



Canada's Response to the U.S. One Big Beautiful Bill Act

# Levelling the Playing Field: What's Needed

JULY 24, 2025



# Overview

On June 26, 2025, the Toronto Region Board of Trade (the “Board”) released [a policy brief](#) analyzing a sweeping U.S. tax reform package that, at the time, included provisions with potentially significant implications for Canada’s investment climate, manufacturing base, and innovation economy.

The reform, officially titled the One Big Beautiful Bill Act (OBBBA), has since become law, following its passage by the U.S. Congress on July 3rd, and subsequent signing by President Donald Trump on July 4th, 2025.

This policy brief outlines some of the key sections of OBBBA that could affect Canada’s economic position, as the United States (U.S.) intensifies efforts to attract capital, Research and Development (R&D) and industrial activity through aggressive tax policy.

Most importantly, with a final text of the Act now in place, it marks a turning point in the U.S. tax policy while also raising an urgent conversation about how Canada can compete for investment and innovation-driven growth in this new landscape.

## **AS A RESPONSE, THE BOARD RECOMMENDS THAT THE FEDERAL GOVERNMENT CONSIDER THE FOLLOWING POLICY LEVERS:**

- 1 Full expensing for capital investment
- 2 A domestic production reduction tax rate
- 3 More competitive business incentives for spending on R&D
- 4 A patent box regime





# Full expensing of qualified assets and R&D expenditures

**SECTION 70301** makes 100% bonus depreciation a permanent feature of the U.S. tax code. It now allows businesses to fully deduct the cost of eligible equipment, machinery, and certain building improvements in the year they are placed in service, rather than spreading the deduction over several years.

Previously, this bonus depreciation was set to phase out gradually by 2027. OBBBA removes that phase-out and locks in full expensing for qualified property placed in service after December 31, 2022.

**SECTION 70302** restores the ability for U.S. businesses to fully deduct the cost of domestic R&D expenditures in the year they are incurred. This section removes the previous requirements that mandated businesses to spread these costs over five years for U.S.-based R&D or fifteen years for foreign R&D.

This incentive now applies retroactively to tax years beginning after December 31, 2021.

## WHAT ARE THE BENEFITS OF THESE TAX CHANGES FOR U.S. COMPANIES?



### They reward investment upfront

It means businesses can now receive the full tax benefit from their investments right away, eliminating the need to wait years to recover those costs through depreciation or amortization.



### They improve cash flow for businesses

When companies can deduct major expenses in the year the costs are incurred rather than spreading deductions over multiple years, it reduces a company's taxable income for that year—lowering the amount of taxes owed.



### They support innovation activities

Immediate deductions free up cash for more R&D and make it easier to invest in tools needed to develop and test new technologies.

# A carrot-and-stick approach to taxation of foreign and export-related income

Two provisions introduced in the 2017 Tax Cuts and Jobs Act (TCJA) were amended under OBBBA, effectively counteracting the impending increases in effective scheduled tax rates to support the retention of intangible assets within the U.S.

**The Foreign-Derived Intangible Income (FDII) and Global Intangible Low-Taxed Income (GILTI)** provisions are designed to work together to shape where companies base their operations and report income. FDII acts as a “carrot” by offering a lower tax rate on income from exports tied to U.S.-based intangible assets, encouraging companies to keep innovation and sales in the U.S. GILTI serves as the “stick” by imposing a minimum tax on income earned through low-tax foreign subsidiaries, discouraging companies from shifting profits offshore.

Under the TCJA, the FDII deduction was set at 37.5% resulting in an effective tax rate of 13.125%. However, this deduction was scheduled to decrease to 21.8% after December 31, 2025, which would have elevated the effective tax rate to 16.4%. OBBBA adjusted the FDII deduction to **36.5%** for taxable years beginning after December 31, 2025. This change results in an effective tax rate of **~13.3%**, preserving a more favourable tax environment for U.S. exporters of goods and services linked to domestic intangible assets.

Similarly, GILTI deductions under the TCJA were set at 50%, yielding an effective tax rate of 10.5%. This deduction was slated to decline to 37.5% post-2025, which would have raised the effective tax rate to 13.1%. OBBBA amended this provision by setting the GILTI deduction at **49.2%** for taxable years beginning after December 31, 2025, resulting in an effective tax rate of **~10.6%**.

