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Tax Alert — Canada

Quebec relaxes QST ITR restrictions

EY Tax Alerts cover significant tax news, developments and changes in legislation that affect Canadian businesses. They act as technical summaries to keep you on top of the latest tax issues. For more information, please contact your EY advisor or EY Law advisor.

Amendments to *An Act Respecting the Québec Sales Tax* (CQLR, c. T-0.1) [AQST]

On 25 October 2017, Revenu Québec published Interpretation bulletin 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). The Bulletin details how the AQST will apply with regard to the phasing out of the input tax refund (ITR) restrictions applicable to large businesses.

Wording of the amending provisions of the AQST is not expected to be known before 1 January 2018. Hence, for their first goods and services tax/harmonized sales tax (GST/HST) and Quebec sales tax (QST) returns of 2018, large businesses must refer to the Bulletin with regard to the application of the various AQST provisions pertaining to the ITR restrictions for large businesses.

Background

In the QST regime, large businesses are currently not allowed to claim an ITR in respect of the QST paid on certain expenses. Large businesses are generally those whose revenues exceeded $10 million in taxable and zero-rated revenue during their last fiscal year. The threshold amount is calculated by including the revenues in respect of supplies made by the business and its associated companies in Canada or outside of Canada through a permanent establishment in Canada. Certain financial institutions are also deemed to be large businesses regardless of their threshold amount.

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The expenses that fall under the ITR restrictions for large businesses generally include:

- Supplies of road vehicles under 3,000 kilograms that must be registered under the Highway Safety Code to be driven on public roads
- Energy (except when used to produce personal property intended for sale)
- Telecommunication services
- Meals and entertainment expenses

Implementation

As expected, the practical implementation of the phase-out of ITR restrictions for large businesses will be rather simple. Large businesses will now be allowed to claim, as an ITR, 25% of the QST paid after 31 December 2017 in respect of expenses that are currently subject to the ITR restrictions (50% for 2019 and 75% for 2020). Large businesses should make sure that they sufficiently document their calculation of the phase-out percentage applied to the QST paid in respect of expenses subject to the ITR restrictions in case of a tax audit (e.g., detailing this calculation in the Excel spreadsheet used to prepare their GST/HST/QST returns).

In general terms, it appears that the self-assessment provisions under which large businesses are currently required to self-assess QST, because of the ITR restrictions, will continue to apply through 31 December 2020, while large businesses will be allowed to claim a partially offsetting ITR equal to the self-assessed QST multiplied by the applicable phase-out percentage, i.e., 25% in 2018, 50% in 2019 and 75% in 2020 (except for taxable supplies of goods and services made to employees or shareholders that result in a taxable benefit and for situations where a large business will cease to use property covered by the ITR restrictions in the course of its commercial activities or will cease to be a registrant and the property was acquired between 31 December 2017 and 1 January 2021; in these cases, QST will have to be remitted according to the applicable phase-out percentage).

Also, it appears that the general limitations applicable to the granting of an ITR for all registrants will apply in conjunction with the phase-out percentages in such a way that large businesses will only be allowed to claim an ITR equal to the applicable phase-out percentage multiplied by the maximum QST amount that may be claimed in respect of goods and services covered by the general limitations (e.g., the $30,000 valuation limit in respect of passenger vehicles purchased as capital property, or the 50% limitation in respect of food, beverages or entertainment expenses).

Some of the main subjects covered in the Bulletin are the following:

- The $30,000 valuation limit in respect of passenger vehicles (section 247 AQST)

- The $800/month limit in respect of the lease of a passenger vehicles (section 456 AQST)
- Ceasing to be a registrant and ceasing to use property in the course of commercial activities (sections 209, 210.5, 243 and 253 AQST)
- Change in use of property where an ITR could be claimed initially and would not be allowed following the change in use (sections 243.1, 253.1, 288.1 and 289.1 AQST)
- Importation of corporeal property in Quebec (section 17 AQST)
- Courtesy and demonstration vehicles for vehicle dealers who qualify as large businesses (sections 287.3 and 288.2 AQST)
- Trade-in credit for vehicles given in exchange by a large business for the purchase of another vehicle (sections 17.1 and 54.1 AQST)
- When a joint election is made so that no tax is payable in respect of the supply of a business or part of a business and the recipient does not carry on the business (section 75.1 AQST)
- Joint election made by closely related legal persons to have supplies deemed made for no consideration (section 334 AQST)
- Joint election covering a joint venture (section 346.1 AQST)
- Allowances paid to employees (section 211 AQST)
- Taxable supplies of goods and services made to employees or shareholders which result in a taxable benefit (sections 290 and 292 AQST)
- Food, beverages and entertainment expenses (section 457.1 AQST)

Some more exceptional situations are also covered in the Bulletin. However, other relevant subjects are not covered in the Bulletin, such as the possibility to claim an ITR in respect of taxable expenses reimbursed to employees (section 212 AQST), the administrative factor (9/109) that may be used to determine the ITR that an employer may claim in respect of reimbursements paid to employees, instead of the actual QST paid by the employee, and the limitation based on a business' gross revenue in respect of food, beverage and entertainment expenses (sections 457.1.4 et seq. AQST).

It is our understanding that a large business will be allowed to claim an ITR equal to the applicable phase-out percentage multiplied by the QST included in a restricted expense that is reimbursed to an employee, depending on the year during which the employee incurred the expense. If the employer uses the administrative factor (9/109), it should be allowed to claim an ITR equal to the applicable phase-out percentage multiplied by 9/109 of the restricted expense that is reimbursed to an employee, depending on the year during which the employee incurred the expense.

Phase-out of restrictions commences 1 January 2018

Under the Comprehensive Integrated Tax Coordination Agreement between the Government of Canada and the Government of Québec, the Government of Québec agreed to phase-out the restrictions on ITRs for large businesses. It was agreed by both parties that phasing-out would be applied in equal annual proportions during a maximum period of three years starting no later than on 1 January 2018.

The Québec Ministry of Finance announced, in the additional information on the fiscal measures of its 2015-2016 budget, that the restrictions on ITRs for large businesses would be phased out as further detailed in the table below.

This commitment was reaffirmed last March in the Government of Québec's detailed financial framework for 2016-2017 to 2018-2019 where the Ministry of Finance accounted for the "downward pressure on the growth of consumption tax revenue" that will be caused by the "gradual elimination of restrictions on [ITRs] for large businesses, as of January 1, 2018."

The following chart shows the percentage of QST paid that will be allowed to be claimed by large businesses as an ITR during the phasing-out period:

Period during which QST will become payable	**Percentage of QST paid that may be claimed as an ITR**
1 January to 31 December 2018	25%
1 January to 31 December 2019	50%
1 January to 31 December 2020	75%
1 January 2021 and beyond	100%

It may be advisable for taxpayers to postpone non-urgent expenditures currently subject to the ITR restrictions to a calendar year in which the restrictions will be partially or completely phased out.

Learn more

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