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Phasing Out of Restrictions on the Granting of Input Tax Refunds to Large Businesses as of January 1, 2018

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Online Tax Strategies

In 2012, further to an agreement with the Government of Canada to harmonize the GST/HST and QST, the Government of Quebec announced that it would eliminate restrictions on the granting of input tax refunds (ITR) for large businesses. In the March 2015 Quebec budget, the Finance Minister announced that the restrictions would be phased out as of January 1, 2018.

On October 25, 2017, Revenue Quebec published QST bulletin TVQ. 206.1.10 to implement the new provisions and clarify the application of the *Quebec Sales Tax Act* (QSTA) with respect to the phase out of the restrictions starting on January 1, 2018 and ending on January 1, 2021.

Enterprises that are currently large businesses or will become one in the coming months or even in the next four years should be aware that the new measures will impact them and should have a system in place to closely monitor their ITR claims for QST purposes.

Concept of large business and restrictions for QST purposes

To summarize, for QST purposes, a large business is generally a business whose taxable sales in Canada, including those of its associates, are in excess of $10M in the last fiscal period ended prior to the start of the year in question. Income includes exports, transactions between closely related companies that have elected to have certain supplies made between them deemed made for no consideration (FP-4616).

Banks, trust companies, credit funds, insurance companies, segregated funds of insurers, the Autorité des marchés financiers, Canada Deposit Insurance Corporation and investment plans are large businesses, regardless of their income amount.

Businesses that are large businesses cannot claim ITRs for certain goods and services acquired in the course of their commercial activities. The goods and services to which the ITR restrictions apply are:

- Road vehicles of less than 3,000 kg that must be registered under the *Highway Safety Code* to travel on public highways;
- Gasoline used to power the engine of such a road vehicle;
- A good or service (improvement) relating to such road vehicle that is acquired or brought into Quebec within 12 months after the vehicle is acquired or brought into Quebec;
- Electricity, gas, combustibles or steam used for a purpose other than to produce movable property intended for sale;
- Telephone service and other telecommunication services, other than 1-800 services and internet services; and
- Food, beverages and entertainment whose deductibility is limited to 50% under the *Taxation Act*.

Phase out of restricted ITRs

As of January 1, 2018, a large business can claim a partial ITR for goods and services subject to the restrictions. The refund rate will increase progressively from 25% in 2018 to 50% in 2019, 75% in 2020 and 100% as of 2021.

Remember that tax is generally payable on the earlier of the date the consideration is paid or the date it becomes payable. There are a number of presumptions in the QSTA, but, usually, consideration becomes payable on the earlier of the date the invoice is issued or the date stated in a written agreement.

Special considerations

The phase out of restrictions on ITR refunds for large businesses over a three-year period will likely result in complex application, administration and monitoring activities requiring advance planning to avoid potential QST assessments. Examples include large businesses with year-ends that do not coincide with the calendar year, monitoring lease periods for multiple-year road vehicle leases and the requirement to keep work sheets in support of partial QST-ITRs in some industries, such as automobile dealerships.

The following list provides an overview of some of the changes that should be considered:

A) Road vehicles (passenger vehicles)

- A large business can claim a partial ITR on the acquisition of a road vehicle subject to the restrictions (or an improvement to such a vehicle), with respect to QST payable after 2017 (25% in 2018). However, the refund must take into consideration the $30,000 limit for passenger vehicles for which QST can usually be claimed.
- There is a rule which provides that when a non-large business registrant sells a vehicle, that registrant can obtain a partial refund of the QST initially paid. This applies to a portion of the tax paid above the $30,000 limit. When a large business sells a vehicle, it may be entitled to a partial QST refund if the vehicle was acquired after 2017 (e.g., a vehicle costing $50,000 in 2018, subject to the $30,000 rule and sold for $35,000 in 2020 may give rise to a partial refund of 75% of the non-refunded QST on the acquisition of the vehicle on the portion of the amount in excess of $30,000).
- In the case of leased vehicles, a partial ITR may be obtained for the QST paid on a leasing period that begins in 2018. It should be noted that under the QSTA, there is a presumption of acquisition for each lease interval, which means that even if a lease exists before 2018, each month of rent represents a new deemed acquisition. Additionally, remember that the monthly CCA of $800 or less must be considered in calculating the partial ITR refund.
- In the case of automobile dealerships that have to self-assess 2.5% of the tax calculated on the value of each vehicle for each month of use of vehicles acquired for sale or lease that are used for another purposes (demos, courtesy, etc.), it will be possible to obtain a partial ITR using the applicable rates for self-assessment periods.
- There are other rules for vehicles brought into Quebec or trade-in vehicles on the purchase of a new vehicle.

B) Other goods and services covered by the restrictions

- A partial ITR may be claimed based on the year of acquisition (25% in 2018, 50% in 2019, 75% in 2020 and 100% in 2021) of the other goods and services covered by the restrictions (see list above).
- As of January 2018, the tax paid on supplies of food, beverages and entertainment by a large business may give entitlement to an ITR calculated on the amount limited to 50% using the partial rate for the year of the supply.

C) Allowance

- Under the QST system, there is a presumption whereby a registrant can claim an ITR equal to 9.975/109.975 of the allowance paid to an employee for taxable supplies of goods and services acquired in Quebec or for the use of a motor vehicle in Quebec (kilometre-based allowance). Previously, this was not possible for large businesses, but will be as of January 1, 2018 in respect of an allowance for which tax is deemed to be paid, according to the year of payment of the allowance (ITR of 25%, 50% or 75%, depending on the year).

D) Taxable benefit to an employee or shareholder

- Under the QSTA, a registrant who makes a supply of goods or services to an employee or shareholder resulting in a taxable benefit must add the amount of QST in calculating its net tax. However, registrant large businesses were not subject to this rule as they were not entitled to an ITR on such goods and services to begin with.
- For the 2018, 2019 and 2020 taxation years, a large business will now be required to include in the calculation of its net tax, the tax resulting from the taxable benefit granted, calculated on the partial rate applicable for the year for which the benefit was paid.

E) Other measures

The Revenue Quebec bulletin announced additional measures relating to the following:

- Incidental supplies (Sec. 34.1 QSTA);
- Goods transferred by a large business on the sale of a business or part of a business (Sec. 75.1 QSTA);
- The election to have taxable supplies made between closely related legal persons deemed made for no consideration (Sec. 334 QSTA and FP-4616 election);
- Application to a deemed branch of another organization (Sec. 343 QSTA);
- Election covering a joint venture (Sec. 346.1 QSTA); and
- Repayment of QST on fuel (Sec. 402.1 and 402.2 QSTA).

Conclusion

The long-awaited measures to phase out GST restrictions for large businesses are not simple. They apply to numerous transactions that will have to be closely monitored to avoid tax compliance issues which could potentially result in QST liabilities.

Your Raymond Chabot Grant Thornton advisor can help you determine which measures apply to your situation and help you undertake the necessary steps to use them. Do not hesitate to contact us.

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