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Guideline

Guidelines for Compliance with the Radio Authorization Condition of Licence Relating to Research and Development (R&D)

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1. Introduction

1.1 Definitions

In these guidelines,

Adjusted gross revenues means total service revenues less inter-carrier payments, bad debt, third party commissions, and provincial and goods and services taxes collected.

Audited financial statements means financial statements prepared in accordance with the standards, as amended from time to time, of the Canadian Institute of Chartered Accountants.

Auditor's report means an auditor's report prepared in accordance with the standards, as amended from time to time, of the Canadian Institute of Chartered Accountants.

Licensee means a wireless telecommunications carrier that has been granted a radio authorization pursuant to the *Radiocommunication Act*, as amended from time to time.

Minister means the Minister of Industry.

Radio authorization means a licence, certificate or authorization issued by the Minister under paragraph 5(1)(a) of the *Radiocommunication Act*, as amended from time to time.

Spectrum licence means a spectrum licence as defined in section 2 of the *Radiocommunication Act*, as amended from time to time.

SR&ED means scientific research and experimental development as defined in the *Income Tax Act*.

Wireless telecommunications means the emission, transmission or reception of intelligence by radio or another wireless electromagnetic system.

1.2 Background

The policy objectives adopted by Canada with respect to telecommunications are set out in section 7 of the *Telecommunications Act*.¹ The Minister, in exercising his authority to issue radio authorizations to wireless telecommunications carriers, as conferred on him by section 5 of the *Radiocommunication Act*,² has due regard to these objectives.³ One of the objectives is “to stimulate research and development in Canada in the field of telecommunications and to encourage innovation in the provision of

¹ See the *Telecommunications Act*, as amended (<http://laws.justice.gc.ca/eng/acts/T-3.4/>).

² See the *Radiocommunication Act*, as amended (<http://laws-lois.justice.gc.ca/eng/acts/R-2/>).

³ Subsection 5(1.1) of the *Radiocommunication Act* allows the Minister of Industry to take into account Canada's telecommunications policy: In exercising the powers conferred by subsection (1), the Minister may have regard to the objectives of the Canadian telecommunications policy set out in section 7 of the *Telecommunications Act*.

telecommunications services.”⁴

To help to meet this objective, the Minister has issued certain radio authorizations which have, as a condition of licence, the requirement to invest a percentage of the licensees’ adjusted gross revenues in eligible research and development (R&D) related to telecommunications. These licensees must provide Industry Canada with an annual report that includes, but is not limited to, a statement of R&D expenditures, signed by a duly authorized officer of the licensee (e.g. Chief Financial Officer), for the fiscal year covered by the report and a description of the R&D activities. Industry Canada reserves the right to request an audited financial statement of R&D expenditures with an accompanying auditor’s report and, if so, will provide reasonable notice. Eligible R&D activities are those which meet the definition of SR&ED adopted by the Canada Revenue Agency in the *Income Tax Act*.⁵

The guidelines put forward in this document were developed to provide licensees with additional information on the condition of licence relating to R&D. In order to facilitate compliance and ensure consistency of reporting, these guidelines also set out the procedures to be followed by the licensees in reporting on these investments in R&D to Industry Canada.

2. Condition of Licence Relating to R&D

2.1 General

The condition of licence relating to R&D is currently found on many spectrum licences and was revised on February 19, 2014, as per Industry Canada’s decision document, SLPB-002-14 – *Decisions on Conditions of Licence Regarding Research and Development and Learning Plans*. The revised condition is as follows:

The licensee must invest, as a minimum, 2 percent of its adjusted gross revenues resulting from the use of this licence, averaged over the term of the licence, in eligible research and development activities related to telecommunications. Eligible research and development activities are those which meet the definition of scientific research and experimental development adopted in the *Income Tax Act*, as amended from time to time. Adjusted gross revenues are defined as total service revenues, less inter-carrier payments, bad debts, third party commissions, and provincial goods and services taxes collected. The licensee is exempt from research and development expenditure requirements if it, together with all affiliated licensees that are subject to the research and development condition of licence, has less than \$1 billion in annual gross operating revenues from the provision of wireless services in Canada, averaged over the term of the licence. For this condition of licence, an affiliate is defined as a person who controls the carrier, or who is controlled by the carrier or by any person who controls the carrier, as per subsection 35(3) of the *Telecommunications Act*.

