Docket: 2010-3708(IT)G

BETWEEN:

CalAmp WIRELESS NETWORKS INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on April 15, 2013, at Montreal, Quebec

Before: The Honourable Justice Paul Bédard

Appearances:

Counsel for the Appellant:	Louis-Frédérick Côté
Counsel for the Respondent:	Simon Petit

JUDGMENT

The appeal from the assessment made under the *Income Tax Act* for the 2006 taxation year ending on May 9th, 2006 is dismissed in accordance with the attached Reasons for Judgment.

The parties will have until July 25, 2013 to arrive at an agreement on costs, failing which they are ordered to file their written submissions on costs no later than August 26, 2013. Such submissions are not to exceed five pages.

Signed at Ottawa, Canada, this 25th day of June 2013.

"Paul Bédard"

Bédard J.

Citation: 2013 TCC 201
Date: 20130625
Docket: 2010-3708(IT)G

BETWEEN:

CalAmp WIRELESS NETWORKS INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Bédard J.

[1] This is an appeal from an assessment made under the *Income Tax Act* (the "Act") for the 2006 taxation year. The issue is whether the Appellant is entitled to an investment tax credit ("ITC") in respect of bonuses paid to its employees engaged in scientific research and experimental development ("SR&ED").

[2] More specifically, by Notice of Assessment dated February 25th, 2009, the Minister of National Revenue (the "Minister") assessed the Appellant, with respect to the taxation year ending on May 9th, 2006, to reduce its initially claimed refundable ITC of $302,973 by an amount of $131,260 on the basis that the amount $1,990,036 (bonuses paid to its employees engaged in SR&ED) didn't constitute an expenditure of SR&ED directly undertaken by the Appellant and didn't constitute a qualified expenditure.

[3] In every other respect, this Notice of Assessment constituted a nil assessment.

[4] On May 19, 2009, the Appellant objected to the Minister's assessment of the taxation year ending on May 9, 2006.

[5] By Notice of Confirmation dated September 17, 2010, the Minister confirmed the assessment with respect to the taxation year ending on May 9, 2010.

[6] The total amount in issue in this appeal is $131,260.

The facts

[7] During the years prior to the month of May 2006, Dataradio Inc. ("Old Dataradio") was a corporation incorporated under the *Canada Business Corporations Act* and was headquartered in the Metropolitan Montreal, in the Province of Quebec.

[8] During the years prior to the month of May 2006, Old Dataradio was a Canadian-controlled private corporation.

[9] Old Dataradio's line of business consisted in the designing, manufacturing, marketing and selling of wireless data products for fixed and mobile applications.

[10] In the years prior to 2006, Dataradio's taxation year ended on July 31st of each calendar year.

[11] At the end of 2005, or at the beginning of 2006, Dataradio requested that its taxation year be modified to February 28th of each calendar year to make it correspond to the taxation year end of a potential purchaser: CalAmp Corp.

[12] Old Dataradio's first 2006 taxation year end was February 28, 2006.

[13] CalAmp Corp. is incorporated under the laws of the State of Delaware and is headquartered in the State of California. Its shares are publicly traded on the NASDAQ stock market.

[14] 4308093 Canada Inc. (4308093) was incorporated under the *Canada Business Corporation Act* and a wholly-owned subsidiary of CalAmp Corp.

[15] On May 9, 2006 CalAmp Corp. acquired all of the outstanding shares of Old Dataradio through its wholly-owned subsidiary 4308093 for USD$54,291,000 (or CAD$60,1 million).

[16] CalAmp Corp. paid a premium over the amount of its evaluation of the net fair market value of Old Dataradio's assets; one factor was that it would gain access to Old Dataradio's engineering resources and to a new market.

[17] CalAmp Corp. intended to continue Old Dataradio's operations after the acquisition and it intended to maintain the employment for all of Old Dataradio's employees and their existing levels of compensation.

