

Encouraging Innovation and Growth

Pre-Budget Submission to the
House of Commons Standing Committee on Finance
By the Intellectual Property Institute of Canada

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Executive Summary

In this submission, the Intellectual Property Institute of Canada (IPIC) proposes two complementary programs to *assist Canada's businesses – in all regions and sectors – meet their expansion, innovation and prosperity goals, and thereby contribute to economic growth in the country.*

The proposed “First Patent Program” would provide a subsidy that encourages new innovators to obtain their first patent. New innovators are often hesitant to allocate resources to the protection of their intellectual property (IP). The program would result in a valuable asset useful in leveraging funds and attracting partners for commercial development.

The proposed “Innovation Box” would encourage companies to develop and implement Canadian innovations, by allowing business income derived from intellectual property to be taxed at a lower rate than regular business income.

The two programs are complementary in that they both are intended to support the commercial implementation of Canadian innovations, while targeting both ends of the previously recognized “innovation gap” in the Canadian economy. Together, these programs will support Canadian R&D, commercialization, intellectual property monetization, and job growth.

Introduction

IPIC welcomes the opportunity to address this question posed by the Standing Committee on Finance:

What federal actions would assist Canada's businesses – in all regions and sectors – meet their expansion, innovation and prosperity goals, and thereby contribute to economic growth in the country?

Growth, innovation, and intellectual property are all connected

The growth of innovative companies includes the key step of protecting IP assets, using tools such as patents, trademarks and industrial designs.

Why is this step important? IP, when properly protected, provides a commercial advantage to the innovator. IP assets can be used to leverage funding, and to attract partners in development – a patent is often a young company's biggest asset.

In Canada, that essential step, in the innovation process, of seeking IP protection is not yet ingrained in the entrepreneurial culture.

Canada is considered above average in the creation of knowledge, ahead of the United States and the United Kingdom.¹ However, it is also near the bottom in terms of transforming knowledge into usable inventions as measured by the number of patents per GDP, resulting in an "innovation gap".² For instance, Canada compares unfavorably with the US on a per capita basis when it comes to the number of patent applications filed, and a greater share of patent applications filed in Canada are non-resident filings.³

Many countries have implemented IP incentive programs to foster growth and innovation. Meanwhile, Canada currently ranks lowest with respect to patents as compared to 15 peer countries on an Innovation Report Card⁴, partly due to increased rates of patenting in other countries.

IPIC recommends two budget measures to foster a culture of innovation, encourage commercialization of new products, and support the growth of companies. The first, a "First Patent

¹ Emergence of Patent Box Regimes - Will Canada Follow Suit? Canadian Manufacturers and Exporters, January 2014

² Ibid

³ See chart labelled "A8 Patent applications for the top 20 offices, 2014" in WIPO World Intellectual Property Indicators, http://www.wipo.int/edocs/pubdocs/en/wipo_pub_941_2015.pdf

⁴ Based on 10 innovation indicators: The Conference Board of Canada, *How Canada Performs - Innovation*, <http://www.conferenceboard.ca/hcp/provincial/innovation.aspx>, current as of September 2015, (site accessed on April 25, 2016)

Program”, targets inventors and small businesses while the second, the “Innovation Box”, is aimed at businesses of all sizes.

The two programs are complementary in that both are intended to support the commercialization of Canadian innovations while targeting both ends of the “innovation gap”.

About IPIC

IPIC is the professional association of patent agents, trademark agents and lawyers practising in all areas of IP law. We have a long history of working with the federal government on a range of issues that are vital for Canadian economic prosperity.

Our membership totals over 1,700 individuals, consisting of practitioners in law firms and agencies of all sizes, sole practitioners, in-house corporate intellectual property professionals, government personnel, and academics. Our members’ clients include Canadian innovators, entrepreneurs, businesses, universities and other institutions.

Recommendation 1: Create a “First Patent Program”

Background

The Quebec government launched its “First Patent Program” in July 2015 to encourage small and medium-sized businesses to patent their inventions. The Quebec Program offers eligible businesses a subsidy on expenses related to obtaining a first patent. The credit equals 50% of the incurred expenses, up to \$25,000.⁵ There has been high demand for this program as funds allocated for the period of July 2015 to March 2016 were exhausted prior to the end of the period.

IPIC proposes that the Federal government adopt a similar program for Canada.

The Program’s Objectives – Opening the Door for Canadian Innovators

The Program would provide assistance to inventors, startups, and SMEs at a critical point where they have developed an innovative idea and are in a position to seek patent protection but may not have the financial resources to do so – or may not understand the importance of doing so. Thus, the Program would encourage qualified Canadian inventors and companies to file patent applications for inventions that provide the foundation of a successful venture. In light of the goal of fostering innovation amongst Canadian businesses, the principal objectives of the Program would be to:

⁵ Additional information on the Program may be obtained at: Ministère de la science, de l’économie et de l’innovation, *Programme premier brevet*, updated on March 15, 2016, <https://www.economie.gouv.qc.ca/bibliotheques/programmes/aide-financiere/programme-premier-brevet/> (accessed on April 14, 2016).