## What are the benefits of this tax approach?



### Lower tax rates

when they sell goods or services to other countries using assets (e.g., patents or software) based in the U.S.



### A tax break

on export income tied to U.S. activities, making it more appealing to keep innovation and technology development in the U.S. instead of moving it abroad.



### A reward-driven environment

for keeping business in the U.S., while also making sure that the U.S. still gets tax money from global profits.

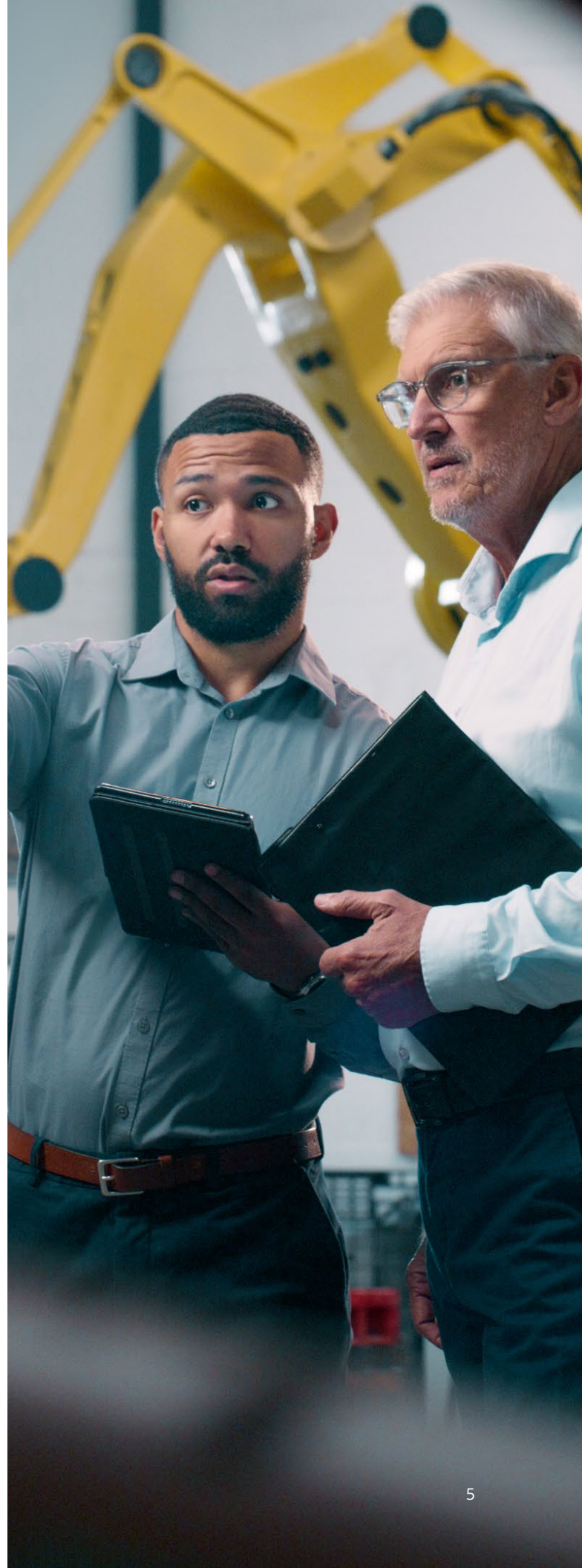


# How does Canada level the playing field?

With the U.S. now allowing full expensing of capital investments and offering generous, faster tax relief for domestic R&D, Canada must ask: where do we go from here?

While these conversations are not new to industrial policy, this is a pivotal moment that calls for a reassessment of our approach. The U.S. is taking deliberate, strategic steps to expand its manufacturing base and anchor innovation within its borders. In this context, Ottawa must view the evolving U.S. tax landscape as a clear call to action. Recent U.S. reforms raise an important question about whether Canada's current tax and investment incentives are sufficiently competitive to attract and retain capital and intellectual property.

