Centre for Productivity and Prosperity
Walter J. Somers Foundation
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INNOVATION: SOLUTIONS TO ADDRESS QUEBEC'S LAGGING PERFORMANCE

Montréal, March 20, 2017 – As the Quebec government prepares to launch a new strategy to stimulate innovation, the HEC Montréal Centre for Productivity and Prosperity – Walter J. Somers Foundation (CPP) has released a study criticizing the ineffectiveness of the policies adopted to date and offering some suggested reforms.

In its report, the CPP explains why Quebec firms have fallen so far behind in terms of research and development (R&D) and proposes some concrete solutions to encourage innovation. "This study shows not only that the huge amounts invested by the Quebec government in innovation for years now have not borne fruit, but also that they have mainly gone to large companies," explains CPP Director Robert Gagné. "Although small and medium-sized enterprises represent 98% of the province's economic fabric, only 1.7% of them claim R&D credits." Since 80% of the money spent every year by the Quebec government to support innovation takes the form of fiscal assistance, it is clear that SMEs, despite their great ability to generate innovation, are not getting the most out of this support.

The conclusion is clear: the Quebec government needs to thoroughly re-examine the way it supports businesses, rather than simply taking more measures without validating their actual impact.

Some recommendations

To reverse this trend and make government actions more effective, the CPP's researchers offer five recommendations:

1) First of all, the Quebec government should take a project-oriented approach to supporting R&D by large companies. Rather than systematically offering funding once they meet the eligibility criteria for R&D tax credits, the government would achieve better results by selecting which projects it wants to support ahead of time. Then it could validate the effectiveness of its support and withdraw the funding if the objectives were not met. "At present, the government's strategy appears to favour large companies," emphasizes Gagné. "Not only because their projects are larger in scope, but also because they have the expertise and resources necessary to claim the R&D credits. The result is that fewer than 500 companies account for nearly 40% of the amounts allocated to R&D credits, but in the end the government is limited in its ability to validate the actual effectiveness of this support."

2) Even though R&D credits have proven increasingly less effective as a way of encouraging R&D by SMEs, the government should keep them in order to maintain parity with other provinces. These credits should be offered only to SMEs, however, and the eligibility criteria should be made more stringent. The rates – currently the most generous in Canada – could remain the same, but the credits should no longer be fully refundable or ongoing. The government would then be spared the expense of funding recurring and relatively unpromising R&D activities.

3) Since only 1.7% of SMEs claim R&D credits, the government should make sure that the other 98.3% also receive support. Rather than opting again for an approach based on income tax credits as a way of reducing the tax burden on a limited number of SMEs, the government should act "upstream" by eliminating the payroll taxes systematically levied on Quebec SMEs. This would allow it to reach as many SMEs as possible, giving them the cash they need to finance innovation activities that might not be recognized as such under the official definition: investing in ICTs, modernizing production, acquiring patents or licences, etc.

4) While the manufacturing sector has always been the motor of R&D in Quebec, the government should specifically address the competitiveness of manufacturing SMEs, first of all to help them better face foreign competition, but also to ensure that they remain true drivers of innovation in the province. To effectively stimulate innovation by these firms, the government should combine all the credits now available so as to refocus the assistance on investment that boosts and supports their competitiveness: purchasing technology and processes developed by third parties, investing in ICTs, modernizing production, etc. With the R&D credit, manufacturing SMEs would thus have two measures encouraging them to innovate, whether their activities are in the form of local R&D or investment aimed at improving production efficiency.

5) Overall, the government should carry out an in-depth review of its programs, measures, policies, strategies and agencies devoted to innovation. "Rather than trying to circumvent the problem of accumulating different layers of assistance by creating a platform like QuébecInnove, intended merely to simplify access to services, the government should systematically examine the effectiveness of its actions and the organizations it is funding," concludes Gagné. "This kind of periodic review would make it possible to focus assistance on the most promising measures."

For more information:
- Consult the report (in French), entitled *Des solutions pour stimuler l'innovation au Québec.*
- Téléchargez le communiqué en français.

About the Centre for Productivity and Prosperity – Walter J. Somers Foundation
The HEC Montréal Centre for Productivity and Prosperity – Walter J. Somers Foundation, created in 2009, has a twofold mission. First of all, it is devoted to research on productivity and prosperity, mainly in Quebec and in Canada as a whole. The Centre then shares its research findings, making them widely accessible and, in the end, educating people about productivity and prosperity.
For more information on the Centre, visit http://cpp.hec.ca/en/**.**

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