[18] An amount of US$5,355,000 (or CAD$5,900,000) in Old Dataradio was allocated to bonuses destined to Old Dataradio's workforce; said bonuses were not conditional on staying with CalAmp Corp.

[19] Old Dataradio's second 2006 taxation year end occurred on May 9th, 2006.

[20] On May 10th, 2006, Old Dataradio ceased to be a Canadian-controlled private corporation.

[21] On May 30th, 2006, Old Dataradio was amalgamated with 4352491 Canada Inc. into a new corporation bearing the corporate number 4366361 (pursuant to the *Canada Business Corporations Act*). This amalgamated corporation, the Appellant, herein continued to be named Dataradio Inc. until February 5th, 2010, at which time it changed its corporate name to CalAmp Wireless Networks Inc.

[22] During the taxation year prior to 2006, Old Dataradio earned investment tax credits with respect to qualified SR&ED which were either refunded or applied against Part 1 tax pursuant to the *Income Tax Act* (the "Act").

[23] For the taxation year which started on March 1st, 2006 and ended on May 9th, 2006, the Appellant declared that Old Dataradio had undertaken SR&ED with respect to fourteen projects which required the participation of fifteen scientists and engineers, twenty-two technologists and technicians, five managers and administrators and finally one person acting as technical support staff (SR&ED employees).

[24] For the taxation year which started on March 1st, 2006 and ended on May 9th, 2006, the Appellant declared that Old Dataradio had paid an amount of $2,589,681 in salaries to its SR&ED employees (excluding the salaries paid to specified employees).

[25] The amount of $2,589,681, which was declared as having been paid as salaries to Old Dataradio's SR&ED employees, included an amount of $1,990,036 which represented bonus incentives referred to at paragraph 18 above.

[26] In the years prior to 2006, Old Dataradio had often paid bonuses to SR&ED employees. However, the evidence revealed that: i) prior to 2006, Old Dataradio's policy was to pay modest Christmas bonuses to salaried employees irrespective or whether their contracts provided for such measures (Exhibit A-1, Tabs 7 and 8); ii) the amounts of these bonuses would vary according to Old Dataradio's annual financial performance and Mr. Robert Rouleau (the Appellant's president during the relevant period) testified that, in the case of SR&ED employees, Old Dataradio's objective was to pay bonuses that would amount to a little more than two weeks salary. A typical example was reviewed during the cross-examination of Mr. Rouleau, namely the case of Mr. Jonathan Beaulieu who received a $2,500 bonus, $1,500 bonus, a $2,020 bonus and a $2,020 bonus in 2002, 2003, 2004 and 2005, respectively; iii) in total, Old Dataradio paid bonuses totalling $201,233 in 2002 and $140,171 in 2003 (Exhibit I-2); iv), Old Dataradio paid Mr. Jonathan Beaulieu a bonus of $24,242 in 2006 (Exhibit I-1, Tab 2, p. 1) and his annual salary on a calendar year basis was approximately $52,530 (Exhibit A-1, Tab 9, p. 2); v) for the 2006 taxation year, the bonuses totalling $5,900,000 were paid to several different categories of employees and not only to SR&ED employees.

[27] The bonus granted for the year 2006 was determined by Old Dataradio's management (the "Vendor"), with the consent of CalAmp Corp. (the "Purchaser"), on the basis of the number of years of service, current salary and merit.

[28] The bonus paid to the Appellant's SR&ED employees in the amount of $1,990,036 was actually paid to the Appellant's employees no earlier than June 23, 2006.

[29] The Share Purchase Agreement (Exhibit I-1, Tab 9) is clear at section 6.5 that CalAmp Corp. intended to continue the employment of all employees of Old Dataradio on an at will basis; however, the bonuses paid were not conditioned on a commitment from the employees to stay with CalAmp Corp.

[30] Paragraph 6.11 of the Share Purchase Agreement (Exhibit I-1, Tab 9) is to the effect that the bonuses were accrued as of the Closing Date.