Although this is part of a broader industrial policy strategy debate, the following section provides an overview of key policy levers Canada could consider in response to a more competitive U.S. tax environment and spotlights an opportunity to revisit measures previously explored but never permanently adopted.



## 1. INTRODUCE FULL EXPENSING FOR CAPITAL INVESTMENTS

Canadian businesses use the [Capital Cost Allowance \(CCA\) system](#) to deduct the cost of long-term assets gradually over time. This depreciation approach aligns the deduction with the asset's useful life and the revenue it helps generate, rather than allowing the full expense to be claimed in the year of purchase. Several categories determine the class of an asset under the CCA system, which determines the effective rate to the remaining undepreciated balance each year, not the original cost.

A key provision of the CCA system is the “half-year rule”, which limits the amount of depreciation a business can claim to only 50% of the asset's value. For example, if a business buys a machine for \$100,000 and the CCA effective rate is 20%, the first-year deduction without the half-year rule would be \$20,000. However, with the half-year rule, only half of the asset's value (\$50,000) is used for calculating CCA in the first year, so the deduction would be \$10,000 instead.

In 2018, the federal government introduced the [Accelerated Investment Incentive \(AII\)](#) to allow businesses to claim up to one-and-a-half times the net addition to a CCA class and suspend the half-year rule. However, this incentive is being phased out for property available for use after 2023. As a result, businesses are returning to slower depreciation schedules and spreading deductions over many years.

### What are the benefits of this tax approach?



#### Slow recovery of investment costs

When businesses are required to deduct the cost of capital assets gradually over extended periods of time, it delays tax relief, reduces near-term cash flow and increases the after-tax cost of investment.



#### The CCA system is fragmented

The system has dozens of CCA classes, each with its own rate and eligibility criteria. This creates compliance burdens and administrative complexity.



#### No full expensing option

Canada does not offer full expensing of the entire cost of capital assets in the year of purchase (with rare, temporary exceptions under the AII).

### Recommendations:

In light of the U.S.'s adoption of permanent full expensing for capital investments, Canada faces increased pressure to enhance its tax competitiveness. To implement full expensing, the federal government would need to:

- Amend the income tax regulations to allow businesses to immediately deduct the full cost of eligible capital assets, such as manufacturing equipment and supply-chain moving capital assets, in the year of acquisition.
- Provide clear definitions of eligible assets and sectors to ensure the measures effectively target areas where investment stimulation is most needed.

## 2. INTRODUCE A DOMESTIC PRODUCTION REDUCTION TAX RATE

To remain competitive in an era marked by dynamic incentives in other jurisdictions, Canada should strongly consider introducing a domestic production reduction to lower the combined federal-provincial effective corporate tax rate for manufacturers. Without a policy response that provides comparable, sustained relief, Canada risks losing high-value investment, weakening its ability to scale strategic industries such as advanced manufacturing, life sciences, clean technologies, and semiconductors.

In Ontario, the combined corporate tax rate stands at **~26%**, which applies to active business income earned by corporations that do not qualify for deductions. In fact, Preferential tax treatments exclude larger, growth-stage firms—the very companies that must scale capital investment to build Canada’s industrial capacity.

According to [2024 data from the Tax Foundation](#), Canada’s combined rate places it among the highest in the G7, ranking just below Germany (29.9%) and Japan (29.7%), and above global trends. Over the past decade, many economies have trended toward corporate tax rates in the 20%–25% range. A well-structured domestic production reduction could help bring Canada’s effective rate within that range, offering a targeted reduction of **1.5 to 6 percentage points** for companies with significant domestic production activities.

### Recommendations:



**Make the deduction available to all corporations** with manufacturing or production activity, not limited to a single sector.



**Structure the tax rate as a percentage of production profits** derived from domestic activities, to make the incentive measurable to manage.



**Set clear eligibility conditions tied to economic impact**, such as maintaining a minimum level of capital investment and employment numbers.



**Enable the deduction to be partially refundable or transferable** to allow scaling or pre-profit firms to benefit before reaching profitability.



