

Venture Capital Tax Credit Program

Scale-Up Qualifying Activity

Policy Statement
Small Business Venture Capital Regulation
Sections: 1 (1); 11 (1)(h); 11(2.3) and 11(3)
Up-dated: January 25, 2022

INTRODUCTION

Budget 2019 introduced several changes to the Small Business Venture Capital Act (Act) to bring the program up to date with current investment practices and the business operations of venture capital backed technology-based start-ups. One change was the addition of a qualifying activity called “scale-up activity”.

“Scale-up activity” is defined under section 1(1) of the SBVC regulation as activities related to the expansion of a business, including the following activities:

- Customer acquisition;
- Brand building; and
- Development of sales brochures, website content and other marketing collateral to promote the business’s products and services.

CRITERION FOR SCALE-UP

Eligible Business Corporations

Eligible Business Corporations (EBCs) are eligible for the scale-up qualifying activity if:

- 2 years has elapsed since the EBC first raised tax credit supported investment; and
- for the previous 2 years the EBC has been “substantially engaged” (see description below) in one or more qualifying activities.

Eligible Small Businesses and Venture Capital Corporation Investment

Eligible Small Businesses (ESBs) are eligible for the scale-up activity if:

- 2 years has elapsed since the ESB first received an eligible investment from a Venture Capital Corporation (VCC); and
- for the previous 2 years the ESB has been “substantially engaged” (see description below) in one or more qualifying activities.

Scale-up activity was added to the list of qualifying business activities to enable EBCs/ESBs to raise tax credit supported investment for marketing and customer

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acquisition activities after the EBC/ESB had first been in one or more other qualifying activities such as manufacturing/processing goods or developing a technology. As the objective of the VC Tax Credit Program is to encourage the development of manufacturing and technology-based businesses in BC, the 2-year requirement prevents businesses joining the VC Tax Credit program and immediately raising funds for marketing activities.

Scale-up is not an eligible qualifying activity at the time of EBC registration.

Substantial Engagement in a Qualifying Activity

Subject to section 28.2 of the Act, an EBC must be substantially engaged in one or more qualifying activities described in section 11 (a) to (h) of the regulation, from the time of registration until 5 years after the date of the last tax credit supported investment.

An ESB must be substantially engaged in one or more of the qualifying activities described section 11 (a) to (h) of the regulation, from the time a VCC makes an eligible investment in the ESB until the VCC has held the investment for 5 years.

Qualifying activities are:

- (a) Manufacturing and processing of goods produced BC.
- (b) Destination tourist resort, tourist attraction or tourist service.
- (c) R&D of proprietary technology produced in BC.
- (d) Development of an interactive digital media product in BC.
- (e) R&D and/or manufacturing and processing of clean technology goods produced in BC
- (f) Advanced commercialization carried on by a business outside Metro-Vancouver and the Capital Regional District.
- (g) Community diversification (all of the above qualifying activities; and non-traditional agriculture; and retail and commercial services that promote community diversification within a region).

To be substantially engaged in a qualifying activity, an EBC/ESB must have more than 50% of its assets and expenses engaged in the one or more qualifying activities. The formula for determining substantial engagement is outlined in section 11(3) of the regulation and is as follows:

Activity Assets + Activity Expenses

Total Assets + Total Expenses

Where,

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Activity Assets = the value of assets of the small business used in British Columbia in the business activity,

Total Assets = the total value of all assets of the small business,

Activity Expenses = all expenses incurred during the calculation period with respect to the portion of the business activity carried on in British Columbia, and

Total Expenses = the total of all expenses incurred during the calculation period with respect to all operations of the small business

Any assets, including scale-up activity assets, that are located outside British Columbia, and any expenses, including scale-up activity expenses (see qualifying and non-qualifying scale-up expenses below), that are incurred outside British Columbia and not used in one or more qualifying activities carried on in the province are not “activity assets and activity expenses”.

