

SR&ED Tax Cases

2022-2023 Rulings

**Lessons Learned: Process Length, Key Themes,
and why “Standard Practice” remains relevant**

Presented by

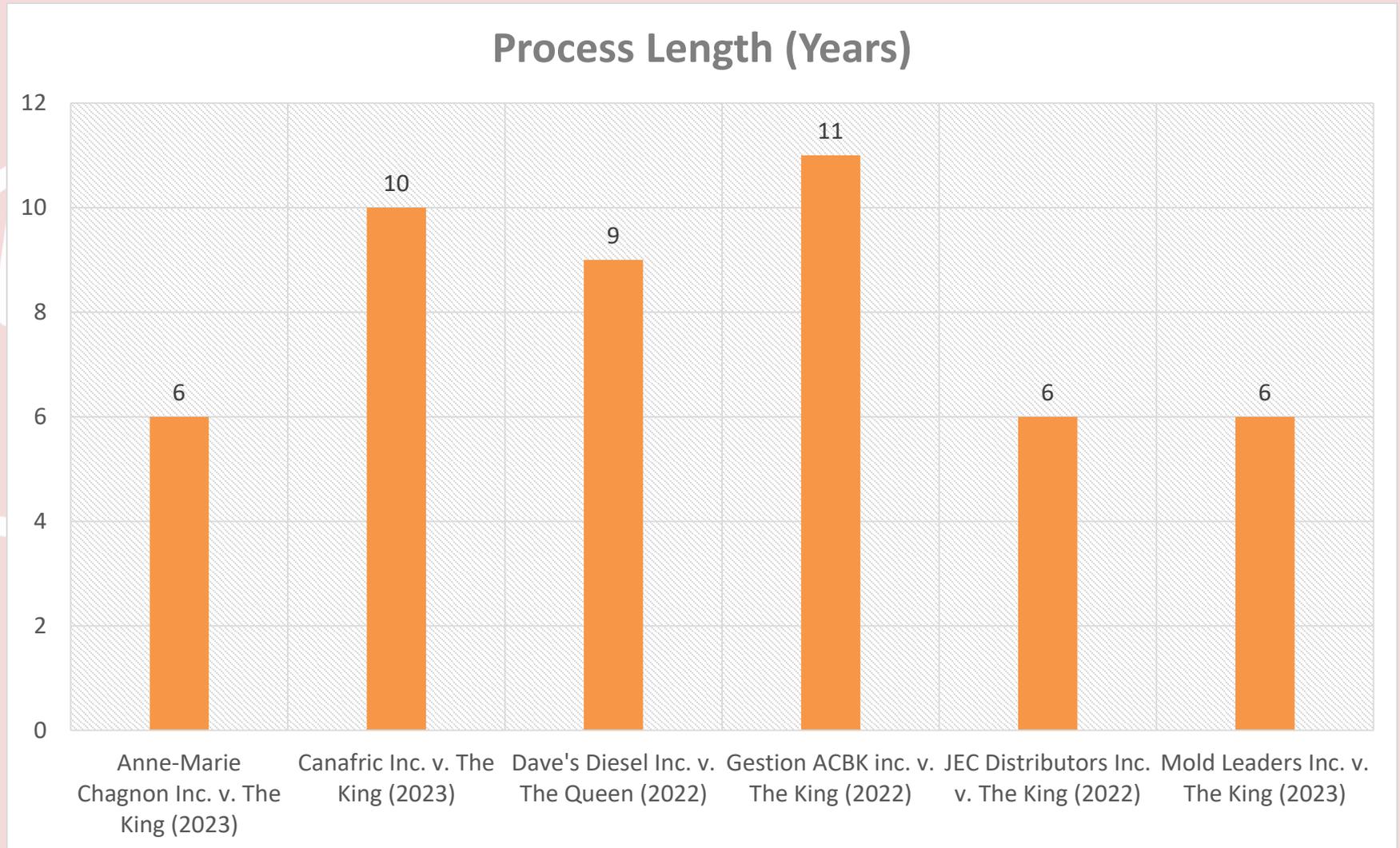
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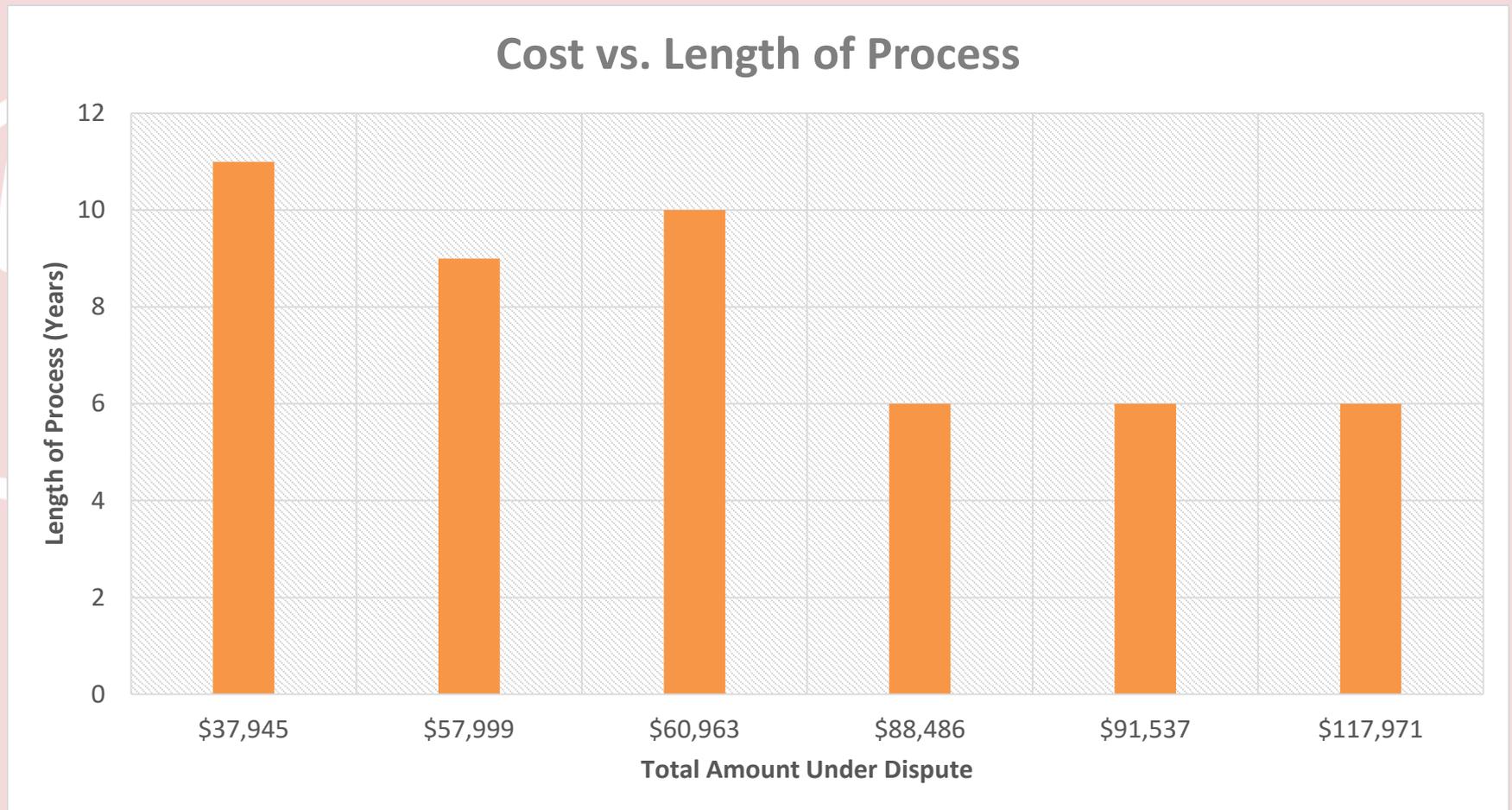
2022-2023 SR&ED Tax Court Rulings

