

**R&D Spending by Government:
Only One Instrument Works—Tax Credits;
Only One Sector Merits Targeting—
Environmental and Enabling Technologies;
Only One Sector Deserves Grants—Universities**

**BDO Dunwoody CEO/Business Leader Poll
by COMPAS for publication in
the *Financial Post* October 16, 2006**



**COMPAS Inc.
Public Opinion and Customer Research
October 16, 2006**

1.0 Introduction

The COMPAS CEO panelists have largely been on a metaphorical honeymoon with the Harper government, repeatedly crediting it with high performance and excellent intentions. R&D is an exception. R&D policy is one area where the Harper government earns only nominally higher performance scoring than its predecessor. Panelists seem concerned that the government is not embarking on a clearly different direction from its predecessors.

Members of the CEO and business leader panel were asked a multitude of questions about desirable policy instruments, desirable targets, and desirable policies. Only tax credits and tax relief earn plaudits though even R&D-targeted tax relief elicited some reservations from panelists, many of whom believe that across-the-board tax cuts are the fairest way of treating business. Grants, loans, venture capital investments and other instruments apart from taxation were seen as poor policies at best (governments are perceived as “poor” at identifying winners and losers) and susceptible to political corruption at worst.

Some concern was expressed about the need to clean up after the R&D record of the previous government. According to the President of a science-based company, “TPC [Technology Partnerships Canada] has an abysmal record, and rumours of corruption and former employees getting jobs with companies who dealt with TPC need to be investigated by the police. So far the Auditor General has not done the thorough audit required.”

CEOs and business leaders on the panel are uncomfortable with grants or loans to businesses though they are supportive of research and development grants to universities.

As for targeting support, the only type of research that merits targeting in their view involves environmental and enabling technologies.



These are the principal findings from the weekly business web-survey conducted by COMPAS for the *Financial Post* under sponsorship of BDO Dunwoody LLP.

2.0 Strong Desire for R&D Tax Relief, Targeting Environmental and Enabling Technologies, and Grants to Universities

Panelists were asked to indicate what kinds of research in general and pure research in particular should receive increased or decreased spending, as shown in tables 2A and B. With respect to policy instruments, respondents greatly prefer tax relief and tax credits over grants and subsidies, as shown in both tables.

Tax instruments are not seen as uniformly perfect. As one national business leader put it, “SR and ED tax credits do not work well in a number of industries. Credit for innovation as well as pure research needs to be provided. Grants work better if provided to non-profit organizations, where interested industries can pool their efforts. More flexibility is needed.”

Despite their imperfections, tax instruments are seen as both superior to grants and essential for the success of the Canadian economy. They are superior to grants because they are more immune to political influence and outright corruption. The previously quoted CEO has this to say about the Technology Partnerships program: “TPC has an abysmal record, and rumours of corruption and former employees getting jobs with companies who dealt with TPC need to be investigated by the police. So far the Auditor General has not done the thorough audit required.”

More than one panelist volunteered concern about distortions in the economy and high costs to taxpayers as a result of encouraging R&D through grants instead of tax relief. According to some respondents, Canada’s aerospace industry makes no economic sense in light of Canada’s small



military. Aerospace industries make good sense when large national investments in the air force allow technological discoveries for military purposes to be adapted to civilian purposes at a marginal cost, according to one CEO. According to another, the very existence of our aerospace industry is a testimony to raw politics. "In my opinion, Canada should not be in the aerospace industry; as a nation we are too small. The only reason it exists is that an already overburdened taxpayer is required to subsidize the politically well-connected in Quebec."

Several panelists emphasized the importance of tax relief for stimulating research and hence the economy. "Some R&D in unpopular/unprofitable sectors is essential for development of society toward far-reaching objectives, and must be encouraged by government intervention," volunteered a senior executive in professional services.

"Tax credits are the best way to encourage R&D expenditures," explained the head of a major engineering firm. "You have to be making a profit before a credit can be applied. This means that companies must be selective about what level of expenditures they can make for R&D purposes and still remain profitable." While favouring tax relief for R&D, this CEO nonetheless acknowledged a certain unfairness. "Grants to companies for doing R&D are fundamentally unfair for businesses that have little or no potential to do R&D, and therefore to benefit from the grants."

Several panelists emphasized the importance of R&D tax relief in specific and corporate tax relief in general at a time when manufacturing is going offshore and many countries are engaged in trade wars.

To the extent that respondents are comfortable with grants for pure research, they favour grants to universities rather than business, as shown in table 2B. To the extent that they are comfortable with targeting sectors for relief, they favour doing so in respect of environmental and enabling technologies, as shown in table 2A.



