INTERPRETATION AND ADMINISTRATIVE BULLETIN CONCERNING THE LAWS AND REGULATIONS

Consumer Taxes

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**

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Reference(s): *Act respecting the Québec sales tax* (CQLR, c. T-0.1), sections 1, 17, 17.1, 30.1, 34.1, 54.1, 75.1, 206.1, 209, 210.5, 211, 240 to 246, 247, 249, 253, 253.1, 287.3, 288.1, 288.2, 289.1, 290, 292, 334, 343, 346.1, 402.1, 402.2, 456 and 457.1[1]

This bulletin explains how the Act respecting the Québec sales tax (AQST) applies with regard to the phasing out of the input tax refund (ITR) restrictions applicable to large businesses, which was announced by the Québec Minister of Finance in conjunction with the Budget Speech of March 26, 2015. The phasing out of such restrictions will begin on January 1, 2018.
This bulletin is subject to the National Assembly passing a bill to implement this measure.

Under the current Québec sales tax (QST) system, businesses considered to be large businesses are not entitled to claim an ITR in respect of certain property and services acquired in the course of their commercial activities. The property and services covered by the ITR restrictions are:

— road vehicles of less than 3,000 kg that must be registered under the *Highway Safety Code* (CQLR, c. C-24.2) to travel on public highways;

— gasoline used to power the engine of such a road vehicle;

— any property or service (improvement) relating to such a road vehicle that is acquired or brought into Québec within 12 months after the vehicle was acquired or brought into Québec;

— electricity, gas, combustibles or steam used for a purpose other than to produce movable property intended for sale;

1 Section 206.1 of the AQST and a number of other provisions related to the ITR restrictions discussed in this bulletin were repealed on August 1, 1995, in respect of small and medium-sized businesses and were supposed to be repealed on November 30, 1996, in respect of large businesses (S.Q. 1995, c. 63). However, generally speaking, the repeal of those provisions in respect of large businesses was initially postponed until March 31, 1997 (*Budget Speech and Additional Information*, May 9, 1996, Appendix A, p. 11), and subsequently postponed indefinitely (*Budget Speech and Additional Information*, March 25, 1997, Appendix A, pp. 204-05 and S.Q. 1997, c. 85).

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— telephone service and other telecommunication services, except for 1-800 services and Internet services; and

— food, beverages or entertainment whose deductibility is limited under the *Taxation Act* (CQLR, c. I-3).

In conjunction with the Budget Speech of March 26, 2015, the Québec Minister of Finance announced the phasing out of the restrictions to allow large businesses to claim an ITR in respect of the property and services currently covered by the restrictions.

Thus, QST that becomes payable on or after January 1, 2018, in respect of acquisitions of property and services covered by the restrictions can be included in calculating a large business's ITR, at the rate of 25% in 2018, 50% in 2019, 75% in 2020, and 100% in 2021 and subsequent years.

APPLICATION OF THE ACT

Capital property (AQST, sections 240 to 245)

1. By virtue of paragraph (3) of section 246 of the AQST, the rules with respect to capital property provided for in sections 240 to 245 of the AQST do not currently apply to a road vehicle, or any improvement made to a road vehicle, in respect of which a large business would not be entitled to claim an ITR due to the restrictions, if the business acquired such a vehicle or improvement or brought it into Québec for use exclusively in the course of the business's commercial activities.

2. Those rules will apply to any road vehicle or improvement made to a road vehicle acquired or brought into Québec on or after January 1, 2018.

Passenger vehicle

Definition (AQST, section 1)

3. The term "passenger vehicle," according to the definition in section 1 of the AQST, has the meaning assigned by section 1 of the *Taxation Act*. However, the definition of that term does not include a road vehicle in respect of which a large business would not be entitled to claim an ITR due to the restrictions, if the business acquired the vehicle or brought it into Québec for use exclusively in the course of the business's commercial activities.

4. Under the new rules, a road vehicle acquired or brought into Québec by a large business on or after January 1, 2018, can qualify as a passenger vehicle (to the extent the conditions provided for in that definition are met), even though a full ITR cannot be claimed in respect of the vehicle due to the phasing out of the restrictions.

5. Note that there is no change in the status of a road vehicle that was acquired before January 1, 2018, and did not qualify as a passenger vehicle because no ITR could be claimed in respect of the vehicle due to the restrictions.

