benefit of more than 12 months and on which the claimant has claimed or would be allowed to claim capital cost allowance (CCA (capital cost allowance)) (see section 5.1). The cost of this property (see section 5.2) is amortized over a number of tax years.

Only expenditures made before 2014 that result in the acquisition of new or used depreciable property, other than a building or a leasehold interest in a building are eligible for inclusion in the pool of deductible SR&ED (scientific research and experimental development) expenditures. Consequently, expenditures for the acquisition of non-depreciable property (including land, a leasehold interest in land, property described in the claimant's inventory, or eligible capital property) cannot be included in the pool of deductible SR&ED (scientific research and experimental development) expenditures (see section 7.1).

Additional comments in Income Tax Folio S3-F4-C1, General Discussion of Capital Cost Allowance, may also be of assistance in determining whether a particular property is depreciable property.

### **Legislative References *Income Tax Act***

Subsection 13(21) Definition of “depreciable property”

Paragraph 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

Former subparagraph 37(8)(d)(i) SR&ED (scientific research and experimental development) expenditures specifically excluded – building and leasehold interest

## **5.1 Capital cost allowance**

A claimant may acquire a depreciable property, such as equipment, to use in its business or professional activities. The cost of the property cannot be deducted when calculating net business income for the tax year. However, since these properties wear out or become obsolete over time, their cost can be deducted over a number of years. For income tax purposes this deduction is called **capital cost allowance** (CCA (capital cost allowance)). Generally, the **undepreciated capital cost** (UCC (undepreciated capital cost)) is the balance left after CCA (capital cost allowance) is deducted from the capital cost of a depreciable property. As stated in section 3.2.4 an SR&ED (scientific research and experimental development) capital expenditure deducted by the claimant in determining their income for tax purposes in the year will be deemed to be an amount that has been allowed to the claimant as CCA (capital cost allowance).

SR&ED (scientific research and experimental development) capital expenditures may be claimed only for property owned (see section 5.1.1) by the claimant or property in which the claimant has a leasehold interest.

**Legislative References *Income Tax Act***

Subsection 13(21) Definition of "undepreciated capital cost"

Paragraph 20(1)(a) Deduction for capital cost of a property

Paragraph 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

Subsection 37(6) Expenditures of a capital nature

**Legislative References *Income Tax Regulations***

Part XI Capital cost allowances

Schedules II to VI Capital cost allowance schedules

**5.1.1 Ownership of capital property**

SR&ED (scientific research and experimental development) capital expenditures made after 2013 cannot be claimed. SR&ED (scientific research and experimental development) capital expenditures are limited to the acquisition of depreciable property. Depreciable property is any property in which CCA (capital cost allowance) can be claimed. CCA (capital cost allowance) may be claimed only for property owned or deemed to be owned (see section 5.1.3) by the claimant or property in which the claimant has a leasehold interest. Thus, in order to claim an allowable SR&ED (scientific research and experimental development) capital expenditure, the expenditure for the SR&ED (scientific research and experimental development) capital property must result in the claimant owning, or obtaining a leasehold interest in, the SR&ED (scientific research and experimental development) capital property. See section 7.2 for a discussion of the acquisition of buildings or leasehold interest in buildings which are not allowed as SR&ED (scientific research and experimental development) capital expenditures.

Where a claimant acquires a capital property, ownership of the capital property will be obtained either at the time the cost was incurred or at a later date. It is a question of fact whether or not a claimant owns or has a leasehold interest in an SR&ED (scientific research and experimental development) capital property.

A claimant who acquires or holds property as an agent or nominee for another cannot claim the property as an SR&ED (scientific research and experimental development) capital property (and cannot claim CCA (capital cost allowance) on such property).

In computing the income of a partnership, the *Income Tax Act* requires that partnership property (including SR&ED (scientific research and experimental development) capital property) be accounted for as if it were owned at the partnership level. For more information, please refer to the SR&ED (scientific research and experimental development) Claims for Partnerships Policy.

#### **Legislative References *Income Tax Act***

Paragraph 20(1)(a) Deduction for capital cost of a property

Paragraph 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

Subsection 96(1) Partnerships – general rules

#### **Legislative Reference *Income Tax Regulations***

Subsection 1102(1a) Partnership property

### **5.1.2 No ownership of capital property**

There may be circumstances in which neither a freehold nor a leasehold interest in capital property is acquired. In these circumstances CCA (capital cost allowance) cannot be claimed in respect of such capital property. For example, if a claimant constructs and incurs the cost to build a structure on

land owned by another person (or otherwise incorporates capital property into property owned by another as an integral part thereof) and does not have a leasehold interest in or ownership of the structure (or capital property), CCA (capital cost allowance) may not be claimed in respect of the structure (or capital property). Since CCA (capital cost allowance) could not otherwise be claimed for this type of property, it would not be depreciable property. Consequently, expenditures for this type of property would not be allowed as an SR&ED (scientific research and experimental development) capital expenditure.

### **Legislative References *Income Tax Act***

Paragraph 20(1)(a) Deduction for capital cost of a property

Paragraph 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

### **5.1.3 Deemed ownership of leased property**

When a lessor acquires new capital property that has yet to be leased and then jointly elects with its first lessee of the capital property under section 16.1 of the Act, the capital property will not be considered to have been used or acquired for use or lease for any purpose whatever before the lessee is deemed to have acquired the property.

Example:

A claimant leases a property from an arm's length party for a period exceeding one year and they jointly make an election under section 16.1 of the Act. The claimant is deemed to have acquired the property at its fair market value and borrowed an equal amount from the lessor. The lease payments are deemed to be blended payments of principal and interest.



The expenditure would not be considered to be **prescribed** (not allowed, see section 8.1) where the lessor acquires new property, which has yet to be leased, and then elects with the first lessee (the claimant) under section 16.1 of the Act.

The treatment of this transaction for ~~SR&ED (scientific research and experimental development)~~ purposes is the same as for any other acquisition of property. The property must still meet the intent criteria (see section 6.0) and the all or substantially all (~~ASA (all or substantially all)~~) criteria (see sections 3.2.1 and 3.2.2) in order to be allowable as an ~~SR&ED (scientific research and experimental development)~~ capital expenditure. ~~SR&ED (scientific research and experimental development)~~ capital expenditure made after 2013 cannot be claimed.

### **Legislative References *Income Tax Act***

Section 16.1 Leasing properties

Paragraph 37(1)(b) Pool of deductible ~~SR&ED (scientific research and experimental development)~~ expenditures – capital expenditures [Repealed]

Subclause 37(8)(a)(ii)(A)(III) ~~SR&ED (scientific research and experimental development)~~ expenditures in Canada under the traditional method – ~~ASA (all or substantially all)~~ capital expenditures [Repealed]

Subclause 37(8)(a)(ii)(B)(III) ~~SR&ED (scientific research and experimental development)~~ expenditures in Canada under the proxy method – ~~ASA (all or substantially all)~~ capital expenditures [Repealed]

## **5.2 Capital cost of property**

These rules are used to determine the amount of ~~SR&ED (scientific research and experimental development)~~ capital expenditures made before 2014 that may be included in the pool of deductible ~~SR&ED (scientific research and experimental development)~~ expenditures.