[31] I also wish to point out that the following assumptions of fact stipulated at paragraph 11 of the Reply to the Notice of Appeal were not refuted by the Appellant.

(w) Old Dataradio's SR&ED employees had no legally enforceable right to require the payment of bonus incentives.

[…]

(z) Prior to the payment of the bonus incentives, Old Dataradio's management represented to its employees that these amounts were a gift.

(aa) The bonus incentives paid to the Appellant's SR&ED employees were not related to the prosecution of SR&ED activities undertaken in the period which started on March 1, 2006 and ended on May 9, 2006.

(bb) The extent and nature of the SR&ED activities undertaken in the period which started on March 1, 2006 and ended on May 9, 2006 was in no way related to the payment of the bonus incentives.

(cc) For the period which started on March 1, 2006 and ended on May 9, 2006, the total of all regular salaries paid to Old Dataradio's SR&ED employees (excluding the salaries paid to specified employees and the bonus incentives) totalled $600,887.

[32] Finally, the evidence reveals that the Appellant elected (Exhibit I-1, Tab 3D, p. 45) in accordance with subsection 37(10) of the Act to use the proxy method, as set out in clause 37(8)(*a*)(ii)(B) of the Act to calculate its SR&ED expenditures. In calculating its 2006 SR&ED expenditures, the Appellant included the bonus incentives paid to its employees who were directly engaged in the prosecution of SR&ED in the amount of $1,990,036 pursuant to subclause 37(8)(*a*)(ii)(B)(IV) of the Act.

[33] I also wish to point out that the Appellant and the Respondent agree on the following:

i) the present appeal pertains to class B and not class C;

ii) the style of cause of this appeal shall correctly identify the Appellant as CalAmp Wireless Networks Inc.

The issue

[34] Since, in its 2006 income tax return, the Appellant elected in accordance with subsection 37(10) of the Act to use the proxy method, as set out in

clause 37(8)(*a*)(ii)(B) of the Act, to calculate its SR&ED expenditures, I am of the opinion that the only issue in the present case is whether the amount of $1,990,036 constituted "expenditures made in respect of an expense incurred in the Appellant's 2006 taxation year for salary and wages..." within the meaning of subclause 37(8)(*a*)(ii)(B)(IV) of the Act. In other work, it must only be determined whether there is a reasonable connection between the bonus incentives and the prosecution of the SR&ED.

The Appellant's position

[35] The Appellant's written submissions are as follows:

> QUESTION:
>
> The question to be answered by this Court is whether the Minister properly reassessed the Appellant for the taxation year ending May 9th, 2006 to reduce his refundable investment tax credit by an amount of $131,260 on the basis that an amount of $1,990,036 did not constitute an SR&ED expenditure and should be excluded as a qualified expenditures.
>
> ANSWER
>
> The definition of qualified expenditure at paragraph 9 of Section 127 of the *Income Tax Act*, R.S.C. 1985, ch. 1 (5th supplement) (hereinafter the "ITA") (Tab 3 of the Respondent's Authorities) is to the effect that a qualified expenditure is an amount incurred by a taxpayer in a taxation year that is an expenditure incurred in the year by the taxpayer in respect of scientific research and experimental development that is an expenditure, among many possibilities, described in paragraph 37(1)(a) (Tab 1 of the Respondent's Authorities). There is no limitation regarding the length of a taxation year. In other words, Parliament took into consideration the fact that a taxpayer could reorganize itself or enters into a transaction that could have an impact on the length of a taxation year and Parliament did not want to restrict the amount of the qualified expenditure in relation to the length of a taxation year.
>
> Section 37(1)(a) ITA (Tab 1 of the Respondent's Authorities) refers to amounts, each or which is an expenditure of a current nature made by a taxpayer in the year or in a preceding taxation year ending after 1973 relating to scientific research or experimental development carried on in Canada, directly undertaken by or on behalf of the taxpayer, and related to a business of the taxpayer. Again, there is no restriction regarding the length of a taxation year. Moreover, the reference to a taxation year or in a preceding taxation year ending after 1973 shows that Parliament intended to increase the benefits for a taxpayer. There is no restrictive intent.