Case Name	Primary Issue	Significance	Win/Loss	Fiscal Year	Process Length (Years)
CanafriC Inc. v. The King (2023)	Extension of technology	Moderate	Win	2013,2014,2015, and 2016	10
Anne-Marie Chagnon Inc. v. The King (2023)	Defining Standard Practice	Low	Loss	2016	6
Dave's Diesel Inc. v. The Queen (2022)	Defining Standard Practice	Low	Loss	2013, 2014	9
Gestion ACBK inc. v. The King (2022)	Defining Standard Practice	Moderate	Loss	2011	11
JEC Distributors Inc. v. The King (2022)	Defining Standard Practice	Low	Loss	2016	6
Mold Leaders Inc. v. The King (2023)	Defining Standard Practice	Low	Loss	2016, 2017	6

Length of Legal Process

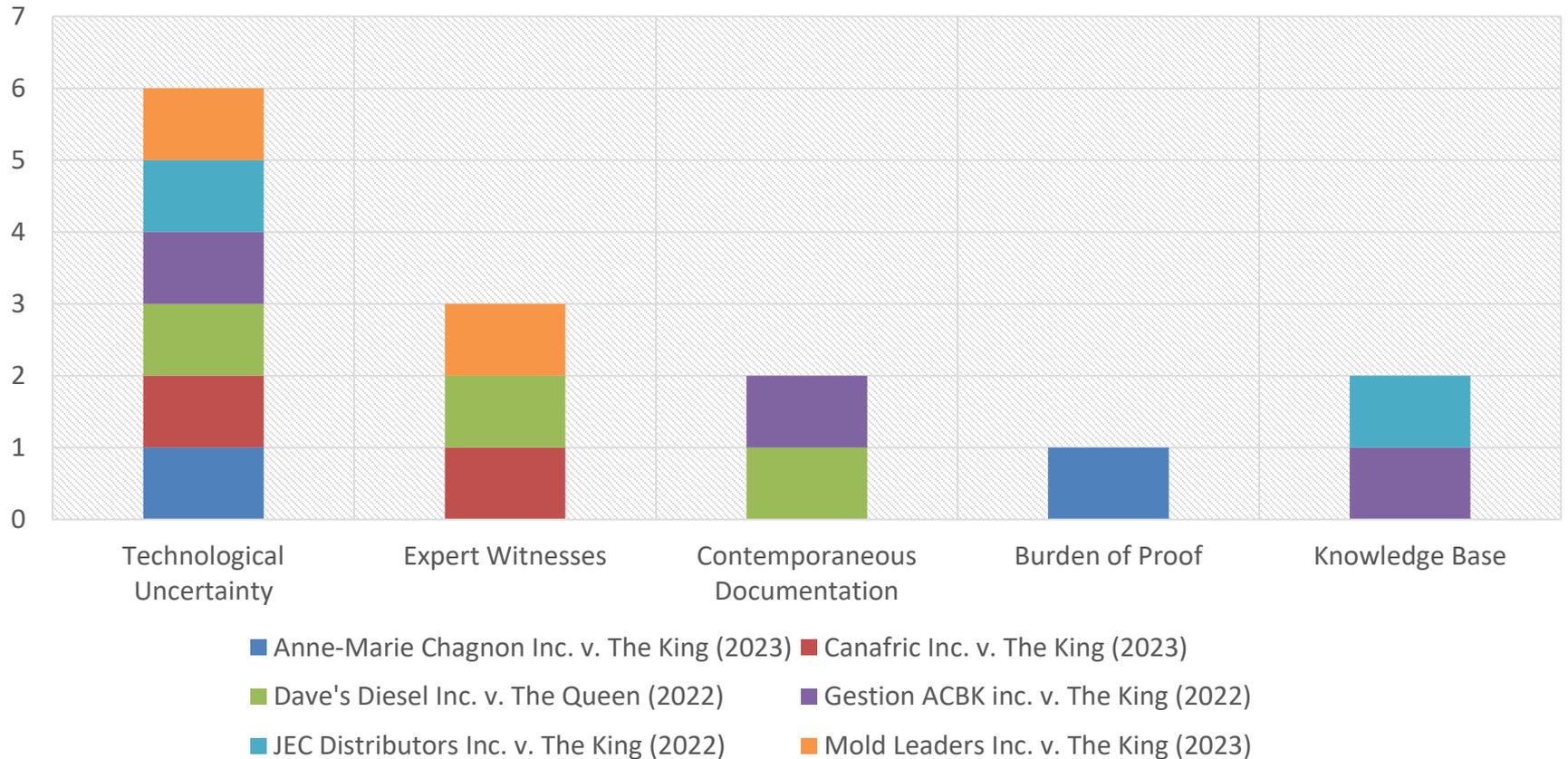


Length of Legal Process (vs Cost)