When referring to depreciable property (see section 5.0) the term "capital cost of property" generally means the full cost to the claimant of acquiring the property and includes:

- the purchase price;
- legal, accounting, engineering, installation, and other fees that relate to the buying or construction of the property (not including the part that applies to land);
- custom and excise duties, transportation and other acquisition costs, and when they are significant, storage costs;
- the cost of any additions or improvements made to the property after it was acquired, provided these costs were not claimed as a current expense; and
- in the case of a property a claimant manufactures for its own use, it includes material, labour, and overhead costs reasonably attributable to the property, but does not include any profit that might have been earned had the property been sold.

### **Legislative References *Income Tax Act***

Paragraph 20(1)(a) Deduction for capital cost of a property

Paragraph 37(1)(b) Pool of deductible ~~SR&ED (scientific research and experimental development)~~ expenditures – capital expenditures [Repealed]

### **Legislative Reference *Income Tax Regulations***

Part XI Capital cost allowances

## **6.0 Intent**

The sections 6.0 to 6.8 are only relevant if the capital property was acquired and available for use before 2014.

It is recognized that the determination of intent can be difficult, particularly because the determination of whether a capital property is intended to be used all or substantially all (~~ASA (all or substantially all)~~) (see section 4.1) of its operating time (see section 4.2) in its expected useful life in the prosecution of ~~SR&ED (scientific research and experimental development)~~ carried on in Canada is made at the time the property is acquired. In making this determination, the intended use of the property in the year in which the expenditure was made to acquire the property as well as over its expected useful life must be considered.

Subsequent use of the property may provide evidence of the claimant's intent at the time the expenditure was made. However, when the subsequent use is contrary to the claimant's stated intent, it is the claimant's responsibility to support their contention that the property was intended to be used ~~ASA (all or substantially all)~~ of its operating time in its expected useful life in the prosecution of ~~SR&ED (scientific research and experimental development)~~ carried on in Canada.

The determination of intent is usually a joint decision that will be made by the Financial Reviewer and Research and Technology Advisor based on all the circumstances related to the acquisition of the capital property. A Research and Technology Advisor who knows the industry and its practices can help to clarify how the property is used in the claimant's project and if the property can be used commercially. Therefore, representations provided by the claimant may assist in determining that the intent test was met.

There is neither a unique test nor exacting jurisprudence that can be fully utilized in establishing the intent of a claimant in regards to the acquisition of a capital property. If after reviewing a claimant's representation it is still unclear whether the intent test has been met or not, the following eight

factors may be considered and should be helpful in reaching a decision. While these factors may be useful in the decision-making process they are not in themselves conclusive evidence of intent:

- reason for purchase;
- potential use of property;
- actual use of property;
- type of SR&ED (scientific research and experimental development) ;
- SR&ED (scientific research and experimental development) environment;
- length of SR&ED (scientific research and experimental development) project;
- claimant's past practices; and
- planning documents.

The list of factors is not exhaustive and intent can only be determined after examining all the relevant facts.

In cases where property acquired with the intent of using it ~~ASA (all or substantially all)~~ in ~~SR&ED (scientific research and experimental development)~~ was later used in commercial activities or was sold, the recapture rules for ITCs (investment tax credit) may be applicable. For more information, please refer to the Recapture of SR&ED (scientific research and experimental development) Investment Tax Credit Policy.

### **Legislative References *Income Tax Act***

Subclause 37(8)(a)(ii)(A)(III) ~~SR&ED (scientific research and experimental development)~~ expenditures in Canada under the traditional method – ~~ASA (all or substantially all)~~ capital expenditures [Repealed]

Subclause 37(8)(a)(ii)(B)(III) ~~SR&ED (scientific research and experimental development)~~ expenditures in Canada under the proxy method – ~~ASA (all or substantially all)~~ capital expenditures [Repealed]

## 6.1 Reason for purchase

The determination as to whether capital property is intended to be used ASA (all or substantially all) (see section 4.1) of its operating time (see section 4.2) in its expected useful life in the prosecution of SR&ED (scientific research and experimental development) carried on in Canada, or whether ASA (all or substantially all) of its value would be consumed in the prosecution of SR&ED (scientific research and experimental development) carried in Canada is made at the time the property is acquired. To determine the intent of a claimant it is necessary to look at all the reasons for the purchase at the time the property was acquired.

## 6.2 Potential use of property

To determine if an acquisition of property meets the intent test it is necessary to consider the potential use of the property. The intent test will normally not be met where property is acquired for both SR&ED (scientific research and experimental development) and commercial purposes. To establish whether or not a property may have a dual purpose, it is necessary to determine if the claimant uses similar property for commercial purposes in its business.

Property that does not lend itself to activities other than SR&ED (scientific research and experimental development) is likely to meet the intent test. However, where similar property is used for commercial purposes the claimant has to demonstrate that their intent is to use that particular property ASA (all or substantially all) for SR&ED (scientific research and experimental development).

## 6.3 Actual use of property

The actual use of property should in most cases confirm a claimant's intent. However, while the subsequent use of property may provide evidence of the claimant's intent at the time the property was acquired, it is not conclusive evidence of intent.

The SR&ED (scientific research and experimental development) legislation provides for an intent test as opposed to a use test. Therefore, the actual use of a property is only one factor that needs to be considered when determining the intent of a claimant. In some cases, the intent test may still be met where, due to a significant and unforeseeable change in circumstances, a property acquired with the intent of being used ASA (all or substantially all) (see section 4.1) in SR&ED (scientific research and experimental development) was later used for other activities.

## 6.4 Type of SR&ED (scientific research and experimental development)

Where the SR&ED (scientific research and experimental development) involves the construction of a custom product or commercial asset it is necessary to determine whether the property is an instrument to facilitate SR&ED (scientific research and experimental development) or whether it is an integral part of the end product. Where it is intended that property will become part of a custom product or commercial asset, the expenditure to acquire that property will not generally be allowed for SR&ED (scientific research and experimental development) purposes.

In some SR&ED (scientific research and experimental development) projects, property may be destroyed or rendered valueless through the SR&ED (scientific research and experimental development) process. A claimant has to show that at the time the property was acquired, the

claimant intended to destroy or cause the property to be rendered valueless through the SR&ED (scientific research and experimental development) process.

The intent test will not be met, if due to unforeseen circumstances, a property acquired with the intent of being used in commercial activities is destroyed or rendered valueless during the prosecution of SR&ED (scientific research and experimental development) carried on in Canada. In such a case the claimant may be entitled to ITC (investment tax credit) if the property is considered to be shared-use-equipment. For more information, please refer to the SR&ED (scientific research and experimental development) Shared-Use-Equipment Policy.

