Mario Piccinin and Lara Iob, Life Science Partners, Ernst & Young Canada

07.10.2013

Tags: Ernst & Young LLP, EY Canada, Life Sciences, R&D, SR&ED, Venture Capitalist, Biotech

Mario Piccinin and Lara Iob of EY Canada discuss some of the key trends of the country's biotech industry and the affiliate's dedication to helping clients navigate the SR&ED tax credit process available in Canada.

What do you see as the biggest challenges of life sciences clients in Canada today?

LI: In recent years, the big challenge in Canada, particularly for biotech companies, has been funding. According to statistics, we have not had any IPOs in this industry for the last five years. The level of traditional funding from venture capitalists has consistently been at a lower level. As a result of less financing, the last few years have been really focused on efficiency, doing things differently, and accomplishing more with less. While there are many well-established public companies, the smaller companies and private companies represent the biggest population of businesses in Canada, and they have been more selective about programs to which they will devote the majority of their resources. Many of these newly created companies or start-ups are referred to as virtual companies, in which a few employees focus and develop on one or two very strict programs. Virtual companies have become more popular, which transcends what we have been seeing consistently with larger companies, who have also been cutting back on R&D and outsourcing more.

MP: We have seen a 12 percent decrease in R&D spending compared to 2011, following a four percent decrease from the year before. That is troubling because R&D is the lifeblood of the industry. Furthermore, venture capital spending was down 60 percent last year in Canada. Not having that R&D spend in Canada reduces the potential for future commercialized products.

Canada needs to step up its innovation game, but at the same time that can bring increased complexity that can lead to less productivity and innovation. How can companies find their way out of this paradox?

MP: We have excellent science and research in Canada. The problem is moving the science from the lab or university to commercialization. With respect to tax incentives, the well-established SR&ED programs of Quebec and Ontario are based primarily on basic research. While this provides tremendous research, there are fewer incentives for taking research to commercialization. On the federal level, there needs to be more incentives, such as flow-through shares, which are allowed in mining but not life sciences.

LI: Companies are certainly working differently, but their counterparts are also starting to work differently. Some venture capital funds are teaming up more with big pharma. Everyone is trying to find different ways to create the bridge between science and business, and one example is the adoption of incubators or partnerships with research organizations.

MP: The industry needs to do more to break down silos. There is more open-source research, in which early-stage research and information is shared, and this does take some risk out of the process.

Are there specific aspects of Quebec and Ontario that put those two provinces ahead of the rest of the country?

LI: Quebec has always been very strong in terms of its own tax incentives and the amounts you can receive as well as the fact that they are refundable. The actual fact that you can get a check in cash back forms part of many small biotech companies’ funding, and significantly helps with cash flow. That has always been a key part of companies setting up shop in Quebec and why there are Canadian counterparts of larger companies that want to be in Canada.

MP: The research work has to be done in Canada to be able to apply for SR&ED credits. EY has been involved in helping companies obtain these credits since the early days of the industry. I call it non-dilutive financing. If you receive 30 percent cash back, that is a big funding source and it really helps the company's cash flow.

What are the biggest challenges associated with EY Canada's sectors (pharmaceuticals, biotech, medical devices) in terms of how you adapt to the needs of individual clients?

LI: The pharmaceutical industry is currently trying to deal with their patent cliffs and pipelines. Achieving growth and continuing to show a positive profit and bottom line has been a challenge for them in recent years. There is not only focus on organic growth in Canada today, but in emerging markets as well. While this brings different challenges, many are moving in this direction. As a global firm, EY can help them as we have offices and life science industry partners worldwide and ensuring that they understand the logistics, laws, regulations, and constraints of other countries.

MP: The ultimate market for biotech and medical devices in most cases exists in the US or other foreign markets. The Canadian marketplace is so small, that for biotech, pharma or medical technology companies it is often not the ultimate market. In addition to support for companies moving to foreign markets, EY Canada has also provided assistance cross-province as there are different structures for tax, regulatory or IP from province to province.

What is EY's position on generics?

LI: The market is getting tighter, and competition is fierce. While many different players are working together, many are also trying to get a piece of the pie, so it will be good for pharmaceutical companies, less good for generic companies. Patent protection is one of the bigger issues that pharmaceutical companies are faced with. The cost of making drugs is colossal, so to ensure a cost-benefit, extending the patent of a drug brought to commercialization is important.