Section 37 ITA (Tab 1 of the Respondent's Authorities) is to the effect that an expenditure in respect of scientific research and experimental development is an expenditure made in respect of an expense incurred during the year for salaries or wages of an employee who is directly engaged in scientific research and experimental development in Canada that can reasonably be considered to relate to such work having regard to the time spent by the employee therein and, for this purpose, where that portion is all or substantially all of the expenditure, that portion shall be deemed to be the amount of the expenditure. Again, there is no reference to the length of a taxation year. Moreover, this section refers to the nature of the work done by the employees. In the present case, the bonuses were paid to SR&ED employees because they were doing scientific research and experimental development work. There is a direct link between the bonus in the present case and the nature of the work performed by the employees. The evidence of the Appellant's witness in clear: in 2006, there is clear link between the nature of the work done (scientific research and experimental development) and the bonuses. The history of the bonuses in the present case is clear: SR&ED employees, on a per capita basis, always received more bonuses than the other employees because the SR&ED employees were conducting scientific research and experimental development work.

Section 37(9) ITA (Tab 1 of the Respondent's Authorities) is to the effect that for the purpose of the scientific research and experimental development expenses, an expenditure does not include a bonus, where the bonus is in respect of a specified employee (Tab 1 of the Respondent's Authorities). The evidence is clear that the bonuses in the present case were not paid to specified employees (see paragraph 11(s) of the Reply to the Notice of Appeal).

Therefore, when Parliament intended to restrict the scientific research and experimental development expenditures, Parliament did so specifically. There is no restriction in the ITA regarding the bonuses in the present case. Therefore, as the Supreme Court of Canada has decided in many cases (inter alia, Copthorne Holdings Limited, Tab 17 of the Appellant's Book of Authorities, page 759 and Multiform Manufacturing Co. Limited, Tab 18 of the Appellant's Book of Authorities, page 6), when Parliament intends to restrict something and does is specifically, there is no restriction regarding the other elements. In other words, considering that Parliament excluded the bonuses to specified employees, the bonuses to the other employees are admissible.

It is clear that the bonuses in the present case are taxable in the hands of the employees (see the definition of "salaries or wages" at section 248 ITA (Tab 4 of the Respondent's Authorities). In this respect, we wish to point out that the Canada Revenue Agency, in its Letter of Interpretation 9320837, November 26th, 1993, expressed the view that all the elements regarding which an employee shall pay tax on are scientific research and development expenses (see Tab 7 of the Appellant's Book of Authorities; see the paragraph on page 2 of 6 starting with "En tenant compte…"). In the present case, the Respondent is trying to restrict its own Letter of Interpretation.

Moreover, as it more fully appears from another Letter of Interpretation issued by the Canada Revenue Agency, 96-06, June 28th, 1996 (Tab 10 of the Appellant's Book of Authorities; see the paragraph on page 38 of 47 starting with "Gratification designe…"), the Canada Revenue Agency has specifically issued an opinion that there is no restriction regarding bonuses in the context of scientific research and experimental development expenses. Indeed, the Canada Revenue Agency expressly refers to bonuses as admissible for scientifically research and experimental development purposes and does not attach any restrictions. In the present case, the Respondent is trying to attach restrictions to the concept of bonuses. This is clearly contrary to the Canada Revenue Agency's historical point of view.

As the Supreme Court of Canada has clearly established (Harel, Tab 19 of the Appellant's Book of Authorities, page 859) an administrative interpretation cannot contradict a clear legislative text; however, an administrative interpretation has weight in case of doubt about the meaning of legislation and becomes and important factor. In other words, if the Court has any doubt about the meaning of the legislation, the above-mentioned administrative interpretations have weight. Considering that the Canada Revenue Agency has always accepted bonuses to employees who are not specified employees, without restrictions, the Court shall conclude that the bonuses in the present case are admissible as scientific research and experimental development expenses and that the restrictions the Respondent is trying to include shall be dismissed.