## **6.5 SR&ED (scientific research and experimental development) environment**

The environment in which SR&ED (scientific research and experimental development) is undertaken will sometimes assist in determining whether a property meets the intent test. Generally, the intent test would be met where property is acquired for use in the prosecution of SR&ED (scientific research and experimental development) carried on in Canada and the claimant is a dedicated SR&ED (scientific research and experimental development) corporation or division. However, where the proxy method is used, the cost of general purpose office equipment or furniture (see section 4.3) cannot be claimed as a capital expenditure for SR&ED (scientific research and experimental development) (see section 3.2).

In addition, there is some indication, though not conclusive, that the intent test would be met where a property is acquired by a start-up SR&ED (scientific research and experimental development) corporation or by a large corporation with a dedicated SR&ED (scientific research and

experimental development) facility. In these cases, additional factors such as the reason for purchase and potential use of the property may have to be considered in determining whether the intent test has been met.

## **6.6 Length of SR&ED (scientific research and experimental development) project**

The length of an SR&ED (scientific research and experimental development) project will vary depending on the type of research being undertaken. In determining whether the intent test has been met it is necessary to take into consideration the length of a research project as compared to the expected useful life of the property.

For a capital expenditure to be allowable for SR&ED (scientific research and experimental development) purposes, a claimant must intend to use the property during ASA (all or substantially all) (see section 4.1) of its operating time (see section 4.2) in its expected useful life for the prosecution of SR&ED (scientific research and experimental development) carried on in Canada. If a claimant intends to use capital property to carry on SR&ED (scientific research and experimental development) over a short period of time, the intent test would not generally be met where this period is less than the expected useful life of the capital property. However, in making this determination the intended use of the property for SR&ED (scientific research and experimental development) purposes throughout its useful life should also be considered.

The cost of a capital property may also qualify as an SR&ED (scientific research and experimental development) capital expenditure where it is intended that ASA (all or substantially all) of the value of the property would be consumed in the prosecution of SR&ED (scientific research and experimental development) carried on in Canada. Where it is intended that ASA (all or substantially all) of the value of the property would be



consumed in the prosecution of SR&ED (scientific research and experimental development) carried on in Canada because technology is changing rapidly or because a property is actually destroyed in the SR&ED (scientific research and experimental development) process, the length of the SR&ED (scientific research and experimental development) project may be irrelevant in determining whether the expenditure for this property is allowable as an SR&ED (scientific research and experimental development) capital expenditure.

## 6.7 Claimants past practices

A claimant's past practices may be relevant in determining whether the intent test has been met if the claimant acquired similar property in a previous year. If an SR&ED (scientific research and experimental development) project is carried on over a number of years, how the capital property was treated in a previous year could be a factor in determining the intent of the claimant. If the cost of property was allowed as an SR&ED (scientific research and experimental development) capital expenditure in a previous year and if similar property is acquired for SR&ED (scientific research and experimental development) in the current year, the CRA (Canada Revenue Agency) would generally expect the similar property to be treated in a consistent manner in the current year.

While a claimant's past practice is an indicator of intent, this factor alone is not conclusive evidence of intent. In cases where there has been a shift in business from SR&ED (scientific research and experimental development) to commercial activities, the claimant's past practices may not be relevant in determining the intent of a claimant.

## 6.8 Planning documents

In some industries, where significant amounts are spent on SR&ED (scientific research and experimental development) work and on capital property in particular, there generally are planning documents relating to an SR&ED (scientific research and experimental development) project. Planning documents that describe the use of capital property such as a project plan, a business case, or any other document that is a request to secure funding for a research project could be helpful in determining whether the intent test was met.

Planning documents will generally contain contingencies for the eventual use of capital property in the event that a research projects fails or for when the research project is completed. Generally, one of these contingencies is that capital property will be used in the commercial activities of the business.

The SR&ED (scientific research and experimental development) work, carried on by a claimant, is performed within the overall business environment of that claimant. From a business perspective, it is important to have contingency plans in order to remain competitive and sustain a viable business operation. Planning documents must be viewed within the context of the business operation. As a result, it is necessary to place more emphasis on the claimant's intended use of property in the SR&ED (scientific research and experimental development) environment and less emphasis on the contingent use of property in a larger business context.

## 7.0 Expenditures not allowed as SR&ED (scientific research and experimental

# development) capital expenditures

For expenditure made before 2014, expenditures for non-depreciable property, buildings (other than a special-purpose building, see [Appendix A](#)), and expenditures of a capital nature that pertain to SR&ED (scientific research and experimental development) carried on outside Canada **are not deductible** as SR&ED (scientific research and experimental development) capital expenditures. Capital expenditures made after 2013, no longer qualify for SR&ED (scientific research and experimental development) tax incentives, see [sections 3.1 to 3.1.2](#).

## 7.1 Non-depreciable property

As discussed in [section 3.2](#), only expenditures incurred before 2014 that result in the acquisition of depreciable property (other than a building or a leasehold interest in a building, see [section 7.2](#)) are eligible for inclusion in the pool of deductible SR&ED (scientific research and experimental development) expenditures, if they meet the definition of SR&ED (scientific research and experimental development) capital expenditures.

Consequently, expenditures for the acquisition of non-depreciable property, such as, land or a leasehold interest in land, property described in the claimant's inventory, or eligible capital property (such as goodwill), cannot be included in the pool of deductible SR&ED (scientific research and experimental development) expenditures.

### Legislative References *Income Tax Act*

Subsection 13(21) Definition of "depreciable property"

Subparagraph 37(1)(b)(i) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

## **Legislative References *Income Tax Regulations***

Paragraph 1102(1)(b) Property not included in Schedule II – inventory

Subsection 1102(2) Property not included in Schedule II – land

Subsection 1102(5) Property not included in Schedule II – leasehold interest in land

## **7.2 Expenditures for buildings**

Capital expenditures made before 2014 that relate to the acquisition of a building (other than a special-purpose building prescribed by regulation, see [Appendix A](#)) including a leasehold interest in a building, do not constitute expenditures on, or in respect of, SR&ED (scientific research and experimental development). They cannot be included in the pool of deductible SR&ED (scientific research and experimental development) expenditures nor can they be included in qualified SR&ED (scientific research and experimental development) expenditures for ITC (investment tax credit) purposes. For more information on the exclusion of lease costs (rent) for a building, please refer to the SR&ED (scientific research and experimental development) Lease Expenditures Policy. Capital expenditures made after 2013, no longer qualify for SR&ED (scientific research and experimental development) tax incentives, see sections 3.1 to 3.1.2.

The purchase or rental of a structure or a portable shelter (see [section 7.2.1](#)) made before 2014 is not restricted and can be included in the pool of deductible SR&ED (scientific research and experimental development) expenditures if the definition of SR&ED (scientific research and experimental development) capital expenditures is met.

