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Improper claims and deductions: nothing to make light of

Since individuals and businesses are responsible for determining their income tax, source deductions and consumption taxes payable, and for remitting these amounts to Revenu Québec, it happens sometimes that they claim deductions for operating expenses, or input tax credits (ITCs) and input tax refunds (ITRs), to which they are not entitled. At first glance everything looks fine. The supporting documents provided appear to meet the documentary requirements but, in fact, they do not always properly reflect the transactions that actually took place between an individual or business and its suppliers.

Revenu Québec counters this by carrying out tax audits and ensuring that income tax returns and supporting documents are accurate and in compliance. To avoid having ITCs, ITRs and certain expenses disallowed, you must provide accurate information and supporting documents that correctly reflect the transactions between you and your suppliers.

Did you know that anyone that improperly claims refunds or deductions for operating expenses without being entitled to them is liable to a penalty, a fine and/or a prison sentence? Fines can reach 200% of the unpaid taxes. In some cases, these sanctions may even apply to the directors of a guilty corporation.

Voluntary disclosure

Revenu Québec encourages individuals and businesses that may have failed to report certain income, or may have claimed ITCs or ITRs on the basis of incorrect documents or information, to correct their tax file through voluntary disclosure. For more information, see the folder *Voluntary Disclosure: Regularizing Your Tax File with the Ministère du Revenu* ([IN-309-V](#)).

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Additional rents

A commercial lease agreement commonly requires the lessee to pay amounts known as "additional rents" as well as basic rent. Additional rents may include amounts related to common area expenses, insurance premiums, property taxes, water charges and business taxes.

Who is responsible for paying GST and QST on an additional rent provided for in a commercial lease?

If, under a lease agreement, the total amount payable for the taxable supply by lease of an immovable includes amounts as additional rents, the lessee must pay the landlord GST and QST on the total amount paid to lease the immovable. This total includes the additional rent, even if the additional amounts are listed separately, since the additional rent is part of the consideration charged by the landlord for the lease of the immovable under the lease agreement.

Generally, property and business taxes paid by the property owner to a municipality are not subject to GST and QST. However, if the property owner indicates a separate amount specifically for such taxes in the commercial lease, that amount is considered a taxable additional rent, even if the lessee pays the amount directly to a third party such as the municipality.

However, if the lessee is directly liable to the municipality for payment of a business tax prescribed by law, the amount is not considered an amount payable to the property owner for a taxable supply of the immovable under the lease agreement, even if the lease agreement contains a clause requiring the lessee to pay the business tax directly to the municipality. In such cases, the business tax is not considered an additional rent.

As a rule, a lessee who is registered for the GST and QST may recover all or a portion of the taxes paid on additional rents by claiming input tax credits (ITCs) and input tax refunds (ITRs).

For additional information, see *GST/HST Memoranda Series: Commercial Real Property—Sales and Rentals (19.4.1)*.



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Associated persons and certain GST and QST thresholds

Under the GST and QST systems, the concept of associated persons involves control between persons. For example, an individual and a legal person are associated with each other for GST and QST purposes if the legal person is controlled by the individual. Also, a person and a partnership are associated with each other if the total of the shares of the profits of the partnership to which the individual and all other persons who are associated with the individual are entitled is more than half of the total profits of the partnership. Two legal persons are associated with each other if they meet the conditions for association set out under the *Income Tax Act* for GST purposes and under the *Taxation Act* for QST purposes. Moreover, persons are associated with each other if each of them is associated with the same third person.



Persons considered to be associated persons must take this association into account when calculating the small supplier threshold and determining their reporting period.

Small supplier threshold

As a rule, a small supplier is not required to register for the GST and QST and is generally not required to collect GST and QST. However, a non-registered small supplier is required to collect the GST and QST on certain [supplies](#), such as the sale of an immovable. Under the QST system, certain small suppliers are required to register for the QST. This is the case, for example, for retailers who sell tobacco products, new tires and new or used road vehicles.