Key Themes

Key Lessons



Win: Extension of Technology

Canafric Inc. v. The King (2023)

Primary Issue	Win/Loss	Fiscal Year	Court	Location	Date(s)	Process Length	Amount Under Dispute
Extension of technology	Win	2013,2014,2015, and 2016	Tax Court of Canada	Hamilton, ON	7/26/2023	10 years	F2013 (\$22,183), F2014 (not specified), F2015 (\$15,476), F2016 (\$23,304)

The Appellant (Canafric Inc.) is a food manufacturing business specializing in developing frozen pie recipes that address their customers' targets and requests, while also aiming to reduce salt and fat contents in its products and maintain their good taste.

During the taxation years in question, the Appellant claimed a total of 13 projects in which they claimed experimental development was required. 7 of these projects were selected for review by the CRA.



Canafric Inc. v. The King (2023)

Key Lessons – Technological Uncertainty

A project must meet all the criteria laid out in the "**five questions**" to be eligible for SR&ED, including identifying the "Technological Uncertainty".

- In this case, the Judge utilized the five questions initially set forth by Justice Bowman in *Northwest Hydraulic Consultants Ltd. V. The Queen (1998)* and then reaffirmed in *CW Agencies Inc. c. Canada (2001)*, to determine the eligibility of each of the Appellant's 7 projects chosen for review.
- The Appellant was able to prove their work did meet the criteria laid out in the "five questions" and the judge allowed their appeal.
- At the Appeal stage, Canafric communicated a 120-page document to the CRA which included a detailed description of the projects and the development process.

The “5 Questions” of SR&ED

1. Was there a scientific or technological **uncertainty**?
2. Did the effort involve formulating **hypotheses** specifically aimed at reducing or eliminating that uncertainty?
3. Was the overall approach adopted consistent with a **systematic investigation or search**, including formulating and testing the hypotheses by means of experiment or analysis?
4. Was the overall approach undertaken for the purpose of achieving a scientific or a technological **advancement**?
5. Was a **record** of the hypotheses tested and the results kept as the work progressed?



Canafric Inc. v. The King (2023)

Key Lessons – Expert Witnesses

Providing an **expert in the field of SR&ED conducted** can be crucial for projects to be seen as SR&ED versus routine engineering.

- In this case, the Appellant's expert witness was involved at every stage of the review process for all the Taxation Years, spoke to specific challenges encountered in every project, had a good recollection of the various meetings with CRA representatives during the review process as well as the specifics of the technical discussions which took place during those meetings.
- The expert witness's credible and reliable demeanour allowed them to successfully establish that the work performed was SR&ED eligible.
- The judge noted the Expert witness, had good recollection of the various meetings with CRA representatives during the review process as well as the specifics of the technical discussions that took place during those meetings.

Defining Standard Practice

Justice Bowman stated in *Northwest Hydraulic Consultants v. The Queen* (1998):

- “Routine Engineering” [...] describes techniques, procedures and data that are generally accessible to component professionals in the field”
- The term “Standard Practice” used to be synonymous with “Routine Engineering”.
- This became a source of contention as many SR&ED applications as many argued the term “Standard Practice” was too broad and nullified the “uncertainty” of many projects. Although this was removed from the policies in 2015, it was still in place when about half of these projects were selected for review. And it's still an implied measurement today

Loss: Defining Standard Practice

Case Name	Win/Loss	Fiscal Year	Court Name	Process Length (Years)	Amount Under Dispute
Anne-Marie Chagnon Inc. v. The King (2023)	Loss	2016	Tax Court of Canada	6	\$117,971
Dave's Diesel Inc. v. The Queen (2022)	Loss	2013, 2014	Tax Court of Canada	9	\$26,865
Gestion ACBK inc. v. The King (2022)	Loss	2011	Tax Court of Canada	11	\$37,945
JEC Distributors Inc. v. The King (2022)	Loss	2016	Tax Court of Canada	6	\$91,537
Mold Leaders Inc. v. The King (2023)	Loss	2016, 2017	Tax Court of Canada	6	\$17,618

Loss: Anne-Marie Chagnon Inc. v. The King (2023)

Primary Issue	Win/Loss	Fiscal Year	Court	Location	Date(s)	Process Length	Amount Under Dispute
Defining Standard Practice	Loss	2016	Tax Court of Canada	Montreal, QC	2023-03-21	6 years	\$117,971

- **Business of the Appellant:** Anne-Marie Chagnon Inc., specializes in the jewelry and goldsmith industry; specifically, in the manufacture and resale of handcrafted jewelry.
- “[49] The Court is of the opinion that the appellant could have solved the problems related to the manufacture of the molds and the finishing of the parts by "routine technical studies" or "usual procedures" known to "competent specialists in this field" and that the evidence as a whole demonstrates that there was no technological or scientific uncertainty.”