The comments in [Income Tax Folio S3-F4-C1, General Discussion of Capital Cost Allowance](#), may be of assistance in determining whether a particular property is depreciable property.

## Legislative References *Income Tax Act*

Paragraph 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

Former subparagraph 37(8)(d)(i) SR&ED (scientific research and experimental development) expenditures specifically excluded – building and leasehold interest

### 7.2.1 Meaning of "building"

**Building** is a broad term covering any structure with walls and a roof affording protection and shelter that is affixed to the land. For example, a mobile home would be considered a building if the wheels, the trailer hitch, brakes and emergency lights are removed and the unit is affixed to cement pads on the ground and services, such as hydro and water, are installed.

The term **structure** includes anything of substantial size that is built up from component parts and intended to remain permanently on a permanent foundation. This definition of "structure" was considered by the Supreme Court of Canada in *British Columbia Forest Products Ltd. (Limited) v. (versus) Minister of National Revenue* 71 DTC 5178, which also concluded that the term **structure** when used in the context of **building or other structure** does not mean only a structure in the nature of a building. Bridges or hydro-electric transmission towers, for example, while clearly not buildings, are structures.

**Portable shelters** such as housing, office, and other service units are regarded as buildings **if they are installed and intended to remain in a particular location**. Such things as tents, canvas marquees and air-supported fabric domes that are not part of a rigid structure are not considered to be buildings or structures.

Property that is **attached to a building**, however firmly, is included in capital cost allowance (CCA (capital cost allowance)) Class 8 if it is acquired exclusively for those purposes stated in CCA (capital cost allowance) Class 8. For example, concrete footings, foundations and structural steel exclusively for the support of machinery are regarded as CCA (capital cost allowance) Class 8 property. Stairs and platforms, the sole purpose of which is to provide access to machinery, also fall within CCA (capital cost allowance) Class 8, whether they are attached to the building or the machinery.

The comments in Interpretation Bulletin IT-79R3, Capital cost allowance – Buildings or other structures, may be of assistance in distinguishing between expenditures for the acquisition of buildings and expenditures for the acquisition of other structures.

#### **Legislative Reference *Income Tax Act***

Former paragraph 37(8)(d) SR&ED (scientific research and experimental development) expenditures specifically excluded

#### **Legislative References *Income Tax Regulations***

Subsection 1102(19) Additions and alterations

Schedule II Capital cost allowances

### **7.2.2 Exception – Third-party payments concerning buildings may be allowed**

A claimant's payment enabling the recipient to acquire a building, or a leasehold interest in a building cannot be included in the pool of deductible SR&ED (scientific research and experimental development) expenditures as a capital expenditure. These types of payments made before 2014 may be allowed as a third-party payment if one of the following conditions is met:

- the recipient of the payment is an approved research institute or an approved association, provided the claimant and the recipient deal at arm's length; or
- the recipient is an approved university, college or organization, provided that the payer does not acquire an interest in that building.

For more information, please refer to section 6.2 of the Third-Party Payments Policy.

### **Legislative Reference *Income Tax Act***

Former paragraph 37(8)(d) SR&ED (scientific research and experimental development) expenditures specifically excluded

## **7.3 Expenditures for capital property that is used outside Canada**

The SR&ED (scientific research and experimental development) Program is designed to encourage SR&ED (scientific research and experimental development) in Canada. The location of the SR&ED (scientific research and experimental development) activities will indicate whether the SR&ED (scientific research and experimental development) is carried on inside or outside Canada. If the activity is performed outside Canada, the SR&ED (scientific research and experimental development) is performed outside Canada.

Expenditures of a capital nature that pertain to SR&ED (scientific research and experimental development) carried on outside Canada are not included in the pool of deductible SR&ED (scientific research and experimental development) expenditures. These expenditures would be included on Schedule T2SCH8, Capital Cost Allowance and deducted in the normal manner.

However, expenditures of a capital nature made before 2014 for equipment acquired from outside Canada used in the prosecution of SR&ED (scientific research and experimental development) in Canada may be included in the pool of deductible SR&ED (scientific research and experimental development) expenditures provided all other requirements outlined in this policy are otherwise met.

### **Legislative References *Income Tax Act***

Paragraph 20(1)(a) Deduction for capital cost of property

Paragraph 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

Subsection 37(2) Research outside Canada

## **8.0 SR&ED (scientific research and experimental development) capital expenditures that are not allowed as qualified SR&ED (scientific research and experimental development) expenditures**

Not all expenditures for SR&ED (scientific research and experimental development) carried on in Canada will earn an ITC (investment tax credit). The following sections discuss SR&ED (scientific research and experimental development) capital expenditures (see section 3.2) that are not allowed as qualified SR&ED (scientific research and experimental development) expenditures for ITC (investment tax credit) purposes.



## 8.1 SR&ED (scientific research and experimental development) capital expenditures prescribed by the *Income Tax Regulations*

The following explains prescribed expenditures in relation to expenditures of a capital nature incurred after 2013, and prescribed expenditures of a capital nature incurred before 2014.

After 2013:

Prescribed expenditures incurred after 2013 are expenditures that are incurred in respect of:

- the acquisition of property that is qualified property (see below) as defined in the *Income Tax Act*; and
- the acquisition of property that has been used or acquired for use or lease or for any purpose before it was acquired by the claimant (see section 8.1.1).

The expenditures for the property described above are generally not expenditures of a current nature (see section 3.1.1). Prescribed expenditures are excluded from the definition of qualified SR&ED (scientific research and experimental development) expenditures.

Before 2014:

Prescribed expenditures of a **capital** nature incurred before 2014 are expenditures that are incurred in respect of:

- the acquisition of qualified property (see below), or
- the acquisition of property that has been **used or acquired for use or lease or for any purpose** before it was acquired by the claimant (see section 8.1.1).

Prescribed expenditures are excluded from the definition of **qualified expenditures**. Consequently, an expenditure for SR&ED (scientific research and experimental development) capital property made before 2014 that may be allowed in the pool of deductible SR&ED (scientific research and experimental development) expenditures (see section 3.2) will not be a qualified SR&ED (scientific research and experimental development) expenditure if it is prescribed.

Qualified property is defined in the Act and earns investment tax credits (ITCs (investment tax credits)) apart from those earned under the SR&ED (scientific research and experimental development) Program. ITC (investment tax credit)s are prevented from being earned twice in respect of a property that is both qualified property and a qualified expenditure for SR&ED (scientific research and experimental development) carried on in Canada.