A person is generally a small supplier during any particular calendar quarter and the following month if the person's total world-wide taxable supplies, including zero-rated supplies, in the previous four calendar quarters does not exceed \$30,000. The total also includes supplies made by an associate of the person at the beginning of the particular calendar quarter. The total excludes the sale of the goodwill of a business, supplies of financial services and sales of capital property. Where the person is a public service body, the total must not exceed \$50,000. Note that, under the QST system, supplies of financial services are not excluded from the calculation of the small supplier threshold.

If the total taxable supplies of associated persons exceed \$30,000 (or \$50,000 for public service bodies) during four consecutive calendar quarters, each associate remains a small supplier for one month after the end of the calendar quarter in which the total exceeds the threshold. The associated persons are not required to collect the GST or QST on supplies made during that month. However, at the beginning of the following month, each person must charge and collect the GST and QST.

Also, if during any fiscal quarter, the total taxable supplies of associated persons exceed the small supplier threshold, the associated persons immediately cease to be small suppliers. Associated persons must immediately begin to charge and collect GST and QST on all of their taxable supplies, including the sale which put them over the threshold.

More information about small suppliers is published in *GST/HST Memoranda Series: Small Suppliers (2.2)*.

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Reporting periods

Persons who register for GST and QST are assigned reporting periods for filing their GST and QST returns. The filing frequency is determined by the total amount of taxable supplies. This amount is equal to the total taxable supplies of goods and services made in Canada during the previous or current fiscal year. The amount does not include supplies made outside Canada, zero-rated exports of goods and services, zero-rated financial services, taxable sales of capital real property or goodwill. For associated persons, the amount includes the total supplies made by each associated person. The filing frequency, which is determined by the total amount of taxable supplies, is as follows:

- If the total amount of taxable supplies is more than \$6 million, each associated person must file GST and QST returns monthly.
- If the total amount of taxable supplies is \$6 million or less but more than \$500,000, each associated person must file GST and QST returns quarterly. They may elect to file monthly.
- If the total amount of taxable supplies is \$500,000 or less, each associated person must file GST and QST returns annually. They may elect to file quarterly or monthly.

As was announced in the 2007 Federal Budget, the total amount of \$500,000 is replaced by the amount of \$1,500,000 for fiscal years that begin after 2007.

GST and QST registered charities and listed financial institutions automatically have an annual reporting period, regardless of their total supplies, unless the charities or institutions elect to file quarterly or monthly.

If an annual filer has a net GST or QST remittance of \$1,500 or more for a fiscal year, quarterly instalment payments are required throughout the following fiscal year. As announced in the 2007 Federal Budget, the amount of \$1,500 is replaced by \$3,000 for fiscal years that begin after 2007.

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Rules concerning the zero-rating of a supply of corporeal property being shipped outside Québec

Specific rules must be respected in order for a [supply](#) of property being shipped outside Québec to be zero-rated. The rules are based on whether or not the recipient is a consumer.

Under section 1 of the *Act respecting the Québec sales tax*, a consumer is an individual who acquires, or brings into Québec, a property or service at his or her expense for his or her personal consumption, use or enjoyment or the personal consumption, use or enjoyment of any other individual. A consumer does not include an individual who acquires, or brings into Québec, the property or service for consumption, use or supply in the course of the commercial activities of the individual or other activities in the course of which the individual makes exempt supplies.



Supply to a recipient who is a consumer

If the recipient of the supply of property is a consumer, section 190 of the Act provides that the supply is zero-rated only if the supplier

- ships the property to a destination outside Québec;
- transfers possession of the property to a common carrier or consignee that has been retained to ship the property to a destination outside Québec;
- sends the property by mail or courier to an address outside Québec.

In such cases, it is the supplier that is responsible for shipping the property outside Québec.

Supply to a recipient who is not a consumer

If the recipient of the supply of property is not a consumer, the supplier is responsible for shipping the property outside Québec (section 190 of the Act) or the recipient is responsible (section 179 of the Act).