Anne-Marie Chagnon Inc. v. The King (2023)

Key Lessons

Technological Uncertainty	A project must meet all the criteria laid out in the " five questions " to be eligible for SR&ED, including identifying the "Technological Uncertainty".	The Appellant was unable to prove they had identified a technological uncertainty and sought to reduce or eliminate that uncertainty through experimentation or analysis in all of their projects.
Burden of Proof	In the Tax Court, the burden of proof on the Appellant is the "balance of probabilities" and not "beyond a reasonable doubt".	In this case, the judge explained "the burden of proof on the Appellant is the balance of probabilities — and not beyond a reasonable doubt, which is a higher standard that does not apply to appeals before this Court." The Appellant was unable to provide adequate proof to defend their claim.

Loss: Dave's Diesel Inc. v. The Queen (2022)

Primary Issue	Win/Loss	Fiscal Year	Court	Location	Date(s)	Process Length	Amount Under Dispute
Defining Standard Practice	Loss	2013, 2014	Tax Court of Canada	Hamilton, ON	2022-06-10	9 years	\$26,865 and \$31,134

- **Business of the Appellant:** Dave's Diesel Inc., is a fuel injection shop for the diesel engine industry.
- The Appellant set out to find a way to remanufacture fuel injectors on its own.

Dave's Diesel Inc. v. The Queen (2022)

Key Lessons

Technological Uncertainty	A project must meet all the criteria laid out in the " five questions " to be eligible for SR&ED, including identifying the "Technological Uncertainty".	In this case, the Appellant was unable to prove they had identified a technological uncertainty and sought to reduce or eliminate that uncertainty through experimentation or analysis in all of their projects.
Expert Witnesses	Providing an expert in the field of SR&ED conducted can be crucial for projects to be seen as SR&ED versus routine engineering.	In this case, the judge observed that the Appellants lone witness "did not study mechanical engineering and has no degree, certificate or designation in the field", and "none of the individuals involved in the project in 2013 or 2014 were engineers or mechanics." The fact that all the individuals involved were non-specialized in the work at hand, and that there was an absence of experts in the related field greatly weakened the Appellants case.
Contemporaneous Documentation	Maintaining a well-organized and complete collection of documentation is imperative for the success of SR&ED applications.	In this case, the judge noted the evidence presented by the Appellant was minimal with concise entries. The lack of measurable or quantified indicators, to support the scientific or technological advancement achieved through the project made it impossible for the Appellant to prove SR&ED occurred.

Loss: Gestion ACBK inc. v. The King (2022)

Primary Issue	Win/Loss	Fiscal Year	Court	Location	Date(s)	Process Length	Amount Under Dispute
Defining Standard Practice	Loss	2011	Tax Court of Canada	Ottawa, ON	2022-09-29	11 years	\$37,945

- **Business of the Appellant:** The Appellant designs, installs, and programs automated systems in the agri-food industry.
- This case dealt with the design and installation of the hydrodynamic system on a residential home.

Gestion ACBK inc. v. The King (2022)

Key Lessons

Technological Uncertainty	A project must meet all the criteria laid out in the " five questions " to be eligible for SR&ED, including identifying the "Technological Uncertainty".	The evidence shows that the Appellant used common techniques to try to resolve the technological uncertainties he faced and the expenses incurred by the Appellant revolved around the construction and installation of a pre-existing thermal storage system.
Contemporaneous Documentation	Maintaining a well-organized and complete collection of documentation is imperative for the success of SR&ED applications.	The Appellant did not have evidence to precisely describe the techniques that he used in order to try to overcome these uncertainties, either during the design or the construction of his system.
Knowledge Base	The knowledge base must be established at the outside of the project.	Without conducting sufficient background research before starting work, the Appellant assumed they were solving a problem that could not be fixed by standard practices. The court was able to quickly discern by the patent of the technology used in this case that there were systems similar to that designed by Hydro LMR since the 1980s.