MP: It is all relative really, but pharmaceutical companies do have many shareholders that expect a certain return. They are not in as bad of a position as other life science startup companies, but they are struggling to achieve the metrics they desire. The FDA has started to grant more approvals to pharmaceutical companies in the last two years, which will hopefully help get more products to market and in the long term, benefit the innovative life science companies.

What tends to be the most noticeable aspects with which your clients need help?

MP: Generally clients need the most help with tax, specifically SR&ED credits and tax structuring. In addition, we work with many startup biotech companies looking for financing. These companies also need other services, such as audit services and advisory with respect to corporate governance. Appropriate tax structuring ensures receipt of full credits; if your ownership structure is not appropriate you are not eligible for SR&ED cash credits. Private companies in Canada actually get a refundable tax credit with cash back as opposed to just a credit for future tax. That is very valuable. It is important to setup the appropriate tax structure when developing IP that may one day be worth a lot to ensure the most efficient tax position in the future.

LI: EY can also assist companies entering into emerging markets, such as helping with tax structuring in other parts of the world, with acquisitions or due diligence.

Could you describe the origins of EY Canada's work with SR&ED credits?

MP: EY Canada has always been at the forefront of tax and SR&ED credits with respect to the technology space in general. Over the years we have tried to develop a greater expertise in the SR&ED practice above and beyond life sciences, as SR&ED can be applied in numerous industries. In Ontario, we really focus on startup biotech companies, which rely heavily on SR&ED credits. EY Canada has recently made a couple of significant acquisitions in Ontario and Saskatchewan of boutique SR&ED companies in order to enhance our branding, reputation and capabilities. Most individuals that come on board are scientists or engineers.

What is the strategic importance of EY Canada to the organization's operations in life sciences?

LI: From a global perspective, Canada is a much smaller market in life sciences compared to the US or Europe. However, there are still a large number of life sciences companies here; our global report revolves around the four life science hubs of Canada, Australia, US and Europe. We continue to have a big presence in Canada with respect to life sciences, which encompasses both pharmaceutical and biotech. We still serve a number of clients in this area and industry.

What is EY Canada’s competitive advantage?

EY either audits or works with many biotech and life science companies both in Canada and globally. The firm was involved with this industry from day one. The biotech industry is only thirty years old, and EY has been producing reports, such as *Beyond Borders* (our global biotech report) for almost the entire life cycle of the biotech industry. We have been constantly supporting the industry since its inception with our Beyond Borders Industry Report and we work with many of the biotech and life science companies in Canada, primarily in the areas of Toronto, Montreal and Vancouver.

LI: We have also progressed with those clients. Having worked with the industry since its beginnings, in terms of watching companies progress and go public, EY Canada has been involved with a tremendous amount of IPOs, other financings and deals with companies. Much of that experience has helped us maintain a competitive edge.

What is the most important advice that you give to clients?

MP: Over the years, the industry has certainly evolved. In the last number of years, the primary advice has been how to help companies be as effective and efficient with their limited resources and to help them obtain more resources such as SR&ED credits or our connections with venture capitalists or other angel investors, and helping them be effective through that process. The focus now is to make commercialization the end game, not simply the scientific research.

LI: EY’s global reports always have a theme. This year’s is called “Matters of Evidence”. In the past the focus has been matters of efficiency, and the advice was to do more with less. Many have managed to do that. The next stage is to show evidence of product value. When considering the current national and global changes, such as the increasing cost of the medical systems, or ageing populations, companies will need to show the value of their product to ensure someone will pay for it. This speaks to many big pharma executives looking to partner with biotech companies, who are now frequently questioning whether drugs actually work, as well as who will pay for them, reimbursement options, and what value they bring versus the current available options. EY keeps its clients abreast of trends we see, and tries to provide them with something different to think about.

Where do you see the biotech, pharmaceutical and medical device industries in Canada in the next five years?

MP: Canada still has excellent science and research, but there are still a lot of small under-funded life science companies. I expect to see consolidation in the market place, which will hopefully lead to stronger life science companies in Canada. I think we will see some consolidation in the industry in order for companies to have more than just one product with a couple of targets. This will provide more opportunities to be successful, and will hopefully help to attract more financing.

LI: In the next five years I also expect to see more consolidation, but more focus as well. That may involve a targeted focus on a specific program, which helps with efficiency for smaller programs. I think we will continue to see a trend of more focus in research and decisions being made on what programs or trials are being run, even in big companies, and targeting other companies for collaboration.

See more interviews