

# THE BOTTOM LINE

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## AC Company wins appeal vs. CRA

By Grant Cameron

A recent tax court ruling against the Canada Revenue Agency shows that small-business owners who have been refused Scientific Research and Experimental Development (SR&ED) credits can take on the federal agency and win, according to tax consultant Julie Bond of Toronto.

Bond represented Airmax Technologies in the case, and successfully argued on appeal that the approach taken by the CRA trivialized research and development in Canada. The tax watchdog had denied the company's claim for nearly \$400,000 in SR&ED expenditures.

"This means that even small companies can go to tax court and right a wrong if they feel they have been incorrectly denied by the CRA," Bond, president

of Bond Consulting, said of the decision.

"The taxpayer wanted to prove that CRA was wrong, and that's what they did."

In the recent ruling, Tax Court of Canada Justice Robert J. Hogan found that the CRA had incorrectly denied Airmax \$387,553 worth of qualified SR&ED expenditures in the company's 2008 taxation year.

The company, an installer of heating, ventilation and air-conditioning systems in residential homes, had claimed the expenditures for a project that led to the development of a new HVAC system for multi-storey residential townhomes.

The company claimed SR&ED expenses based on the work it did.

However, the Minister of National Revenue opted to break the project down into component sections and claimed that the company was merely reproducing existing technology. The CRA determined that only the work conducted by Airmax on the air diffuser constituted eligible SR&ED expenses and that all of the remaining development work involved "routine engineering."

The CRA, therefore, disallowed most of the SR&ED expenditures. After weighing the evidence, however, Justice Hogan decided that Airmax had established that the balance of its claim constituted proper SR&ED expenditures.

In a written ruling, he stated that the company had to make modifications to

including the amuser, flexible ductwork, the boiler and electronically commuted fan motor, in order to make it work at the level necessary to ensure commercial success.

He said the evidence showed that the development work was undertaken to ensure that the constituent parts of the HVAC system could function together as a complete system for multistorey townhouses, and that Airmax developed a product unlike any other in the market.

Bond said the ruling means the CRA will have to look at projects in their

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entirety, and can no longer break a job down into component sections and then deny a company its SR&ED credits. "It's very important because this type of approach from CRA has been going on for the last three years," said Bond. "Tax consultants from coast to coast have been frustrated because if you break R&D projects into components everything looks simple and that's not in the spirit of the program." According to Bond, the ruling could open up a Pandora's Box for the CRA; as companies that have been denied

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*Elliot Schiller,  
Teeger Schiller*

SR&ED claims in the past may now have grounds to appeal.

The CRA, however, does not believe that to be the case.

Mylene Croteau, media relations advisor with the CRA in Ottawa, wouldn't comment on the specifics of the case, but she indicated the agency has reviewed the ruling and would not be changing its approach.

She said the agency decided not to file an appeal of the decision with the Federal Court of Appeal.

"The decision of the Tax Court of Canada is based on the facts specific to this case and does not warrant a change in the existing CRA policies and procedures."

However, Elliot Schiller of Toronto management consultants Teeger Schiller believes the ruling could have significant ramifications for the CRA. "From the beginning of time, the CRA and the Canadian taxpayer have argued over when the SR&ED starts and when it really ends and routine engineering kicks in. Obviously,

the taxpayer always believes that the SR&ED started earlier than CRA believed."

The ruling, he said, essentially means that the CRA can no longer "take the yellow out of the egg without saying that the whole egg counts."

Much of Schiller's work is focused on SR&ED claims and obtaining grants and tax incentives for small- and medium-sized companies.

Members of the Association of Professional Accounting and Tax Consultants, which represent independent accountants, tax consultants and preparers, and bookkeepers, regularly consult with him on SR&ED work.

He said the CRA routinely breaks up components of a project to determine if a company can claim SR&ED expenditures, a practice he maintains is wrong.

He used the analogy of Sir Edmund

Hillary's 1953 climb of Mount Everest to illustrate his point.

"If you could convince the CRA, which is what this tax ruling did, that SR&ED begins when you walk over the Khumbu Icefall, you've now added three more weeks to the project, said Schiller. "If the CRA had their way, the only thing that would count would be the six hours that they spent trying to figure out how to get over the Hillary Step. That's a six-hour project versus a four-week project. That's a lot of difference in money."

Although the ruling is a step forward, Schiller said the downside is that the CRA still has the right to interpret every project on its own merits. "It's an important ruling except that the CRA has the ability to argue that it was a fluke, a one-time ruling."

This excerpt is from The Bottom Line, January, 2013. Elliot Schiller is a Director at Teeger Schiller Inc. He manages the SR&ED Division which annually obtains over \$6M for clients to support their R&D activities.

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## David Teeger

### Director

David Teeger C.A., C.A. (S.A.) graduated as a Chartered Accountant in South Africa, and upon arrival in Canada he obtained his Canadian C.A. designation and joined Richter & Associates, a management consulting firm, where he concentrated his practice on various business sectors including household goods, fashion, automotive parts, public associations, and retail chains. He performed many roles in his 15 years at Richter, including managing the professional services organization in North America and all business operations throughout Europe.

David's professional capabilities include computer audits, feasibility studies, system analyses and assistance in the selection, negotiation and implementation of computerized solutions.

As a founding partner of Teeger Schiller Inc., he has focused his practice on consulting to management. His team of professionals has helped businesses select and successfully install a variety of ERP business solutions and add-on systems including business intelligence solutions to give new life to existing computer systems. David's clients not only rely on him to successfully manage the implementation of their new systems, but to manage the change that occurs in their organizations as a result of the use of these new tools.



## Elliot Schiller

### Director

Elliot Schiller, Ph.D., C.M.C. began his career as a Chemical Engineer working for Grumman Aircraft, in Long Island, New York. He obtained his Ph.D. at the University of Pittsburgh with funding from the U.S. Atomic Energy Commission, and, after being awarded a Presidential Fellowship, he went on to perform research and development activities at Brookhaven National Laboratory.

Since coming to Canada, he has primarily assisted consumer products and retail organizations in a variety of strategic management initiatives, traveling around the globe on behalf of his clients. In 1987, Elliot joined Richter & Associates, and it is here that he first met David Teeger.

As a founding partner of Teeger Schiller Inc., he has focused the SR&ED / Grant Division on obtaining grants and tax incentives for over 100 companies in the small to medium sized business sector. His team has provided services to the discrete / processing manufacturing, material development, textiles, apparel, automotive and computer sciences sectors. Annually, Teeger Schiller Inc. secures more than \$5 million in government funding to assist its clients in having their business initiatives supported by government funding.



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