### **Legislative References *Income Tax Act***

Subsection 37(1) Pool of deductible SR&ED (scientific research and experimental development) expenditures

Subclause 37(8)(a)(ii)(A)(III) SR&ED (scientific research and experimental development) expenditures in Canada under the traditional method – ASA (all or substantially all) capital expenditures [Repealed]

Subclause 37(8)(a)(ii)(B)(III) SR&ED (scientific research and experimental development) expenditures in Canada under the proxy method – ASA (all or substantially all) capital expenditures [Repealed]

Subsection 127(9) Definition of "first term shared-use-equipment"

Subsection 127(9) Definition of "second term shared-use-equipment"

Subsection 127(9) Definition of "qualified expenditure"

Subsection 127(9) Definition of "qualified property"

## **Legislative Reference *Income Tax Regulations***

Paragraph 2902(b) Prescribed expenditures for purposes of qualified expenditures

Former paragraph 2902(b) Prescribed capital expenditures for purposes of qualified expenditures

### **8.1.1 Acquisition of used property**

After 2013:

Expenditures for capital property incurred after 2013 do not qualify for SR&ED (scientific research and experimental development) tax incentives. Since the rules for prescribed expenditures for used property incurred after 2013 are not generally applicable to expenditures of a current nature (see section 8.1), they will generally not be applicable to expenditures incurred after 2013.

Before 2014:

Expenditures for capital property incurred before 2014 that was used or acquired for use or lease or for any purpose whatsoever before the claimant acquired it are prescribed expenditures. An expenditure made before 2014 for capital property that was used or leased before the claimant acquired it is allowed as an SR&ED (scientific research and experimental development) capital expenditure but does not entitle the claimant to an ITC (investment tax credit).

To be considered not to have been used, the property must not only be new when the claimant acquired it, but it must not have been acquired for use or lease or for any purpose whatever by any previous owner. As a result of these requirements, if a property that has been used or was acquired for a use (even though unused) is transferred to a new owner, eligibility for the

ITC (investment tax credit) is not transferable. For a specific exception regarding leased property where an election under section 16.1 of the Act has been made, see section 5.1.3.

The cost to acquire a piece of equipment that is used regularly for demonstration purposes is considered to be a prescribed expenditure. However, new equipment that is demonstrated for or tested by a prospective purchaser of that particular piece of equipment would not normally be considered to have been used for a purpose.

### **Legislative Reference *Income Tax Act***

Subsection 127(9) Definition of "qualified expenditure"

### **Legislative Reference *Income Tax Regulations***

Paragraph 2902(b) Prescribed expenditures for purposes of qualified expenditures

Former paragraph 2902(b) Prescribed capital expenditures for purposes of qualified expenditures

## **8.1.2 Refurbishment of used property**

Significant refurbishments to a claimant's SR&ED (scientific research and experimental development) capital property before 2014 ("the equipment") will normally be an allowable SR&ED (scientific research and experimental development) capital expenditure providing the refurbished equipment continues to satisfy all other SR&ED (scientific research and experimental development) eligibility conditions (see section 3.2).

Where used equipment is refurbished by a **vendor** and those refurbishments are so significant that the equipment, when acquired by a claimant can be said to be new, the expenditure for the equipment would qualify for the ITC (investment tax credit) as a capital expenditure, provided that all other eligibility requirements are met. However, where, subsequent to the acquisition of used equipment, a **claimant** carries out significant

refurbishments only the costs of the refurbishments may qualify as an SR&ED (scientific research and experimental development) capital expenditure.

Based on the ordinary meaning of the word "significant" and the phrase "when acquired by the claimant, can be said to be new," the refurbishments should go beyond the simple replacement of worn parts to the point where the refurbishments bring the equipment to the current state of the art (a new state). Refurbishments that are merely performance related enhancements that do not change the essential nature of the equipment would not qualify as new.

It would be a question of fact whether particular refurbishments would bring the equipment to a new state such that the same useful life will be produced as newly manufactured equipment. The following are factors to consider when determining if particular refurbishments would bring a piece of equipment to a new state:

- a considerable number of parts of the equipment, compared to the total number of parts comprising the equipment as a whole that have been replaced with new parts or parts that have been rebuilt as new (such that the same useful life will be produced as a newly manufactured equipment);
- a number of major parts of the equipment, compared with other parts that are considered to be minor (in number, effect or importance) that have been replaced with new parts or parts that have been rebuilt as new (such that the same useful life will be produced as a newly manufactured equipment).

The list of factors is not exhaustive and whether particular refurbishments would bring a piece of equipment to a new state can only be determined after examining all the relevant facts.

## **8.2 Expenditures for purchases of SR&ED (scientific research and experimental development) capital property from non-arm's length parties**

When the claimant purchases goods or services (other than SR&ED (scientific research and experimental development) contracts) from a person or partnership with whom they do not deal at arm's length at the time of the transaction, the allowable amount of the qualified SR&ED (scientific research and experimental development) expenditure for ITC (investment tax credit) purposes is limited to the cost to the non-arm's length (NAL (non-arm's-length)) person of providing the goods or services.

In the case of a property sold to the claimant by a non-arm's length supplier, the eligible amount of qualified SR&ED (scientific research and experimental development) expenditure for ITC (investment tax credit) purposes is limited to either the capital cost of the property (see section 5.2) to the claimant or the adjusted selling cost of the property to the supplier, whichever amount is less.

Determining adjusted selling cost involves tracing the costs incurred by non-arm's length parties in providing a property. The cost to the party performing the SR&ED (scientific research and experimental development) will be the cost paid for by the NAL (non-arm's-length) party who acquired the property at arm's length. There will be no inter-company profit included in the cost of the property to the performer.

For more information on non-arm's length situations, please refer to the Total Qualified SR&ED (scientific research and experimental development) Expenditures for Investment Tax Credit Purposes Policy. The Income tax folio, S1-F5-C1, Related persons and dealing at arm's length, describes in general terms the criteria for determining whether persons deal with each other at arm's length.

## 9.0 Sale of SR&ED (scientific research and experimental development) capital property or change in use of SR&ED (scientific research and experimental development) capital property

### 9.1 Recapture of capital cost allowance for claimed and unclaimed SR&ED (scientific research and experimental development) capital expenditures

A disposition of depreciable property (sale of SR&ED (scientific research and experimental development) capital property) is subject to the provisions of the *Income Tax Act* dealing with capital cost allowance (CCA (capital cost allowance)) recapture and capital gains and losses. Where any depreciable property (see section 5.0) is disposed of for proceeds in excess of the capital cost of the property (see section 5.2) to the claimant, that disposition may give rise to a capital gain. However, any loss on the disposition of depreciable property is specifically excluded from a claimant's capital loss and, as a result, no deduction is permitted for such losses.

There may be circumstances where the claimant sold SR&ED (scientific research and experimental development) capital property during the year, but there are unclaimed expenditures for the SR&ED (scientific research and experimental development) capital property in the pool of deductible SR&ED (scientific research and experimental development) expenditures at the end of the year. Effectively these unclaimed expenditures represent the unclaimed CCA (capital cost allowance) (deduction) (see section 3.2.4) of the SR&ED (scientific research and experimental development) capital property.