Loss: JEC Distributors Inc. v. The King (2022)

Primary Issue	Win/Loss	Fiscal Year	Court	Location	Date(s)	Process Length	Amount Under Dispute
Defining Standard Practice	Loss	2016	Tax Court of Canada	Toronto, ON	2022-12-28	6 years	\$91,537

- **Business of the Appellant:** JEC Distributors Inc., is a company who manufactures and distributes products for the auto industry.
- The Appellant claimed 3 different projects in their 2016 SR&ED claim. Their first project aimed to develop a system of sensors that could be applied to each welding gun to monitor the flow and temperature of the water to that gun. In their second project the Appellant wanted to develop a way of reliably collecting the waste chips made from the use of the dressing system. Their third, and final, project dealt with finding a way to manage the adhesives and sealants that get on the welding tips during the welding process.

JEC Distributors Inc. v. The King (2022)

Key Lessons

Technological Uncertainty	A project must meet all the criteria laid out in the " five questions " to be eligible for SR&ED, including identifying the "Technological Uncertainty".	In this case, the Appellant was unable to prove they had identified a technological uncertainty and sought to reduce or eliminate that uncertainty through experimentation or analysis in all of their projects.
Knowledge Base	The knowledge base must be established at the outside of the project.	The Appellant assumed they were solving a problem, as a literature review at the outset of the project was not completed to establish the knowledge base.

Loss: Mold Leaders Inc. v. The King (2023)

Primary Issue	Win/Loss	Fiscal Year	Court	Location	Date(s)	Process Length	Amount Under Dispute
Defining Standard Practice	Loss	2016, 2017	Tax Court of Canada	Ottawa, ON	2023-08-21	6 years	F2016 (\$17,618), F2017 (\$70,868)

- **Business of the Appellant:** Mold Leaders Inc. (ML), conducted a business of injection molding, computer numerically controlled machining and prototype injection molding for their clientele.
- The Appellant claimed 8 projects for SR&ED, all of which revolved around making custom molds for their customers and the “uncertainties” they encountered in each process.

Mold Leaders Inc. v. The King (2023)

Key Lessons

Technological Uncertainty	A project must meet all the criteria laid out in the "five questions" to be eligible for SR&ED, including identifying the "Technological Uncertainty".	The Appellant was unable to prove they had identified a technological uncertainty and sought to reduce or eliminate that uncertainty through experimentation or analysis in all of their projects.
Expert Witnesses	Providing an expert in the field of SR&ED conducted can be crucial for projects to be seen as SR&ED versus routine engineering.	The Appellant had retained the company National R&D Inc. as an expert witness for their case, however, because the individual from National R&D Inc. "did not have sufficient background in the plastic injection molding industry to be qualified as an expert in that industry", he was not accepted as an expert and his expert report was not admitted into evidence.

Lessons, Recap...

- To be eligible for SR&ED Investment Tax Credits (ITCs), the method must be a **systematic investigation or search** where hypotheses formed using the existing knowledge base are tested through experimentation and analysis and documentation is kept throughout the process.
- It is vital to **establish an uncertainty** (gap in the knowledge base) and why experimental development is the only option.
- Compare your work to the **five questions** and ensure you have documentation to support it (ex. Hypothesis – test – analysis)
- Providing **an expert in the field of SR&ED conducted** can be crucial for projects to be seen as SR&ED versus routine engineering.
- **Keep clear documentation** to show Business project costs are not being included within SR&ED Projects.
- Maintaining a well-organized and complete collection of **documentation is imperative** for the success of SR&ED applications.
- In the Tax Court, the **burden of proof** on the Appellant is the "balance of probabilities" and not "beyond a reasonable doubt".

Summary

- The "**5 questions of eligibility**" set forth by Northwest Hydraulic / CW Agencies remains the benchmark for SR&ED eligibility.
- The **knowledge base** must be established at the outside of the project.
- Knowledge of the program requirements is essential, as is **clear documentation**.
- **Be prepared to wait:** the process length, from the fiscal year in which the work was performed to when the court made a final decision, ranged from 6 to 11 years in this small selection of rulings.