### 3. STRENGTHEN CANADA'S BUSINESS INCENTIVES FOR BUSINESS SPENDING IN R&D

Canada's Scientific Research and Experimental Development (SR&ED) 35% tax credit has long been the country's flagship tool for incentivizing private-sector R&D. However, the incentive faces several challenges that limit its effectiveness:

- **High compliance burden and lengthy claim preparation process:** The complexity of eligibility criteria makes it difficult for companies without in-house tax expertise to navigate the system. This can result in significant time and resource demands, a significant barrier for many companies, discouraging them from claiming and/or increasing the likelihood of errors in preparing claims.
- **Narrow eligibility criteria:** The SR&ED's definitions of eligible activities are rooted in traditional models of scientific inquiry and experimental development, which often do not reflect the realities of modern R&D. As a result, innovative work in fields such as artificial intelligence (AI) and machine learning may not qualify, even when it involves significant technical uncertainty and investment.
- **No focus on commercialization:** Unlike other countries that offer incentives tied to the commercialization of intellectual property (IP), SR&ED primarily focused on R&D expenditures without directly encouraging the retention and commercialization of high-value assets within the country.
- **Regulatory uncertainty:** The SR&ED guidelines are frequently updated to reflect shifting government priorities and fiscal evaluations. However, for innovation-driven industries that rely on a stable and predictable R&D investment environment, these ongoing changes introduce uncertainty that can hinder the planning and execution of long-term projects.





## Recent efforts to enhance SR&ED

In the [2024 Fall Economic Statement](#), following extensive consultations, the federal government announced significant enhancements to the SR&ED. Key changes include increasing the expenditure limit for the enhanced 35% refundable credit from \$3M to \$4.5M, raising the taxable capital phase-out thresholds to \$15-\$75M (before: \$10M-\$50M), extending the enhanced credit to eligible Canadian public corporations and reinstating the eligibility for property acquired on or after December 16, 2024.

These changes provide sustainable, non-dilutive funding opportunities that enable longer-term reinvestment in Canadian-based R&D. They represent an advantage for both businesses currently claiming SR&ED and those that were previously ineligible but now qualify. Overall, this marks a positive step forward in supporting a more robust tax-friendly innovation landscape for Canadian businesses.

The newly elected federal government has the opportunity to reaffirm its commitment to innovation by implementing the SR&ED reforms announced in 2024. Although the legislation has not yet passed, these measures were the result of broad-based, extensive consultations, reflected stakeholder consensus and outlined targeted enhancements needed to modernize Canada's R&D incentive framework.

*Note: the legislation for the SR&ED changes is not yet available, and the proposal is subject to change as it has not been passed into law. With the prorogation of Parliament until March 24, 2025, and a new elected federal government on April 28, 2025, further details remain pending.*

## Recommendations:



### **Introduce legislation to implement the SR&ED reforms announced in 2024:**

These long-awaited measures lay out targeted enhancements to modernize the incentive and ensure it resonates with industry and its current needs.



### **Introduce a commercialization**

**bonus:** As the tax incentive only rewards R&D spending, not downstream commercialization, the federal government could add a 'bonus' that offers an additional tax credit on profits from products or services developed and held in Canada.



### **Introduce an export-linked SR&ED enhancement:**

An incentive that provides an additional refundable tax credit to firms that earn a significant portion of their revenue from international markets, contingent on that revenue being tied to Canadian IP. This would reward firms that successfully scale from Canada, align with trade diversification goals, and encourage retention of high-value functions domestically.



**Modernize eligibility definitions:** The SR&ED definitions are still grounded in traditional R&D models, which call for a review and modifications of current definitions and ensure that modern R&D activities are eligible for the tax credit.



## 4. INTRODUCE A PATENT BOX REGIME

Canada has long celebrated its robust research capabilities, highly skilled workforce and world-class technology breakthroughs. However, it is no longer surprising when the commercial value of those assets is captured by foreign markets. [According to the World Bank's World Development Indicators and Finance Canada Calculations](#), Canada has consistently posted a net deficit in payments for the use of IP in contrast to peer jurisdictions over the last two decades. In practical terms, this means Canadian businesses pay more to use foreign IP than they earn from licensing their own IP abroad.