- (a) provide businesses with financial aid for protecting their inventions at an early stage; and
- (b) allow businesses to reallocate capital saved in the patenting process into further developing their business ventures.

The Program's Features – Accessible, Simple and Cost-effective

An advantage of the First Patent Program would be its clear scope and intent to foster a culture of innovation. The Program should be easily accessed and simple to administer.

IPIC would be pleased to:

- Assist with development of the criteria and application process.
- Assist with development of a promotional strategy. IPIC members would be well placed to promote the program, as would IPIC in its public awareness activities such as our Bank of Speakers partnership with the Canadian Intellectual Property Office (CIPO).
- Examine how IP education could be offered to innovators in conjunction with this program.

Costs of the Program

1. The grant would cover 50% of patenting expenses. Such expenses would include patenting costs and professional fees incurred up to the patent's grant.
2. IPIC believes the maximum funding provided by the program (the 50% of expenses) should be \$25,000.
3. We estimate that there are currently about 600 to 800 applicants/year who file a first patent application.
4. Therefore, if the program is successful in increasing the number of applications, we could use the figure of 1,000 applicants/year for financial estimates.
5. The program cost would therefore be in the range of \$25 million plus administration costs.

Benefits

It has been often said that young companies either do not have the budget to protect their IP or don't realize the importance of doing so. The existence of the Program, and its promotion, would immediately encourage innovators to protect their inventions. This step is essential to positioning a growing company for successful commercial deployment of their invention. And the financial aspect is important for startups, who have many competing spending priorities, and may otherwise not protect their IP.

Recommendation 2: Explore the feasibility of an “Innovation Box”

The Standing Committee on Finance has previously made the recommendation

It is well known that Canada lags in private sector investment in R&D and commercialization. The Standing Committee on Finance recommended in its December 2014 report that the government explore the feasibility of a “patent box”. We are therefore encouraging the government to carry out the Committee’s recommendation, with the nuance that the expression “Innovation Box” be used. Because the results of innovation can include many forms of intellectual property such as patents, trademarks, and industrial designs, a broader term seems more appropriate, at least for a feasibility study.

The innovation box is a new incentive

An innovation box is a tax incentive that allows business income from intellectual property to be taxed at a lower rate than regular business income. The expression “innovation box” comes from a checkbox provided on tax forms to identify revenues that would be eligible for the reduced innovation tax rate.

There is a distinction between R&D tax incentives and innovation boxes. R&D incentives support technology developments or input into the innovation process; conversely innovation boxes support the output or commercialization of R&D. In other words, innovation boxes differ from tax credits for R&D because they operate on the “back end” of the production cycle; innovation credits and deductions, on the other hand, operate on the “front end” of the cycle. These incentives are *complements* and not substitutes, working together to improve both R&D activity and commercialization activity in Canada.

Notably, Quebec announced, in its latest budget, an Innovation Box scheme that would lower corporate income tax spent on innovation from 11.8 to 4 percent, as of January 2017.

The Objectives Behind Adopting an Innovation Box for Canada

In a globalized economy, businesses consider a multitude of factors to determine the location of R&D, commercialization, and manufacturing activities. Implementing an innovation box may incentivize businesses to carry out these activities in Canada.

The federal government should consider modifying Canada’s tax regime by adopting an innovation box model to provide favorable tax treatment for income derived from exploiting the fruits of domestic R&D activities.

The innovation box regime would encourage companies to test and develop Canadian innovations and, in doing so, generate new market opportunities and new taxable revenue.

An innovation box may serve as a tool to attract “highly mobile IP” to relocate to Canada. That is, an innovation box regime would “pull” R&D activity into Canada by encouraging firms to adopt innovative processes and by requiring domestic IP ownership and development. This would help address the innovation gap in Canada. Such a regime should also avoid domestically developed IP from relocating outside Canada.

Studies indicate that firms are typically inclined to locate production facilities in the vicinity of their R&D activities⁶. Thus, by incentivizing the domestic location of R&D facilities, further domestic investment in production facilities may result, which would have economic benefits to Canada. It is believed that added or “found” tax revenue resulting from firms maintaining R&D and production facilities in Canada would result in the tax incentives funding themselves.⁷

Conclusion

IPIC makes two recommendations to assist Canada’s businesses meet their expansion, innovation and prosperity goals, and thereby contribute to economic growth in the country: *create a “First Patent” Program and explore the feasibility of an “Innovation Box”*.

We thank the Standing Committee on Finance for considering our recommendations. For more information, please contact our Acting Executive Director, Anne-Josée Delcorde, at 613-234-0516 or ajdelcorde@ipic.ca.

⁶ Commentary NO. 379 *Improving the Tax Treatment of Intellectual Property Income in Canada* C.D. Howe Institute, April 2013

⁷ Ibid