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Acquisition (AQST, section 247)

6. Where a passenger vehicle is acquired for use as capital property in the course of a commercial activity, the ITR that a registrant can claim in respect of the tax payable must be calculated on a value of $30,000 or less (before the application of the taxes).

7. That rule will apply to a passenger vehicle acquired by a large business on or after January 1, 2018. Thus, a large business will be entitled to claim an ITR in respect of the tax calculated on a value of $30,000 or less, at the rate of 25%, 50% or 75%, depending on the year the vehicle is acquired.

Sale (AQST, section 249)

8. A registrant who makes a taxable supply by way of sale of a passenger vehicle used as capital property in the registrant's commercial activities can claim an ITR calculated on the basis of the basic tax content of the passenger vehicle where a portion of the tax originally paid could not be recovered.

9. That rule will apply to a passenger vehicle acquired by a large business on or after January 1, 2018. The tax originally paid that could not be recovered includes the tax that could not be claimed due to either the $30,000 limit or the ITR restrictions.

10. Example:

2018 – <u>Purchase of a passenger vehicle subject to the ITR restrictions</u>

• Sale price (before the application of the taxes): $50,000

• QST paid: $50,000 × 0.09975 = $4,987.50

• ITR: $30,000 × 0.09975 = $2,992.50 × 25% = $748.13

2020 – <u>Taxable sale of the passenger vehicle</u>

• Fair market value: $20,000

• ITR: According to the formula provided for in section 249 of the AQST:

[(4,987.50 × 20,000 / 50,000) × (4,987.50 – 748.13) / 4,987.50)] × 75% = $1,271.81

11. For greater certainty, no ITR can be claimed upon the sale of a road vehicle that is covered by the restrictions and acquired by a large business before January 1, 2018. (See point 5.)

Lease (AQST, section 456)

12. With respect to the supply of a road vehicle under a lease, the QST system includes a presumption of acquisition for each lease interval. Thus, a road vehicle that does not qualify as a passenger vehicle at a time during a lease interval before January 1, 2018, can qualify as a passenger vehicle for a lease interval that begins on or after January 1, 2018.

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13. Also, the QST paid for a lease interval that begins on or after January 1, 2018, can be included in calculating a large business's ITR, at the rate of 25%, 50% or 75%, depending on the year of the lease interval.

14. In addition, where the cost of the lease of a passenger vehicle exceeds the applicable limit for the deduction allowed in computing income under the *Taxation Act*, a large business will be required to either adjust its ITR claim for each reporting period in view of the limit or make an adjustment in calculating its net tax each year.

15. For example, a large business leases a road vehicle subject to the ITR restrictions. The lease requires 36 monthly payments from January 1, 2017, to December 1, 2019. The large business can claim an ITR only in respect of the monthly payments that become payable on or after January 1, 2018, at the rate of 25% for each such payment that becomes payable in 2018 and 50% for each one that becomes payable in 2019.

Change in use of property and a person who ceases to be a registrant (AQST, sections 209, 210.5, 243 and 253)

16. A number of situations in which property is no longer used in the course of a person's commercial activities may result in a deemed disposition. In such a case, the person must remit an amount of tax in respect of the property concerned, unless no ITR could be claimed in respect of the property because it was covered by the restrictions.

17. For property that is covered by the ITR restrictions and acquired or brought into Québec after December 31, 2017, and before January 1, 2021, the amount of tax to be remitted is adjusted according to the year it was acquired or brought into Québec. For example, for property acquired in 2018 in respect of which an ITR of 25% was claimed, a large business has to remit only 25% of the tax calculated on the fair market value of the property or the basic tax content of the property, as applicable.

Change in ITR eligibility due to the restrictions (AQST, sections 243.1, 253.1, 288.1 and 289.1)

18. Where a large business owns property in respect of which it was entitled to an ITR and it begins to use the property for any purpose that, due to the ITR restrictions, would not entitle it to claim an ITR if it acquired the property at that time, the business must pay the tax calculated on the fair market value of the property at that time.

19. The self-assessment provisions will continue to apply to changes in use that occur through December 31, 2020. A large business will have to pay the tax in accordance with those provisions and will be entitled to claim an ITR, at the rate of 25%, 50% or 75%, depending on the year of the deemed disposition.