Spectrum licences and their licence conditions can be viewed on the Spectrum Management and Telecommunication website at <http://www.ic.gc.ca/spectrum>.

⁴ See the *Telecommunications Act* at paragraph 7(g).

⁵ See the *Income Tax Act*, as amended (<http://laws-lois.justice.gc.ca/eng/acts/I-3.3/index.html>).

3. Definition of R&D

3.1 The Income Tax Act Definition of “Eligible” R&D

R&D activities must meet the definition of SR&ED as defined in the *Income Tax Act*⁶ in order to be eligible under the condition of licence. These activities may take the form of basic research, applied research or experimental development.

It should be noted that Industry Canada’s use of the *Income Tax Act* definition is for the purposes of the Department’s condition of licence related to R&D. In accepting the licensees’ reports on their R&D investments, Industry Canada is not making a determination that the Canada Revenue Agency (CRA) will accept these expenditures as eligible for tax deductions and/or tax credits for SR&ED. Licensees interested in ensuring that their investments in R&D are eligible for these tax deductions and/or tax credits should consult the provisions of the *Income Tax Act* and the *Income Tax Regulations* related to SR&ED.

3.2 Industry Canada and R&D

In addition to meeting the definition of eligible R&D activities as defined in the *Income Tax Act*, Industry Canada also requires that the R&D activities under the condition of licence be relating to telecommunications, as defined in the *Telecommunications Act*.

For the purposes of compliance with Industry Canada’s condition of licence relating to R&D, the type of expenditure is a material consideration, but where the R&D was performed is not relevant. To be deemed an investment for the purposes of compliance with Industry Canada’s condition of licence related to R&D, an expenditure must be a current expenditure of the type that would be taken into account by the CRA when assessing eligibility for a tax deduction and/or a tax credit for SR&ED.

3.3 Calculation of Revenues Resulting from the use of a Licence

The R&D condition of licence is attached to the licence itself, and not to the licensee. However, a licensee may choose to report on the aggregate of all of its licences. The licensee may also calculate and report on a licence-by-licence or on a frequency-band-by-frequency-band basis.

4. Reporting Process

4.1 Reporting Requirements Under the Radio Authorizations

Reporting requirements relating to investments made in R&D apply to certain spectrum licences and can be found in the licence conditions appended to these licences. All spectrum licensees must submit an

⁶ See the *Income Tax Act*, as amended (<http://laws-lois.justice.gc.ca/eng/acts/I-3.3/>).

annual report within 120 days of their fiscal year-end, for each year of the term of their licence, indicating continued compliance with all licence conditions. This annual report must include a statement of R&D expenditures, signed by a duly authorized officer of the licensee (e.g. Chief Financial Officer). R&D reports should provide a breakdown of R&D projects by method of investment and an indication of how much investment was made in each category. Industry Canada reserves the right to request an audited financial statement of R&D expenditures with an accompanying auditor's report. Licensees may share R&D facilities and allocate expenses accordingly, provided that an expense is only claimed by one licensee, and only one time.

The specific wording of reporting requirements may vary between satellite licences and spectrum licences. All licensees should refer to their conditions of licence for specific reporting requirements. Spectrum licences and their licence conditions can be viewed on the Spectrum Management and Telecommunications website at <http://www.ic.gc.ca/eic/site/smt-gst.nsf/eng/home>.

5. Transferred, Divided and Subordinated Spectrum Licences

Many spectrum licences are transferable and divisible. When a spectrum licence is transferred or divided, the condition of licence relating to R&D continues to apply for the remainder of the term of the licence. Licensees should refer to the conditions of licence for the specific obligations relating to transferability and divisibility.

Where research and development (R&D) requirements exist, the responsibility of being in compliance rests with the primary licensee for each licence. The adjusted gross revenue resulting from operations of the licence should include all payments to the primary licensee from the subordinate licensee. In any given year, "annual gross operating revenues from the provision of wireless services in Canada" for the purposes of determining the \$1 billion threshold shall include revenues from operations of all licences issued under the *Radiocommunication Act*, whether the licensees hold primary or subordinate spectrum licences, radio licences or other authorizations. The R&D investment made by the subordinate licensee can be counted towards the primary licensee's R&D requirement, and should be reported accordingly to Industry Canada.

The related Client Procedures Circular, CPC-2-1-23 — *Licensing Procedure for Spectrum Licences for Terrestrial Services* will be amended accordingly.