A proportion of the proceeds of disposition for the SR&ED (scientific research and experimental development) capital property that is sold may be allocated to the **unclaimed** expenditures for the SR&ED (scientific research and experimental development) capital property, which will reduce the claimant's pool of deductible SR&ED (scientific research and experimental development) expenditures. Generally, the sale proceeds **or** the amount of unclaimed expenditures for the capital property, whichever amount is less, would be included in the pool of deductible SR&ED (scientific research and experimental development) expenditures.

A proportion of the proceeds of disposition for the SR&ED (scientific research and experimental development) capital property that is sold may be allocated to the (previously) **claimed** expenditures for the SR&ED (scientific research and experimental development) capital property, which will be included in the claimant's income calculation as CCA (capital cost allowance) recapture.

### **Example:**

#### **Facts**

The undeducted SR&ED (scientific research and experimental development) expenditures balance carried forward from the prior year (line 450 of Form T661) is \$500. An SR&ED (scientific research and experimental development) capital property was sold during the year for \$100. Its original cost was \$1,000. The amount of unclaimed expenditures for the SR&ED (scientific research and experimental development) capital property included at line 450 of Form T661 is \$60.

#### **Solution:**



**Determine the amount at line 440 on Form T661**, whichever amount is the lesser of the proceeds of disposition (\$100) and the amount of unclaimed expenditures for the SR&ED (scientific research and experimental development) capital property (\$60). Line 440 amount on the Form T661: \$60.

If the sale proceeds are more than the unclaimed balance of SR&ED (scientific research and experimental development) expenditures for the capital property, the difference is generally included in income up to the amount of recapture of CCA (capital cost allowance) (the claimed deduction for the SR&ED (scientific research and experimental development) capital property). If the sale proceeds are more than the original cost of the capital property, the excess is either a capital gain or income, depending on the facts of each case.

**Determine the recaptured CCA (capital cost allowance)**, whichever amount is the lesser of the original cost (\$1,000) and the proceeds of disposition minus the line 440 amount on Form T661 ( $\$100 - \$60 = \$40$ ). The recapture of CCA (capital cost allowance) is \$40 (include this amount in income for the year).

Where **all** the expenditures for the SR&ED (scientific research and experimental development) capital property remain unclaimed in the previous year's pool balance of deductible SR&ED (scientific research and experimental development) expenditures reported at line 450 of Form T661, recapture with respect to SR&ED (scientific research and experimental development) capital expenditures will be reflected as a reduction to the pool of deductible SR&ED (scientific research and experimental development) expenditures. In this case, provided the proceeds are less than the capital cost of the property, which is normally the case, the proceeds can be entered at line 440 of Form T661. This

effectively removes the appropriate portion of unclaimed expenditures for the capital property included in the prior year balance of the pool of deductible SR&ED (scientific research and experimental development) expenditures. In the event the proceeds exceed the capital cost of the property to the claimant, the capital cost of the property should be recorded at line 440 of Form T661 and the excess reported as capital gain. If the pool balance of deductible SR&ED (scientific research and experimental development) expenditures at the end of the prior year is zero, the recapture should be reported on Schedule T2SCH1, Net Income (Loss) for Income Tax Purposes.

### **Legislative References *Income Tax Act***

Subsection 13(1) Recaptured depreciation

Subsection 13(7.1) Deemed capital cost of certain property

Subsection 13(21) Definition of “undepreciated capital cost”

Paragraph 20(1)(a) Deduction for capital cost of a property

Paragraph 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

Subsection 37(6) Expenditures of a capital nature

Subsection 39(1) Meaning of capital gain and capital loss

## **9.2 Recapture of SR&ED (scientific research and experimental development) investment tax credit**

When the claimant sells the SR&ED (scientific research and experimental development) capital property or converts it to commercial use, there may be recapture of ITC (investment tax credit) earned on SR&ED (scientific research and experimental development) expenditures for that property. These rules are in addition to the recapture of CCA (capital cost allowance) for claimed and unclaimed SR&ED (scientific research and experimental development) capital expenditures rules noted in section 9.1.

At the outset of an SR&ED (scientific research and experimental development) project, for equipment used for the prosecution of SR&ED (scientific research and experimental development) carried on in Canada, a claimant may intend to use the property in SR&ED (scientific research and experimental development) throughout its useful life, but subsequently change its use or dispose of it. The recapture rules are intended to reflect the net cost of performing SR&ED (scientific research and experimental development). Since this net cost cannot be determined at the outset, the recapture rules will reverse all or a portion of the ITC (investment tax credit) when the sale of the property takes place or when it is converted to commercial use.

For more information, please refer to the [Recapture of SR&ED \(scientific research and experimental development\) Investment Tax Credit Policy](#).

## **10.0 Related topics to SR&ED (scientific research and experimental development) capital expenditures**

### **10.1 Development of an asset**

If capital expenditures are incurred before 2014 in the development of an asset (such as prototype, pilot plant / commercial plant, custom product / commercial asset), the SR&ED (scientific research and experimental development) capital property acquired must be all or substantially all (ASA (all or substantially all)), attributable to the prosecution of SR&ED (scientific research and experimental development) carried on in Canada for the expenditures to be eligible SR&ED (scientific research and experimental development) expenditures. This would require that the capital property to which the expenditure relates:

- have minimal life expectancy (less than 10%) after its involvement in the development of the asset;
- have limited value (less than 10%) after its involvement in the development of the asset; or
- be used in the performance of other SR&ED (scientific research and experimental development) after its involvement in the development of the asset.

For more information, please refer to the SR&ED (scientific research and experimental development) while Developing an Asset Policy.

Capital expenditures incurred after 2013, no longer qualify for SR&ED (scientific research and experimental development) tax incentives.

## **10.2 Criteria in determining whether an expenditure is on account of capital or a current expense**

The following criteria, developed by the Courts, are to be considered in determining whether an expenditure is on account of capital or a current expense. The Courts have generally taken the position that there is no rigid test to be used to determine whether an outlay is capital in nature or a current expense and that it is very much a question of fact. The circumstances specific to each case will be determinative of the issue.

- enduring benefit
- maintenance or betterment
- integral part or separate property
- relative value
- acquisition of used property
- anticipation of sale

For more information on these factors, please refer to Income Tax Folio S3-F4-C1, General Discussion of Capital Cost Allowance.

## 10.3 Expenditures for software and software licenses before 2014 may be capital or current expenditures

Since SR&ED (scientific research and experimental development) expenditures cannot include expenditures for capital property or the use of, or the right to use capital property after 2013 (see section 3.1.1), **the following comments apply to expenditures for software incurred before 2014.**

Software and the rights or licenses to use computer and / or systems software fall within prescribed classes for capital cost allowance (CCA (capital cost allowance)) purposes. For example, definitions in the Regulations, in part, read:

"Computer software includes systems software and a right or licence to use computer software" and

"Systems software means... and includes a right or licence to use [systems software]..."