This persistent deficit highlights a deeper economic challenge: While Canada excels at generating innovative ideas, other countries are often the ones to scale, profit from and ultimately, take ownership of Canadian innovation. **[In the 21st-century economy, the question is no longer whether Canada should address this problem. The real question is how.](#)**

Canada has long considered a patent box regime to anchor IP-generated profits at home. A patent box applies a preferential tax rate to income derived from intellectual property, encouraging companies to scale their innovations domestically. While Canada's SR&ED program reduces the cost of R&D, the patent box rewards its results. These tools could be complementary, supporting the full innovation cycle: ideation, experimentation, validation, and commercialization. As noted earlier, SR&ED support ends once the IP is developed. There is no incentive for domestic firms to scale, manufacture or market their IP in Canada. **[Here lies the paradox: we subsidize discovery, yet make delivery elsewhere the more lucrative choice.](#)**



WHAT'S HOLDING BACK CANADA'S PATENT BOX?

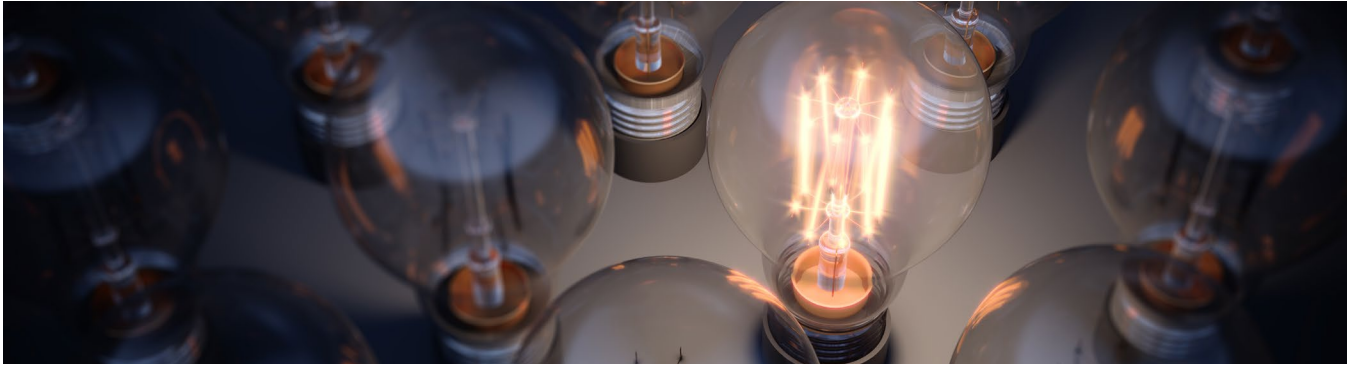
Several countries globally have already introduced patent box regimes. For instance, 13 of the 27 EU member states have set a regime ranging from 4.5% (Hungary) to 10.5% (Portugal). In the U.S., the preferential rate for IP income is 13.3% (determined by the OBBBA's amendment to the FDII). Ireland's Knowledge Development Box allows for a 6.25% rate for profits derived from patented or similar protected inventions or copyrighted software, which was introduced to enhance the country's offering as an IP location alongside a 12% corporate tax rate, R&D tax credits and an amortization regime. Across these examples, one result stands out: when countries offer tax advantages for locally developed and commercialized IP, they can retain the economic returns of R&D and create stronger innovation ecosystems.

**What steps, if any, has the federal government taken to implement a comparable regime in Canada?** Since 2018, the government has discussed, evaluated and socialized broadly the idea of protecting and advancing the commercialization of IP, including a patent box regime—yet efforts have translated into minimal or no action.

With an investment of \$85.3 million over five years, Canada's National Intellectual Property Strategy focused on areas that can help Canadian businesses to understand, protect and access IP. These areas include IP Awareness, education and advice, tools for businesses to develop their IP strategy, and IP legislation amendments such as minimum requirements for patent demand letters, patent research exemptions and many others. No tax incentive was introduced to accelerate commercialization.

