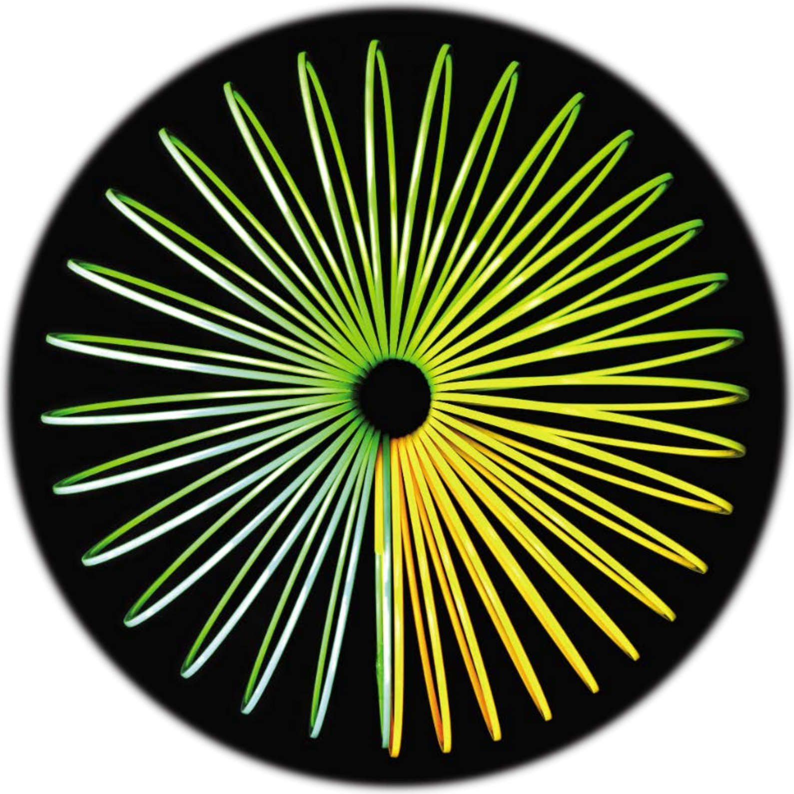

Canadian indirect tax news

Quebec ITR restrictions: The beginning of the end

November 21, 2017

The countdown is on. The phase-out of input tax refund (ITR) restrictions under the Quebec sales tax (QST) regime will begin on January 1, 2018. Get ready!

On October 25, 2017, Revenu Québec issued Interpretation Bulletin TVQ. 206.1-10, *Particulars regarding the phasing out of the ITR restrictions applicable to large businesses that is to begin on January 1, 2018* (the Bulletin), thereby confirming the government's commitment to phase out the ITR restrictions for large businesses.

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The current rules - a reminder

If you are a large business, you generally cannot claim an ITR for QST paid in respect of the following goods and services:

- road vehicles of less than 3,000 kg that must be registered under the Highway Safety Code to travel on public highways;
- fuel (other than diesel fuel) used to power the engine of such a road vehicle;
- energy used for a purpose other than to produce movable property intended for sale;
- telecommunication services;
- food, beverages or entertainment.

A person is generally considered to be a large business during a fiscal year if sales of goods and services, including sales of associated persons, exceeded $10 million during the preceding fiscal year.

Implementation of ITR restriction phase-out will begin on January 1, 2018

The government chose a fairly simple rule to implement the phase-out of ITR restrictions for large businesses. Under the *Comprehensive Integrated Tax Coordination Agreement between the Government of Canada and the Government of Quebec*, the phase-out will occur over three years, as follows:

- January 1, 2018: 25%
- January 1, 2019: 50%
- January 1, 2020: 75%
- as of January 1, 2021: 100%

Large businesses will thus be able to claim an ITR at the rate of 25% of the QST payable after December 31, 2017 (50% for calendar 2019, 75% for calendar 2020 and 100% for calendar 2021 and therefter) in respect of expenses now subject to the ITR restrictions.