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20. Example:

2016 – Purchase of a vehicle that does not have to be registered to travel on public highways (an off-highway vehicle)

• Sale price (before the application of the taxes): $25,000

• ITR: $25,000 × 0.09975 = $2,493.75

2019 – Change in registration to travel on public highways – Application of the change-in-use rule (AQST, section 243.1)

• Fair maket value: $20,000

• Self-assessment: $20,000 × 0.09975 = $1,995

• ITR: $1,995 × 50% = $997.50

Road vehicle in inventory used for another purpose – Automobile dealers (AQST, sections 287.3 and 288.2)

21. Where a large business received a supply of a road vehicle for resupply and begins to use the vehicle for a purpose that, due to the restrictions, would not entitle it to claim an ITR if it acquired the vehicle at that time, the business must pay 2.5% of the tax calculated on the value of the vehicle for every month in which the vehicle is used for that purpose.

22. The self-assessment provision will continue to apply through December 31, 2020. A large business will have to pay the tax in accordance with that provision and will be entitled to claim an ITR, at the rate of 25%, 50% or 75%, depending on the month in which the vehicle is used for that purpose.

Property brought into Québec (AQST, section 17)

23. Where a large business brings into Québec corporeal property covered by the ITR restrictions, it must pay the QST in respect of the property. That rule continues to apply in respect of the total value of the property brought into Québec before January 1, 2021. A large business will be entitled to claim an ITR, at the rate of 25%, 50% or 75%, depending on the year the property is brought into Québec.

Credit granted by a supplier for a used vehicle given in exchange (AQST, sections 17.1 and 54.1)

24. Where a large business acquires a road vehicle or brings such a vehicle into Québec, the value on which the tax must be calculated may be reduced under certain conditions. The reduction in the value of the road vehicle corresponds to the credit granted by the supplier for another road vehicle (hereinafter the "trade-in") accepted by the supplier in full or partial consideration for the supply of the road vehicle acquired or brought into Québec.

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25. That measure will remain in effect through December 31, 2020, for any trade-in in respect of which no ITR can be claimed due to the restrictions. Thus, the measure will not apply to any trade-in in respect of which a partial ITR can be claimed beginning in 2018.

26. Example:

2016 – Acquisition of vehicle No. 1 in respect of which QST is paid

• ITR: $0

• Value in 2020: $10,000

2020 – Acquisition of vehicle No. 2

• Sale price (before the application of the taxes): $30,000

• Credit for vehicle No. 1: ($10,000)

• Amount on which QST is applied: $20,000

• QST payable: $20,000 × 0.09975 = $1,995

• ITR: $1,995 × 75% = $1,496.25

Telecommunication service (AQST, section 30.1)

27. The presumption that a supply of a telecommunication line by way of lease, licence or similar arrangement is deemed to be the supply of a telecommunication service remains in effect through December 31, 2020.

28. Beginning January 1, 2018, a large business that acquires such a supply will be entitled to claim an ITR, at the rate of 25%, 50% or 75%, depending on the year the telecommunication service is acquired.

Incidental supply (AQST, section 34.1)

29. Currently, where a large business acquires a supply of property or a service covered by the ITR restrictions that is incidental to the supply of a particular property or service not covered by the restrictions, the business is not entitled to claim an ITR in respect of the incidental supply. The business cannot rely on the presumption that the incidental supply is deemed to be a part of the other supply not covered by the restrictions.

30. That rule will continue to apply through December 31, 2020. A large business will be entitled to claim an ITR, at the rate of 25%, 50% or 75%, depending on the year the incidental supply covered by the restrictions is acquired.

Transfer of the property of a business (AQST, section 75.1)

31. Where a supply of a business or part of a business is made, the supplier and the recipient may make a joint election under paragraph (2) of section 75 of the AQST so that no tax is payable in respect of the supply.

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32. However, that election does not apply where the recipient does not carry on the business and the supply constitutes a taxable supply of any property or service in respect of which the recipient would not be entitled to claim an ITR due to the restrictions, if the recipient were a registrant that acquired the property or service for consumption or use exclusively in the course of its commercial activities.

33. That rule will continue to apply through December 31, 2020. A recipient that is a large business will have to pay tax in respect of the supply of any property or service covered by the restrictions and will be entitled to claim an ITR, at the rate of 25%, 50% or 75%, depending on the year the supply is made.

Election made by closely related legal persons to have supplies deemed made for no consideration (AQST, section 334)

34. Under certain circumstances, closely related legal persons may make a joint election so that every taxable supply made between them is deemed to have been made for no consideration. However, that election does not apply to a supply of property or a service in respect of which the recipient is not entitled to claim an ITR due to the restrictions.