In 2021, the Strategic Intellectual Property Program Review was first announced with further support from Budget 2022. In the same Budget, the federal government committed to \$100 million to adopt a patent box regime. The Program Review entailed examining how Innovation, Science and Economic Development Canada's (ISED) programs develop and commercialize IP. Examples of those programs included the Strategic Innovation Fund, Innovative Solutions Canada, Global Innovation Clusters, and the National Research Council of Canada's Industrial Research Assistance Program, among many others. The following year, ISED conducted this review by hosting several focus groups with experts and program beneficiaries. No public record was found on the results of the study, nor evidence of how the review concluded on the need for financial incentives beyond operational programming.





In 2024, the Department of Finance Canada conducted [consultations](#) on “the suitability of creating a patent box regime,” which resulted in the announcement of an ‘intention’ to implement it in the [2024 Fall Economic Statement](#). The previous federal government committed to announcing further details in Budget 2025, which aligns with the current government’s [political agenda](#). In conclusion, many promises and millions of dollars allocated to “explore” ideas yet to be unveiled, which, in the end, recognize the value of a much-needed patent box.

#### FACTORS INFLUENCING THE IMPLEMENTATION OF A PATENT BOX REGIME

- 1 Fiscal caution
- 2 Political tradition and technical design
- 3 Intergovernmental coordination
- 4 Shifting government priorities

Many factors explain the hesitation. First, there are fiscal concerns. A patent box offers a preferential tax rate on corporate income, which the government could view as an expense.

In a climate of budget constraints, particularly during the COVID-19 pandemic and post-pandemic recovery periods, the idea of introducing a new corporate tax break faced resistance given other more ‘pressing’ concerns (e.g., immediate financial assistance for reopening). Second, Canada has historically favored upfront incentives for R&D and shifting to a patent box regime requires a change in mindset and policy to avoid overlaps or duplications. Third, federal-provincial coordination has been a barrier. Corporate income tax is shared across levels of government. If only the federal government reduces its tax rate on IP income, the overall rate could still be too high to be globally competitive. A truly effective regime requires provincial engagement and alignment to build a harmonized federal-provincial model.

Lastly, timing and priorities have played a role. In recent years, the federal government has prioritized other innovation strategies like the [Global Innovation Clusters](#). In sum, fiscal caution, policy tradition, technical design, intergovernmental coordination and shifting government priorities have all contributed to Canada’s lack of a patent box regime. Despite multiple signals of intent, no action is currently in place, leaving Canada behind jurisdictions that already use this tool to retain and grow IP-driven business.



## WHY IT'S CRITICAL FOR CANADA TO ACT NOW

The global landscape for innovation investment has grown fiercely competitive, and Canada risks falling further behind if it does not move promptly. Reasons why action is imperative now include:

- **U.S. Tax pressure is intensifying:** As discussed, the U.S. FDII and GILTI regimes have already put Canada at a competitive disadvantage for attracting and retaining IP since 2018. Now with the OBBBA amending the regimes and maintaining the tax incentives, the longer Canada waits, the more investment could be siphoned off to the south.
- **Canada's innovation ecosystem is losing ground:** The net deficit in IP royalties and license payments in Canada has widened over time, signalling the need to finally make it financially competitive to commercialize IP here. Continuing the status quo will perpetuate the narrative of seeing Canadian investors and startups creating valuable IP, but larger foreign companies acquiring it.
- **Peer jurisdictions have already done it:** Canada is one of the few advanced economies without some form of IP incentive regime. It is clear how those economies are winning the race for investment, innovation and economic growth—highly powered by IP commercialization.

### Recommendation:

Canada has the opportunity in Budget 2025 to finally deliver on years of commitment and business community advocacy. With implementation no later than 2026, the federal government should introduce legislation for a national patent box regime grounded in the substantial consultations and evaluations that have built the case and the momentum to act. An additional framework that could guide this initiative is the [OECD Nexus Approach](#), a key rule that outlines how countries can use patent box regimes to encourage R&D, foster growth and foster growth and employment. This rule would ensure that Canada's patent box is globally accepted and trade-compliant.





The Toronto Region Board of Trade is one of the largest and most influential chambers of commerce in North America and is a catalyst for the region's economic growth agenda. Backed by more than 11,500 members, we pursue policy change to drive the growth and competitiveness of the Toronto region, and facilitate market opportunities with programs, partnerships and connections to help our members succeed – domestically and internationally.

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