Software intended to be incorporated into a product cannot be included in the pool of deductible SR&ED (scientific research and experimental development) expenditures.

However, a deduction for an expenditure on something that is merely a tool for performing SR&ED (scientific research and experimental development) that will not be incorporated into a product created by a claimant may be included in the pool of deductible SR&ED (scientific research and experimental development) expenditures if it otherwise qualifies. An example would be software purchased for use as a tool in computer-aided design.

In determining whether the acquisition cost of software and software licences should be treated as a current expenditure or treated as a capital expenditure, the nature, purpose, and anticipated life of the computer software must be considered. If the acquisition would benefit only the current fiscal period the relevant cost would be considered a current expenditure. If the nature of the acquisition was of an enduring nature such that it would provide benefits beyond the current year, the acquisition should be considered capital in nature. Computer software is generally considered to have an "enduring nature" where its useful life is anticipated to last beyond one year.

In determining whether a particular expenditure is on account of capital (capital expenditure) or income (current expenditure) within the provisions of the *Income Tax Act*, the question to be answered is whether a payment or a legal obligation to pay was related to the acquisition of a depreciable property, (see section 5.0), or whether the payment was simply a current expenditure. When answering such a question, an expenditure is considered to have been made at the time a payment is made unless the claimant has entered into a legal obligation to make (a) future payment(s). The treatment of the payment or the debt giving rise to the legal obligation to pay must be determined at the time of payment or when a definite obligation to make the payment has been entered into.

In determining whether a payment can be considered a current expense in the form of a monthly payment or whether the individual payments or total obligation should be treated as a depreciable property (SR&ED (scientific research and experimental development) capital property), it is not the individual payments that have to be considered but rather the total obligation to pay in relation to that which was acquired.

For discussion purposes, assume that a user needs the use of computer software and has to make a choice between a fixed term five-year commitment and a short term month-to-month agreement for the right or licence to use computer software.

Where the fixed term five-year commitment is chosen the claimant has the option of paying the amount in full at the commencement of the agreement, or paying the amount in monthly instalments over the term of the agreement. Since the fixed term five-year commitment (total obligation in relation to what was acquired) fits the description of property of a prescribed class that is a depreciable property (SR&ED (scientific research and experimental development) capital property) the expenditures for such a commitment would be SR&ED (scientific research and experimental development) capital expenditures provided all other requirements outlined in this policy are otherwise met.

Where a short term non-guaranteed month-to-month agreement to use the same computer software is chosen, usually these agreements allow either party to terminate the agreement by giving the other one month's notice. Under agreements such as these, the month-to-month payments will normally only benefit the period in which they were made and will not benefit future periods. Therefore, the expenditures are considered to be a current expenditure and precluded from being depreciable property provided all other requirements concerning the current expenditure are otherwise met. When there is nothing to support or no reason to believe that these monthly payments will benefit future periods, there is no basis to capitalize these payments.

Therefore, it is the total of the entire obligation that has to be considered at the time of making the obligation to determine whether it is a current expense or whether it will accrue some benefit for a future year(s). In order

to be considered an amount in respect of depreciable property (right or license to use software), it is only necessary to establish that some part of the amount relates to use in a future year(s). In an agreement where there is no time guarantee for the use of the software and the payments are on a month to month basis with no time guarantee, the monthly payments in question can be considered to be current lease expenditures where it is reasonable to assume that the cost in respect to a future year(s) use is not being paid up front. Such current expenditures would be included on Form T661 as an SR&ED (scientific research and experimental development) lease expenditure.

### **Legislative References *Income Tax Act***

Paragraph 37(1)(a) Pool of deductible SR&ED (scientific research and experimental development) expenditures – current expenditures

Paragraph 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

### **Legislative References *Income Tax Regulations***

Paragraph 1102(1)(a) Items deducted from income deemed not to be on account of capital

Subsection 1104(2) Definition of "computer software"

Subsection 1104(2) Definition of "systems software"

## **10.4 Related current costs**

If an existing capital property (for example, equipment) is used temporarily for SR&ED (scientific research and experimental development), the costs (for example, maintenance and repairs) that would not have been incurred if the SR&ED (scientific research and experimental development) had not been carried out may be included as a current expenditure in calculating



the pool of deductible SR&ED (scientific research and experimental development) expenditures, when the claimant choose to use the traditional method.

Current expenditures (for example, foreign travel expenditures) for the acquisition of equipment from outside Canada that is used in the prosecution of SR&ED (scientific research and experimental development) in Canada may be included in the pool of deductible SR&ED (scientific research and experimental development) expenditures provided all other requirements are otherwise met.

For more information on these types of related current costs, please refer to the SR&ED (scientific research and experimental development) Overhead and Other Expenditures Policy.

### **Legislative References *Income Tax Act***

Paragraph 37(1)(a) Pool of deductible SR&ED (scientific research and experimental development) expenditures – current expenditures

Paragraph 37(1)(b) Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]

## **11.0 Documentation and other evidence**

It is recommended that the claimant keep a list of capital property they acquired prior to 2014 for the prosecution of SR&ED (scientific research and experimental development) carried on in Canada to support their claim for SR&ED (scientific research and experimental development) capital expenditures (see section 3.2). Claimants should be able to provide explanation and supporting evidence of how the capital expenditure was used in the prosecution of SR&ED (scientific research and experimental

development) carried on in Canada. Claimants should be able to provide enough information to establish the intended use of the equipment when it was acquired, as well as its actual use during its useful life.

In capturing plant (capital) costs, separate schedules should be maintained for the listing of all major equipment by name, specification, usage and actual purchase cost in addition to installation costs.

This information should be retained, ready to be provided upon request. For more information concerning documentation and other supporting evidence, please refer to Information Circular IC78-10R5, Books and Records Retention / Destruction and Keeping records.

## **11.1 Examples of documentation and other evidence**

Examples of documentation and other evidence that support SR&ED (scientific research and experimental development) capital expenditures are:

- logbooks or other documentation that support the SR&ED (scientific research and experimental development) use of equipment for the period;
- invoices, purchase contract, cancelled cheques, and so forth; and
- supporting schedules to reconcile capital expenditures on Schedule T2SCH8, Capital Cost Allowance, and Form T661 to the financial statements.

For further information on documentation, please refer to Appendix 2 of T4088, Guide to Form T661 Scientific Research and Experimental Development Expenditures (SR&ED (scientific Research and Experimental Development)) Claim.

# Appendix A – Special-purpose building

Special-purpose buildings are prescribed in the *Income Tax Regulations* (repealed after 2013) and are approved by the Department of Finance on a building-by-building basis. To date, only one type of building has been prescribed as a special-purpose building. Special-purpose buildings are the only **buildings** allowed as SR&ED (scientific research and experimental development) capital property.