Section 179 of the Act provides that where the supply of property is made to a recipient, other than a consumer, who intends to ship the property outside Québec, the supply is a zero-rated supply if all of the following conditions are met:

1. The recipient ships the property outside Québec as soon as is reasonable after the property is delivered by the supplier to the recipient.
2. The property is not acquired by the recipient for consumption, use or supply in Québec before the shipment of the property outside Québec by the recipient.
3. After the supply is made and before the recipient ships the property outside Québec, the property is not further processed, transformed or altered in Québec except to the extent reasonably necessary or incidental to its transportation.
4. The supplier maintains evidence satisfactory to the Minister of the shipment of the property outside Québec by the recipient.

Furthermore, in the case of property that is a continuous transmission commodity that the recipient intends to ship outside Québec by means of a wire, pipeline or other conduit,

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section 179 also requires that the recipient not be a registrant.

Summary of the rules

The fact that property is being shipped outside Québec does not make its supply zero-rated. The rules regarding the status of the recipient (whether or not the recipient is a consumer) must be respected.

The rules regarding the zero-rating of a supply of property being shipped outside Québec can be summarized as follows:

1. If the recipient is a consumer, the supplier is responsible for shipping the property outside Québec.
2. If the recipient is not a consumer, either the supplier or the recipient is responsible for shipping the property outside Québec.

In both cases, the supplier must retain sufficient documentary proof to show that the conditions provided under the Act for zero-rating of supplies have been respected.

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Sale of a medical or dental practice

Under subsection 167(1) of the *Excise Tax Act* (ETA) and section 75.1 of the *Act respecting the Québec sales tax* (AQST), two non-registrants (a vendor and a purchaser) may qualify to make a joint election to have no tax payable on the sale of a medical or dental practice between them. However, it may not be necessary for the vendor and the purchaser to make this election where, for example, both are engaged exclusively in non-commercial activities.

The sale of a medical or dental practice that is in operation (which constitutes a business) involves the transfer of the assets described below.

Medical and dental supplies, equipment and furniture

Sales of medical and dental supplies may be taxable or zero-rated. Sales of equipment and furniture are generally subject to the GST and the QST. If a person sells movable property that was acquired for use exclusively (90% or more) in the course of non-commercial activities and that was not consumed or used in the course of commercial activities, the sale is deemed made in the course of non-commercial activities. Such a sale will not be subject to the GST and the QST.

Goodwill

In general, section 167.1 of the ETA and section 75.2 of the AQST apply to the sale of a medical or dental practice where, under the agreement, the purchaser acquires all, or substantially all (90% or more), of the property necessary to carry on the business.

Section 167.1 of the ETA and section 75.2 of the AQST provide that, where the sale of the medical or dental practice satisfies the conditions to make the joint election under subsection 167(1) of the ETA and section 75.1 of the AQST, the portion of the sales price that is reasonably attributable to goodwill will not be subject to the GST and the QST, regardless of whether the vendor and the purchaser file the joint election.

Leasehold improvements

Where a non-registrant vendor (such as a dentist or a doctor) engaged exclusively in exempt activities, makes a taxable supply of capital property or leasehold improvements to a non-registrant purchaser, (for example, another dentist or doctor), the vendor must collect and remit the GST and the QST payable on that supply.

Where the improvements are supplied in the course of the sale of a business, the sale of the improvements remains taxable even though the vendor and the purchaser may file a joint election under subsection 167(1) of the ETA and section 75.1 of the AQST.

However, the vendor may be eligible for a rebate of the GST and the QST paid on the acquisition of and improvements to the capital property.

For further information on the sale of a medical or dental practice, consult policy statement [P-166](#), *Sale of a Medical or Dental Practice Between Two Non-registrants*.

For further information on the election under subsection 167(1), consult policy statement [P-188](#), *Supply of a Business or Part of a Business for the Purpose of the Election under Subsection 167(1)*.