> ***Example:***
> A services provider sends an invoice dated January 3, 2018 to a customer that is a large business for QST purposes. The invoice is for telecommunication services provided in December 2017.
>
> Since the QST relating to these services became payable (i.e., was invoiced) in January 2018, the large business can claim an ITR equal to 25% of the QST payable.
>
> An ITR cannot be claimed, however, if the invoice was dated December 30, 2017 and paid in January 2018.

Special rules

Generally, it appears that the ITR limits for all registrants will continue to apply as the ITR is phased out. This rule provides that large businesses may only claim an ITR equal to the applicable phase-out rate multiplied by the maximum

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amount of QST that can be claimed in respect of goods and services subject to the general limits.

Road vehicles: The $30,000 valuation limit on passenger vehicles purchased for use as a capital asset, as well as the $800 monthly lease limit on passenger vehicles, must be taken into account.

Food, beverages and entertainment: The 50% limit on food, beverage and entertainment expenses must be taken into account.

Self-assessment: In some circumstances, large businesses are currently required to self-assess the QST on goods brought into Quebec (a similar rule also applies to services acquired outside Quebec for use in Quebec). However, they will be entitled to claim a partial ITR equal to the self-assessed QST multiplied by the applicable phase-out rate.

Taxable benefit: A large business must add, in computing its net tax, an amount of QST, multiplied by the applicable phase-out rate, resulting from a taxable benefit for the employee following the supply of a property or service subject to the ITR restrictions.

Other topics of interest in the Bulletin

The Bulletin covers a wide range of scenarios, including:

- Where a person ceases to be a registrant and property is no longer used in commercial activities;
- change in use of property in respect of which an ITR could initially be claimed, but which no longer qualifies for an ITR following the change of use;
- bringing tangible property into Quebec;
- courtesy or demonstration vehicles for automobile dealers;
- credit for trade-in by a large business against the purchase of a road vehicle;
- joint election made so that no tax is payable in respect of the supply of a business where the recipient does not carry on the business;
- election in respect of supplies deemed made for no consideration by closely related persons;
- election covering a joint venture;
- allowances paid to employees.

Issues not discussed in the Bulletin include:

- claiming an ITR in respect of taxable expenses refunded to employees;
- the administrative factor (9/109) that can be used to determine the ITR an employer may claim in respect of refunds paid to employees through an expense account;
- the limit based on the gross revenue of a business with respect to food, beverage and entertainment expenses.

Apparently, special rules were not required for these situations. A large business can seemingly claim an ITR equal to the phase-out rate multiplied by the QST included in an expense subject to a restriction and paid to an employee, based on the year in which the employee incurred the expense.

Moreover, an employer that uses the administrative factor (9/109) should be able to claim an ITR equal to the phase-out rate multiplied by 9/109 of the expense subject to restriction and paid to an employee, based on the year in which the employee incurred the expense.

Practical advice

Accounting records

Since the restrictions will be phased out, large businesses should have control measures in place to ensure that they claim a portion of the QST based on the applicable rate for the particular calendar year. This will facilitate requests for information in the case of a QST audit by Revenu Québec.

Consider postponing your purchases

A registrant that is planning an imminent purchase of a good or service currently subject to ITR restrictions (for example, a road vehicle), should consider whether it would be advantageous to postpone the purchase until a calendar year in which the restrictions will be partially or fully eliminated.

Additional information

According to our information, the draft legislation implementing the phase-out of ITR restrictions will not be tabled this fall, but probably during the winter. However, these measures will apply as of January 1, 2018, regardless of the date of Royal Assent of the legislation. In the meantime, we should rely on the Bulletin in applying the new rules.

As well, no changes have been made to the QST return. Taxpayers should simply enter the equivalent of 25% of the QST paid in respect of restricted expenses in box 206 of the detailed calculations form.

Questions?

If you have any questions about these new measures, please contact your local Deloitte indirect tax specialist.

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