As the Supreme Court of Canada has written on many occasions (inter alia, Placer Dome, Tab 14 of the Appellant's Book of Authorities, pages 727, 728 and 729, Canada Trustco, Tab 15 of the Appellant's Book of Authorities, page 610 and Corporation Notre-Dame de Bon-Secours, Tab 16 of the Appellant's Book of Authorities, page 20), the interpretation of tax legislation should follow the ordinary rules of interpretation. The Court shall look at the purpose of the legislation. As we have seen above, Parliament did not restrict the concept of taxation year in any way and Parliament, when it wanted to restrict an element did so specifically (bonuses paid to specified employees are excluded), therefore bonuses to non-specified employees shall be included. Finally, a reasonable doubt, not resolved by the ordinary rules of interpretation, shall be settled by recourse to the presumption in favour of the taxpayer (see Corporation Notre-Dame de Bon-Secours, p. 20). In other words, if the Court has a doubt about the interpretation of the legislation, the Appellant shall win the case.

Finally, as the Supreme Court of Canada pointed out in the case of Hickman Motors Limited (Tab 13 of the Appellant's Book of Authorities, pages 26 and 27), the standard of proof in tax cases is the civil balance of probabilities. The initial onus is on the taxpayer to demolish the Minister's assumptions in the assessment. The initial onus of demolishing the Minister's exact assumptions is met where the Appellant makes out at least a prima facie case. In the present case, the Appellant has clearly made a prima facie case to the effect that the bonuses paid were paid to employees,

> who were not specified employees, because they were doing scientific research and experimental development work and that there are no restrictions in the law regarding said employees. When Parliament intended to include restrictions, it did so specifically, as more fully appears from the exclusion of the bonuses in relation to specified employees. Moreover, there is no restriction in the law regarding the length of a taxation year. Therefore, if the Respondent wishes to include restrictions (the length of a taxation year and restrictions to bonuses over and above the specific restriction regarding specified employees), the Respondent has the burden of proof.

[36] The Appellant's written submissions are instructive in the present appeal but they do not address the only relevant issue: is there a reasonable connection between the bonus incentives and the prosecution of the SR&ED? The Appellant did not recognize that, under the proxy method, such as in the present case, salary and wages for SR&ED purposes are allowed under subclause 37(8)(*a*)(ii)(B)(IV) of the Act, which reads as follows:

> "(8) In this section,
>
> (a) references to expenditures on or in respect of scientific research and experimental development
> […]
> (ii) where the references occur other than in subsection 37(2) include only
> […]
> (B) where a taxpayer has elected in prescribed form and in accordance with subsection (10) for a taxation year expenditures incurred by the taxpayer in the year of which is
> […]
> (IV) that portion of an expenditure made in respect of an expense incurred in the year for salary or wages of an employee who is directly engaged in scientific research and experimental development in Canada that can reasonably be considered to relate to such work having regard to the time spent by the employee thereon, and, for this purpose, where that portion is all or substantially all of the expenditure, that portion shall be deemed to be the amount of the expenditure, […]"
> [Our emphasis]

[37] Subclause 37(8)(*a*)(ii)(B)(IV) of the Act clearly specifies that only that portion of salary and wages that can reasonably be considered to relate to SR&ED activities can be allowed as an expenditure for SR&ED purposes.

[38] Since it is a question of fact whether any portion of a bonus may be related to SR&ED activities in the year, I must determine the underlying reasons for paying the bonus. To this end, I must distinguish the method of calculating the bonuses from the

reasons for paying the bonuses. The reasons for paying the bonuses will reveal whether there is a sufficient nexus with SR&ED.

[39] In this case, Mr. Rouleau testified that the method of calculating the bonuses was based on the number of years of service, current salary and merit of each employee.