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Interest rates in effect for the GST

Prescribed interest rates are adjusted quarterly based on market trends. Penalties and interest related to the GST are calculated daily.

The prescribed annualized interest rates and the penalty rates for the quarterly periods from January 1, 2007, to December 31, 2007, are listed below.

Period	Annualized interest rate (%)	Penalty rate (%)
January 1 to March 31, 2007	3.65	6
April 1 to June 30, 2007	9	*
July 1 to September 30, 2007	9	*
October 1 to December 31, 2007	9	*

* The penalty is equal to: (a) 1% of the amount overdue on the return, plus (b) one-quarter of the amount calculated in (a), multiplied by the number of complete months the return was overdue, to a maximum of 12 months.

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CRA publications

In recent months, the Canada Revenue Agency (CRA) has published or updated the following documents:

■ GST/HST Technical Information Bulletins

- GST/HST Rate Reduction and Real Property ([B-096](#))

■ GST/HST Info Sheets

- GST/HST Rate Reduction and Purchasers of New Housing – July 2007 ([GI-015](#)) (revision)
- Annual Information Schedule for Financial Institutions ([GI-035](#))
- Beverages ([GI-036](#))
- Children's Camps Operated by Public Sector Bodies ([GI-037](#))

■ GST/HST Guides

- Rebate for Tour Packages, Foreign Conventions, and Non-Resident Exhibitor Purchases ([RC4160](#)) (revision)

■ GST/HST Notices

- Questions and Answers on the Cancellation of the Visitor Rebate Program and the Implementation of the New Foreign Convention and Tour Incentive Program ([Notice 221](#)) (revision)

■ GST/HST Memoranda

- Agriculture and Fishing ([4.4](#)) (revision)

■ GST/HST Policy Statements

- Whether Administrative Overhead Costs Fall under Subsection 186(1) of the *Excise Tax Act* ([P-196R](#)) (revision)
- Tax Status of Damage Payments, Whether or not Within Section 182 of the *Excise Tax Act* ([P-218R](#)) (revision)

Other recent tax-related news

- QPP contributions for 2008
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- The Minister of Revenue, Jean-Marc Fournier, is proud to introduce an innovative pilot project - the pre-completed income tax return

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Service Statement

Revenu Québec recently updated its *Service Statement*.

The *Service Statement* provides continuity with commitments already made to the public and businesses. It clearly shows Revenu Québec's desire to provide quality services.



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Transfer of retirement income from one spouse to the other

Starting with the 2007 taxation year, spouses may jointly decide to include a portion of one spouse's retirement income in the calculation of the other spouse's income.

Under the measure, up to half of a taxpayer's eligible retirement income may be transferred to his or her spouse. [Spouses on December 31, 2007](#), may take advantage of this measure, provided they were residents in Canada at the end of the taxation year.

Please note that the Québec income tax withheld from the eligible retirement income must be transferred to the other spouse in the same proportion as the retirement income is transferred.

Eligible retirement income

If a taxpayer is 65 or over, his or her eligible retirement income may include

- life annuity payments under a pension plan or a pension fund;
- payments from a registered retirement savings plan (RRSP);
- payments from a deferred profit-sharing plan (DPSP);
- payments from a registered retirement income fund (RRIF); or
- income from an income-averaging annuity or ordinary annuity, or income accrued under certain life insurance policies.

If a taxpayer is under 65, his or her eligible retirement income may include

- life annuity payments under a pension plan or a pension fund;
- payments received **further to the death of a spouse** from an RRSP, a DPSP, a RRIF or an annuity.

The old age security pension and pensions paid under the Québec Pension Plan and the Canada Pension Plan are not eligible retirement income.

Amount for retirement income

The eligible retirement income that a taxpayer transfers to his or her spouse may entitle the receiving spouse to the age amount, the amount for a person living alone and the amount for retirement income (line 361 of the income tax return), or allow that spouse to increase the amount to which he or she is entitled.

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