35. That rule will continue to apply through December 31, 2020. A recipient that is a large business will have to pay tax in respect of the supply of the property or service covered by the restrictions and will be entitled to claim an ITR, at the rate of 25%, 50% or 75%, depending on the year the supply is made.

Application to be deemed a branch of an organization (AQST, section 343)

36. Where a particular unincorporated organization is a member of another unincorporated organization, they can make a joint application so that the particular organization is deemed to be a branch of the other organization and not a separate person.

37. However, that election does not apply to the supply of property or a service in respect of which the recipient that is a large business is not entitled to claim an ITR due to the restrictions. That rule will continue to apply through December 31, 2020.

Election covering a joint venture (AQST, section 346.1)

38. Where an operator is a participant in a joint venture with a co-venturer, an election may be made so that the property and services supplied, acquired or brought into Québec by the operator on behalf of the co-venturer are deemed to be supplied, acquired or brought into Québec by the operator and not by the co-venturer.

39. However, that election does not apply to the acquisition or bringing into Québec of property or a service in respect of which the co-venturer, were the property or service acquired by the co-venturer, would not be entitled to claim an ITR due to the restrictions.

40. That rule will continue to apply through December 31, 2020. A co-venturer that is a large business will have to pay tax in respect of the supply of the property or service covered by the

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restrictions and will be entitled to claim an ITR, at the rate of 25%, 50% or 75%, depending on the year the supply is made.

Allowance (AQST, section 211)

41. Under the QST system, there is a presumption whereby a person can claim an ITR equal to 9.975/109.975 of the allowance that the person pays to an employee of the person for taxable supplies of property and services acquired in Québec, or for the use of a motor vehicle in Québec, in relation to activities engaged in by the person.

42. However, that presumption does not apply to an allowance that relates to property or a service in respect of which the person would not be entitled to claim an ITR due to the restrictions, if the person were a registrant that acquired the property or service for consumption or use exclusively in the course of its commercial activities, .

43. For an allowance paid on or after January 1, 2018, a large business will be entitled to claim an ITR of 25%, 50% or 75% of the tax the business is deemed to have paid, depending on the year the allowance is paid.

Employee benefit (AQST, sections 290 and 292)

44. Under the QST system, a registrant who makes a supply of property or a service to an employee or shareholder of the registrant resulting in a taxable benefit must add the amount of QST in calculating the registrant's net tax. That rule does not apply to property or a service covered by the ITR restrictions where the registrant is a large business at any time in the taxation year of the employee or shareholder.

45. For the 2018, 2019 and 2020 taxation years, a registrant that is a large business at any time in any of those years will have to include, in calculating the net tax of the registrant, the tax resulting from the taxable benefit granted, calculated at the rate of 25% for 2018, 50% for 2019 and 75% for 2020.

Food, beverages and entertainment (AQST, section 457.1)

46. Currently, a large business is not entitled to claim an ITR for the tax paid in respect of a supply of food, beverages or entertainment where section 421.1 of the *Taxation Act* applies to limit the deductibility of the amount to 50% of either the amount paid or payable or the amount that would be reasonable in the circumstances, whichever is less.

47. Beginning January 1, 2018, a large business will be entitled to claim, for the tax paid in respect of a supply of food, beverages or entertainment, an ITR calculated on the amount limited to 50%, at the rate of 25%, 50% or 75%, depending on the year the supply is made. The large business will be required to either adjust its ITR claim every reporting period in view of the limit or make an adjustment in calculating its net tax each year.

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QST rebate of the tax paid in respect of fuel (AQST, sections 402.1 and 402.2)

48. Generally speaking, a large business that is a public carrier or that purchased, in Québec, fuel that was exported and used outside Québec is not entitled to claim an ITR in respect of the fuel due to the restrictions. However, under certain circumstances, such a business is entitled to claim a rebate of the QST paid in respect of the fuel where it is entitled to a refund in respect of the fuel under the *Fuel Tax Act* (CQLR, c. T-1).

49. That measure will continue to apply through December 31, 2020. The application for a QST rebate will, however, have to be adjusted to take into account any ITR received in 2018 or subsequent years. For example, if a large business is entitled to an ITR of 25% of the tax the business paid in respect of fuel acquired in 2018, it will be entitled to claim only 75% of the QST rebate provided for by the measure.

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