[40] However, the evidence reveals that the bonuses were paid mainly on the basis of two factors:

a) the belief by Old Dataradio's shareholder that salaried employees should share in the financial success resulting from the sale of the company (Exhibit I-1, Tab 8, p. 2);

b) the corresponding benefit to the purchaser CalAmp Corp. of creating conditions which would favour the retention of employees following its acquisition of Old Dataradio (Exhibit I-1, Tab 4, pp. 50 and 51: Tab 5, p. 4 (3rd par.: "[…] In addition, with a changeover of management, many employees tend to leave or retire. The payment of their bonus represented a strategic decision, that was agreed upon by the purchaser. […]"; Tab 9, p. 43, par. 6.5.

[41] I am of the opinion that there is no connection with the payment of the bonuses at issue and the bonus policy followed in the past by Old Dataradio, with any SR&ED work carried on during the year at issue. Old Dataradio's traditional policy stand in stark contract to the payments made to its employees for the taxation year at issue, which represents a period of approximately two months. For example, Mr. Beaulieu was paid a bonus of $24,242 in 2006, an amount which was almost ten times higher than any bonus he had ever previously received.

[42] It is also worth nothing that Mr. Rouleau (the only Appellant's witness) candidly admitted that the bonuses paid to Old Dataradio's SR&ED employees were not related to the prosecution or SR&ED activities undertaken in the two months in the 2006 period (see Transcript, p. 56, lines 17 to 24).

[43] Subclause 37(8)(*a*)(ii)(B)(IV) of the Act also limits allowable amounts to those expenditures incurred in the year. It is clear from the opening words of clause 37(8)(*a*)(ii)(B) of the Act that the word "year" at subclause 37(8)(*a*)(ii)(B)(IV) refers to the concept of "taxation year" which corresponds, in the instant case, to the "fiscal period" of the appellant, which in turn corresponds to period for which the

appellant's accounts are established for purposes of assessment under the Act (Sections 249 and 249.1 of the Act). In this case, this fiscal period is that of March 1, 2006 to May 9, 2006 (Exhibit I-1, Tab 3C, p. 2; Tab 3D, p. 44). This is the only period which is relevant to the determination of whether the bonuses paid to Dataradio's SR&ED employees were directly related to the prosecution of SR&ED activities.

[44] I want also to point out that my analysis is also consistent with the CRA's published "SR&ED Salary or Wages Policy" (SR&ED Salary or Wages Policy, Canada Revenue Agency: December 19, 2012) which, in particular, specifies that:

> "[…]
> There would be no reasonable link between the expenditure and the prosecution of SR&ED where, for example, an employee […] receives:
>
> - salary, including a bonus, when the income that was used to pay the amount was not earned from the ongoing, normal activities of the business. This would include an amount paid to an employee that was earned from a capital transaction such as the sale of the business, the sale of shares or the sale of an asset. […]
>
> Such amounts do not have the capacity of being allocated to SR&ED (cannot be SR&ED expenditures). In other words, the allocation of salary or wages to SR&ED is made after such amounts are excluded from remuneration."

[45] In addition, the payment of the bonuses at issue does not satisfy the criteria set out in *Alcatel Canada Inc. v. Canada*, 2006 TCC 149, par. 36, which held that an expenditure would in particular be allowable in circumstances where there existed "a recurrent need to compensate employees engaged" in SR&ED activities. In this case, the payment of the bonuses at issue was an isolated event and not the result of the application of Old Dataradio's traditional policy in respect of Christmas bonuses.

[46] Finally, the Appellant has not shown the expenditures "as having a direct relationship with the research projects and also being essential to their completion […]" (*Laboratoire Du-Var Inc. v. Canada*, 2012 TCC 366, par. 27 & 34 to 38).

[47] For these reasons, the appeal is dismissed.

Signed at Ottawa, Canada, this 25th day of June 2013.

"Paul Bédard"

Bédard J.

CITATION:	2013 TCC 201
COURT FILE NO.:	2010-3708(IT)G
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