

# **AN ALTERNATIVE FUNDING MODEL FOR AGRIBUSINESS RESEARCH IN CANADA**

**ELLIOTT CURRIE AND ADAM DALE**

**UNIVERSITY OF GUELPH**

**GUELPH, ONTARIO, CANADA**

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**ATLANTA, GEORGIA, U.S.A.**

# **BACKGROUND AND PROBLEM**

## **Research Funding Dwindling**

- Especially Near Market or Applied

**Matching Funding Required, % increasing?**

**Traditional Reliance on Government Funding for Research**

**Now Matching Funding and Tax Credits**

**NEED Reliable On-Going Research Funding**

**Who is Setting the Research Agenda?**

# **GOALS AND PROCEDURES**

**Need Stable Long-Term Monies for Matching Purposes**

**We use a three stream model for research funding**

**“A Small Canadian Controlled Private Corporation (CCPC) can, for \$100,000 up front initial Investment, generate \$250,000 annually in Research Dollars, in Perpetuity”.**

# **MATCHING GRANTS**

**Growing Forward II, requires 25% matching funds from industry (funding from Federal and Provincial agricultural ministries)**

**National Research Council of Canada, Industrial Research Assistance Program (IRAP), requires 50% matching funds,**

**Ontario Ministry of Agriculture and Food (OMAF) New Directions requires 50% matching**

**Now tax credits**

# **TAXATION**

**Scientific Research & Experimental Development Expenditures (SR&ED) 35% Refundable Federal Tax Credit on eligible expenditures (CCPC)**

**Large corporations (20% reducing to 15% 2014)**

**Provincial Credits can be merged up to 34.5% credit PLUS the Federal SR&ED Credits**

**Capital Gains are Taxed at  $\frac{1}{2}$  of Applicable Tax Rate**

# TAX CREDITS

**Example: \$200,000 research grant to match \$200,000 contributed by industry**

**Receive 35% Refundable tax on \$200,000 = \$70,000**

**Cost for \$400,000 Research is \$130,000**

**Merge Provincial Credits of 20%, receive another \$40,000 tax refund**

**Cost for \$400,000 research is \$90,000**

**Tax Credits do not cover depreciable assets. 2013 budget**

# TAX IMPACTS

## Large & Public Corporations taxed at 28%

Table 2. Tax Credit Variations and Expenditures (000's)

	Example 1 (35%)	Example 2 (55%)	Example 3 (69.5%)
<b>Taxable Income</b>	300	300	300
<b>Taxes Payable - CCPC rate 15%</b>	45	45	45
<b>Research Expenditure (RE)</b>	200	200	200
<b>Research Tax Credit (35%)</b>	(70)	(110)	(139)
<b>Taxes Payable (refund)</b>	(25)	(65)	(94)
<b>Net Research Expenditure (NRE)</b>	130	90	61
<b>50/50 funding research Impact (RE x 2)/NRE</b>	3.08 times	4.44 times	6.56 times
<b>Portion of Research paid by CCPC</b>	32.50%	22.50%	15.25%

# **INVESTMENT STRATEGY**

**At today's interest rates to generate \$300,000 for research would require \$10 to \$15,000,000**

**We propose using Capital Markets that only requires a one time investment**

## **Index Options**

- Buy in-the-money Put on the S&P 500, 1 ½ to 2 years out
- Sell out-of-the-money Put one month
- Repeat monthly

**Considered low risk as covered and if market goes up sold puts worthless, keep the money**

**If market goes down, purchased Put increases in Value, temporary loss on sold puts, balanced following month**



# ACTUAL RESULTS

These Gains are Treated as Capital Gains so taxed at 1/2 the rate, if a CCPC taxed at 7.5%, (if not trading for gain)

Date	Investment \$	# of Options	Expenses \$	Gain \$	Net Gain \$
May '08	18,577	1	18,577	1,640	-16,937
Jun '08		1	2,111	3,059	949
Jul '08		1	26,862	29,346	2,484
Aug '08	14,827	2	19,900	3,749	-16,151
Sep '08	21,313	3	77,572	58,009	-19,563
Oct '08		3	146,179	154,816	8,636
Nov '08		3	114,274	124,986	10,711
Sep '11		14	112,527	103,073	-9,455
Oct '11		14	82,186	103,483	21,296
Nov '11		14	43,056	78,413	35,356
Dec '11		0	71,802	242,575	170,773

**Notes:** Gain for Dec '11 includes the assumed sale of all long options

# **RESEARCH FUNDING STRUCTURE**

**Propose that a Co-operative or Association or other Not for Profit Organization, establish a For Profit Subsidiary that is the investment and research arm of the organization**

**The investment is a one time event, generating ongoing gains**

**Investment earnings be injected into the Research,**

**If adequate may not need Government Monies**

# **STRATEGIC OVERVIEW**

**Co-op or Associations start own for-profit CCPC, and invest one time**

**Take Capital Gains/Returns and invest in R&D**

**SR&ED Tax Credit more than offsets the income tax owed**

**In some cases there can be flow through of net proceeds or tax credits back to the parent and their shareholders**

# **CONCLUSION**

**Government has own Agenda**

**Those with the Money make the rules**

**Need to inject own R&D money**

**Invest and make Adequate money to meet matching requirements**

**USE only the “INCOME”,**

**Keep the Principle to generate future cash flows for research**

**Potentially make own decisions on research**

**A \$100,000 UP FRONT  
INITIAL INVESTMENT,  
CAN GENERATE  
\$250,000 ANNUALLY IN  
RESEARCH DOLLARS, IN  
PERPETUITY.**

**ANY QUESTIONS?**