AN ALTERNATIVE FUNDING MODEL FOR AGRIBUSINESS RESEARCH IN CANADA

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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)

<table>
<thead>
<tr>
<th></th>
<th>Example 1 (35%)</th>
<th>Example 2 (55%)</th>
<th>Example 3 (69.5%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Taxable Income</td>
<td>300</td>
<td>300</td>
<td>300</td>
</tr>
<tr>
<td>Taxes Payable - CCPC rate 15%</td>
<td>45</td>
<td>45</td>
<td>45</td>
</tr>
<tr>
<td>Research Expenditure (RE)</td>
<td>200</td>
<td>200</td>
<td>200</td>
</tr>
<tr>
<td>Research Tax Credit (35%)</td>
<td>-70</td>
<td>-110</td>
<td>-139</td>
</tr>
<tr>
<td>Taxes Payable (refund)</td>
<td>-25</td>
<td>-65</td>
<td>-94</td>
</tr>
<tr>
<td>Net Research Expenditure (NRE)</td>
<td>130</td>
<td>90</td>
<td>61</td>
</tr>
<tr>
<td>50/50 funding research Impact (RE x 2)/NRE</td>
<td>3.08 times</td>
<td>4.44 times</td>
<td>6.56 times</td>
</tr>
<tr>
<td>Portion of Research paid by CCPC</td>
<td>32.50%</td>
<td>22.50%</td>
<td>15.25%</td>
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</tbody>
</table>
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 ½ the rate, if a CCPC taxed at 7.5%, (if not trading for gain)

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

**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.
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?