A **special-purpose building** is a building the working areas of which are designed and constructed to have a displacement in any direction of not more than .02 micrometre and to have per .028 cubic metre of interior airspace:

- not more than 350 airborne particles of a size less than or equal to .1 micrometre in diameter and no airborne particles of a size greater than .1 micrometre in diameter;
- not more than 75 airborne particles of a size less than or equal to .2 micrometre in diameter and no airborne particles of a size greater than .2 micrometre in diameter;
- not more than 30 airborne particles of a size less than or equal to .3 micrometre in diameter and no airborne particles of a size greater than .3 micrometre in diameter; or
- not more than 10 airborne particles of a size less than or equal to .5 micrometre in diameter and no airborne particles of a size greater than .5 micrometre in diameter.

## **Legislative Reference *Income Tax Act***

Former paragraph 37(8)(d) Capital expenditures specifically excluded

## **Legislative Reference *Income Tax Regulations***

Section 2903 Special-purpose buildings [Repealed]

# Appendix B - Consolidated policy references

## Appendix B.1 Legislative references

### List of provisions

<b><i>Income Tax Act</i></b>	<b>Description</b>
Section 13	Rules concerning depreciable property
Subsection 13(1)	Recaptured depreciation
Subsection 13(7.1)	Deemed capital cost of certain property
Subsection 13(21)	Definition of "depreciable property"
Subsection 13(21)	Definition of "undepreciated capital cost"
Subsections 13(26) to (32)	Available for use
Section 16.1	Leasing properties
Paragraph 20(1)(a)	Deduction for capital cost of a property
Subsection 37(1)	Pool of deductible SR&ED (scientific research and experimental development) expenditures
Paragraph 37(1)(a)	Pool of deductible SR&ED (scientific research and experimental development) expenditures – current expenditures
Paragraph 37(1)(b)	Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]
Subparagraph 37(1)(b)(i)	Pool of deductible SR&ED (scientific research and experimental development) expenditures – capital expenditures [Repealed]
Subsection 37(1.2)	Available for use

<b>Income Tax Act</b>	<b>Description</b>
Subsection 37(2)	Research outside Canada
Subsection 37(6)	Expenditures of a capital nature
Subclause 37(8)(a)(ii)(A)(III)	<del>SR&amp;ED (scientific research and experimental development)</del> expenditures in Canada under the traditional method - <del>ASA (all or substantially all)</del> capital expenditures [Repealed]
Subclause 37(8)(a)(ii)(B)(III)	<del>SR&amp;ED (scientific research and experimental development)</del> expenditures in Canada under the proxy method - <del>ASA (all or substantially all)</del> capital expenditures [Repealed]
Paragraph 37(8)(d)	<del>SR&amp;ED (scientific research and experimental development)</del> expenditures specifically excluded
Former paragraph 37(8)(d)	<del>SR&amp;ED (scientific research and experimental development)</del> expenditures specifically excluded
Former subparagraph 37(8)(d)(i)	<del>SR&amp;ED (scientific research and experimental development)</del> expenditures specifically excluded – building and leasehold interest
Subparagraph 37(8)(d)(i)	<del>SR&amp;ED (scientific research and experimental development)</del> expenditures specifically excluded – building and leasehold interest
Subsection 37(11)	Filing requirement
Subsection 39(1)	Meaning of capital gain and capital loss
Section 54	Definition of “capital property”
Subsection 96(1)	Partnerships – general rules
Subsection 127(9)	Definition of "first term shared-use-equipment"
Subsection 127(9)	Definition of "qualified expenditure"
Subsection 127(9)	Definition of "qualified property"

<b><i>Income Tax Act</i></b>	<b>Description</b>
Subsection 127(9)	Definition of "second term shared-use-equipment"
Subsection 127(11.2)	Time of an expenditure and acquisition
Subsection 248(19)	When property available for use

## List of regulations

<b><i>Income Tax Regulations</i></b>	<b>Description</b>
Part XI	Capital cost allowances
Paragraph 1102(1)(a)	Items deducted from income deemed not to be on account of capital
Paragraph 1102(1)(b)	Property not included in Schedule II – inventory
Paragraph 1102(1)(d)	<del>SR&amp;ED (scientific research and experimental development)</del> deduction deemed not allowed for capital cost allowance
Subsection 1102(1a)	Partnership property
Subsection 1102(2)	Property not included in Schedule II – land
Subsection 1102(5)	Property not included in Schedule II – leasehold interest in land
Subsection 1102(19)	Additions and alterations
Subsection 1104(2)	Definition of "computer software"

**Income Tax****Regulations****Description**

Subsection 1104(2)	Definition of "systems software"
Paragraph 2902(b)	Prescribed expenditures for purposes of qualified expenditures
Former paragraph 2902(b)	Prescribed capital expenditures for purposes of qualified expenditures
Section 2903	Special-purpose buildings [Repealed]
Schedule II	Capital cost allowances
Schedules II to VI	Capital cost allowance schedules

**Appendix B.2 Jurisprudence****List of court cases****Case****number****Case name**

71 DTC 5178	<i>British Columbia Forest Products Ltd (Limited) v. (versus) Minister of National Revenue</i>
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**Appendix C – Revisions****C.1 Explanation of changes**

The following are the explanation of changes to the SR&ED (scientific research and experimental development) Capital Expenditures Policy as part of the revision of December 18, 2014:

Section 1.0 has been revised to delete the first sentence of the previous policy which mentioned that this policy document was a consolidation of the CRA (Canada Revenue Agency) publications.

New section 2.1 has been added to provide an overview for the legislative changes resulting from the federal 2012 budget, specifically that capital expenditures for SR&ED (scientific research and experimental development) are no longer allowed after 2013. As a result, former sections 2.1, 2.2, and 2.3 have been renumbered 2.2.1, 2.2.2, and 2.2.3 respectively.

New sections 3.1 – 3.1.2 have been added to explain the legislative changes resulting from the federal 2012 budget, specifically that capital expenditures for SR&ED (scientific research and experimental development) are no longer allowed after 2013. Explanations are also added for expenditures of a current nature, and the capital look-through rules concerning contract expenditures and third-party payments. As a result, former sections 3.1, 3.2, 3.3, 3.4 and 3.5 have been renumbered 3.2.1, 3.2.2, 3.2.3, 3.2.4, and 3.3 respectively.

Sections 8.1 and 8.1.1 have been revised to reflect the change in legislation for prescribed expenditures.

Section 10.3 has been revised to reflect the change in legislation as it pertains to expenditures for the use of or the right to use capital property and its effects on software and software licenses.

Appendix B.1 has been revised to update the legislative references.

Appendix B.3 "CRA (Canada Revenue Agency) publications" has been removed.

Legislative references have been updated throughout the document and wording throughout the document has been added to indicate capital expenditures no longer qualify for SR&ED (scientific research and



experimental development) tax incentives after 2013.

Other minor formatting and editing corrections were made throughout the document.

**Date modified:**

2014-12-18