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*Table 2A: (Q2-3) Using a 7 point scale where 7 means increase
spending a lot and 1, decrease spending a lot, what should the
federal government be doing in each of the following general
situations?*

	Mean	7	6	5	4	3	2	1	DNK
Special tax relief or tax credits to businesses for research purposes (more than a billion)	4.8	12	21	27	17	7	6	3	7
Targeting specific <u>technologies</u> such as environmental or enabling technologies	4.8	11	30	24	13	7	7	7	2
Targeting individual <u>industries</u> like aerospace	3.8	4	11	18	26	17	10	12	2
Providing <u>venture capital</u> for private enterprise research	3.7	6	12	15	20	19	11	16	2
R&D grants and subsidies to businesses (hundreds of millions)	3.7	3	12	18	19	16	11	14	7

*Table 2B: (Q4) Governments subsidize pure or basic research.
Using the same 7 point scale, where 7 means increase spending
a lot and 1 means decrease spending a lot, what should the
federal government be doing in each of the following specific
situations involving pure research?*

	Mean	7	6	5	4	3	2	1	DNK
Tax credits to businesses doing pure research	4.8	11	23	30	18	7	7	3	2
Grants to academics for Pure research	4.5	10	15	25	23	17	6	3	2
Grants, loans, and subsidies to businesses for pure research	4.1	4	18	22	20	14	8	12	2



	Mean	7	6	5	4	3	2	1	DNK
Spending on pure research within the government	3.3	3	4	13	24	21	20	13	2

3.0. Two Camps—Free Market Fairness vs. *Real Politique*

Respondents were asked a series of questions about policies and principles in general, as shown in table 3A. Above all, panelists embrace a free market perspective. They are convinced that “politicians and public servants have poor records identifying the kinds of R&D or businesses that will grow and help the Canadian economy.” They also believe by a large margin that “low across-the-board taxes are the only fair and efficient way of stimulating the economy.”

Quite a number nonetheless acknowledge a *real politique* perspective that

- “in the real world, any Prime Minister is going to be subject to blackmail by companies threatening to move abroad if they don’t get grants or subsidies” and that
- “Canada must always be prepared to subsidize R&D by some businesses because of the subsidies given to their foreign competitors by foreign governments.”¹

Irrespective of their views on the substance of R&D policy, panelists tend to give the Harper government mediocre performance scores, as shown in table 3B.

¹ The elements of table 3 were dimensionalized using factor analysis. Two factors emerged—a dominant factor representing free market views and a secondary factor representing a *real politique* perspective.



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*Table 3A: (Q5) On a 7 point agree-disagree scale where 7 means
agree strongly and 1, disagree strongly, to what extent do you
agree with the following opinions?*

	Mean	7	6	5	4	3	2	1	DNK
Politicians and public servants have poor records identifying the kinds of R&D or businesses that will grow and help the Canadian economy	5.9	42	28	14	8	4	2	1	2
Low across-the-board taxes are the only fair and efficient way of stimulating the economy	5.4	32	23	18	13	4	8	2	1
Grants to businesses are a poor idea because grants favour the politically well connected	5.4	30	25	19	11	8	3	3	1
Tax credits are better than grants because they involve no politics	5.3	26	31	18	13	5	3	5	1
Grants and tax credits both favour companies with an aptitude for "red tape" over companies that just want to do business well	5.2	17	28	29	16	4	3	2	1
Grants are inherently unfair, which is evident by the phenomenon of repeated beneficiaries	5.0	22	19	18	19	8	7	3	4
In the real world, any Prime Minister is going to be subject to blackmail by companies threatening to move abroad if	4.9	17	17	34	17	7	3	4	2



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	Mean	7	6	5	4	3	2	1	DNK
they don't get grants or subsidies									
Canada must always be prepared to subsidize R&D by some businesses because of the subsidies given to their foreign competitors by foreign governments	4.7	11	23	21	23	12	3	5	3
Grants and tax credits increase the profits of the benefiting company but may not actually increase R&D activity	4.3	14	13	18	19	15	11	6	4

Table 3B: (Q1) The many hundreds of millions of dollars spent on R&D by the federal government have been subject to debate. On a 100 report card scale, what score would you give for...

	%
The previous Liberal government's performance in R&D spending	48
The present Conservative government's intentions on R&D spending	52

3.0 Methodology

The COMPAS web-survey of CEOs and leaders of small, medium, and large corporations was conducted October 11 - 13, 2006. Respondents constitute an essentially hand-picked panel with a higher numerical representation of small and medium-sized firms.



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Because of the small population of CEOs and business leaders from which the sample was drawn, the study can be considered more accurate than comparably sized general public studies. In studies of the general public, surveys of 126 are deemed accurate to within approximately 8.8 percentage points 19 times out of 20. The principal and co-investigator on this study are Conrad Winn, Ph.D. and Tamara Gottlieb.