SCENARIOS

Example 1:

Scenario

- An EBC was registered in the program on December 15, 2019 and has been substantially engaged in a qualifying activity from the date of registration.
- The EBC is in good standing and in compliance with the Act.
- The EBC first raised tax credit supported investment on March 30, 2020.

Result

- The EBC is eligible for the “scale-up” activity from March 30, 2022. Even though the EBC was registered in the program on December 15, 2019, and 2 years have elapsed since the EBC was registered, it did not raise tax credit supported investment under the program until March 30, 2020.

Example 2:

Scenario

- An EBC was registered in the program on October 10, 2019, and has been substantially engaged in the qualifying activity of R&D of proprietary technology from the date of registration (over 50% of assets/expenses have been applied to R&D in BC)
- The EBC first raised tax credit supported investment on December 2, 2019.
- From March 31, 2022, the EBC has primarily completed its R&D activities and is now planning to expand its operations including acquiring customers, building its brand, and marketing its products.
- The EBC is in good standing and in compliance with the Act.

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- From March 31, 2022
 - 20% of the EBC's assets and expenses are qualifying and applied to R&D
 - 60% of the EBC's assets and expenses are qualifying and applied to Scale-up
 - 20% of the EBC's assets and expenses are non-qualifying

Result

- The EBC is eligible for the "scale-up" activity from December 2, 2021, as more than 2 years has elapsed since it was registered in the program, it has been substantially engaged in a qualifying activity for the last 2 years, and 2 years has elapsed since it first raised tax credit supported investment.
- As at March 31, 2020, the EBC is 80% engaged in the qualifying activities of R&D of proprietary technology (20%) and Scale-up (60%)

QUALIFYING AND NON-QUALIFYING SCALE-UP EXPENSES

Qualifying Scale-Up Expenses

Tax credit supported investment can be applied to the following qualifying scale-up expenses:

- Advertising.
- Advertising agency services and commissions (BC).
- Attending trade shows to demonstrate an EBC's product or technology.
- Brand design and brand development (BC).
- Costs for recruiting/training sales agents.
- Customer surveys.
- Customer product/technology support.
- Demonstrating a product or technology to potential customers.
- Development of advertising and promotion materials (BC).
- Domain name costs.
- Marketing consultancy services (BC).
- Marketing automation tools and analytics (the activity of using tools/analytics must be BC-based – the tools/analytics can be on-line outside BC).
- Marketing wages/salaries*.
- On-line advertising.
- Operating and demonstrating a prototype.
- Demonstrating a technology to equipment manufacturers.
- Printed marketing materials and displays.
- Social media monitoring and participation (BC).
- Trade shows and event attendance.
- Travel expenses to attend trade shows/meet potential customers.
- Video development to promote a product or technology.

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- Website design, website content management and file management (BC).

(BC) denotes that the expense must be incurred in BC to qualify as an activity expense. Other expenses can be incurred outside BC as long as they support the business being carried on in BC.

*Small Businesses engaged in the export of goods from BC or in the provision of services outside BC can reduce the percentage of wages and salaries of those reporting to work in BC from 75% to more than 50%.

Services that are directly associated with the export of manufactured goods can be included as an “Activity Expense”. These expenses include:

- Shipping and forwarding costs.
- Warehousing/distribution costs.
- Installation and maintenance costs to install equipment in a non-BC location.
- Inspection and permitting costs for installation of equipment in a non-BC location.

Non-Qualifying Scale-Up Expenses

Tax Credit supported investment cannot be applied to the following expenses:

- Feasibility studies; studies identifying new markets and new products; and site selection.
- Business development costs (e.g., costs associated with building customer relationships; networking, cultivating partnerships, strategic relationships and relationship building; and prospecting).
- Direct sales.
- Gifts, samples and contributions to customers and others.
- Sponsorships.
- Multi-level marketing, pyramid selling, network marketing or other forms of referral marketing.
- Public relations.
- Sales commissions to third party sellers/marketers.
- Operation of a call centre.
- Proposal development and submitting bids.