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Re: *Additional Comments on Restricted Input Tax Credits*

Dear Messrs. Nowak and Dimitrakopoulos:

This letter follows up on our discussions last December during the Institute's annual liaison meetings with Canada Revenue Agency and the Department of Finance. There, Institute representatives raised the issue of the timing for reporting and applying the rules relating to restricted input tax credits (RITCs). Simply stated, reporting RITCs pursuant to the timeframes required in Harmonized Value-added Tax System Regulations, No. 2 (Regulation) is not possible, and the inability to comply exposes businesses to significant penalties and increased administrative costs. The Institute respectfully submits that, to make the Regulation administrable, it should be amended to allow more time for reporting RITCs. In the meantime, the Institute requests CRA to apply administrative tolerance when auditing the RITCs reported on registrants' returns.

I. BACKGROUND

Tax Executives Institute is the preeminent association of business tax executives. The Institute's 7,000 professionals manage the tax affairs of 3,000 of the leading companies in Canada, the United States, Asia, and Europe and must contend daily with the planning and compliance aspects of Canada's business tax laws.

Canadians make up 10 percent of TEI's membership, with our Canadian members belonging to chapters in Vancouver, Calgary, Montreal, and Toronto, which together constitute one of our nine geographic regions. Our non-Canadian members (including those in Europe and Asia) work for companies with substantial activities in Canada. In sum, TEI's membership includes representatives from most major industries including manufacturing, distributing, wholesaling, and retailing; real estate; transportation; financial services; telecommunications; and natural resources (including timber and integrated oil companies). TEI concerns itself with issues of tax policy and administration and is dedicated to working with government agencies to reduce the costs and burdens of tax compliance and administration to our common benefit. In that connection, TEI remains a strong supporter of simplifying sales tax administration and the goal to have the harmonized sales tax model adopted by all Canadian provinces that impose a sales tax.

II. CURRENT RULES FOR REPORTING RITCS

As a temporary measure beginning July 1, 2010, and effective through June 30, 2018, large businesses and certain financial institutions (other than selected listed financial institutions) must recapture input tax credits for the provincial part of the harmonized sales tax (HST) paid or payable on specified property and services in British Columbia and Ontario. Paragraph 30(d) of the New Harmonized Value-added Tax System Regulations, No. 2 establishes the timing for reporting RITCs as the earlier of: (1) the day on which the tax becomes payable by the registrant,[1] and (2) the day on which that tax is paid.

The penalty for not reporting an amount as required under the RITC rules is substantial: (1) a "base penalty" equal to five percent of the amount that should have been reported minus the amount reported; plus (2) one-fifth of the "base penalty" for each complete month (up to a maximum of five months) that begins on the day the return was required to be filed.

III. HOW BUSINESSES TYPICALLY CAPTURE AND REPORT ITCS AND RITCS

Most businesses capture input tax credits at one of three times: (1) when a supplier's invoice is posted in their systems; (2) when a supplier's invoice is matched with receiving documents; or (3) when an invoice is paid. Once input tax credits have been captured, businesses manage RITC reporting by either incorporating them as part of the input tax credit recording process or as part of a post-recording analytical review. Companies work expeditiously to complete these procedures in a timely manner, but accurate identification and reporting of RITCs

[1] The Act defines when the tax becomes payable as the earliest of: (1) the date an invoice is issued, (2) the date on the invoice, or (3) where there is a written agreement, the due date prescribed in that agreement (unless there is undue delay).

does not occur simultaneously with the issuance of an invoice by a vendor. It is common for a business to receive an invoice from a vendor in one month and to pay that invoice in the next month, especially where invoices require approval by senior company officials. These internal payment approval requirements often reflect the need to comply with governmental regulations such as those implementing provisions of the *Sarbanes-Oxley Act* in the United States.

Under the current rules, the recipient of a utility bill dated January 29 is required to report the related RITC on its January GST return even if it did not receive the bill (and pay it) until sometime in February *after the due date for the January return*. This common situation would both force the registrant to file an amended January GST return and expose the registrant to penalties. These frequently recurring situations also redirect CRA resources away from more productive pursuits to the processing of large numbers of amended returns and related correspondence.

Businesses are working diligently to develop processes, training, and procedures to properly administer the RITC rules. Their good faith efforts, however, cannot solve the underlying issue: The current rules do not reflect the way companies do business, and hence, compliance is impossible. There will always be invoices issued in one month that are received, processed, and paid in another. If left unchanged, the RITC rules effectively guarantee that each originally filed monthly GST return will be inadequate, spawning the need for registrants to serially file amended GST returns. This process will consume valuable resources of both registrants and the government.

IV. RECOMMENDATIONS

In order to put registrants in a position to comply with the RITC reporting requirements, Finance must amend the applicable regulation. The Institute urges Finance to amend paragraph 30(d) of the New Harmonized Value-added Tax System Regulations, No. 2 to permit reporting RITCs either:

a) within 90 days of the invoice date, or
b) in the period in which it is accounted for unless there has been a deliberate or undue delay in the reporting.

Until a legislative change can be adopted, TEI recommends CRA apply administrative tolerance for registrants striving to comply with the filing deadlines in the current RITC reporting rules. Without administrative relief, businesses will be unduly burdened with the costs of developing processes to identify and report these "timing differences," and CRA will be faced with processing a significant volume of amended returns. The proposed relief will not reduce the amount of tax collected, but only result in a small potential difference in the timing of the receipt of that tax.

V. CONCLUSION

Tax Executives Institute appreciates the opportunity to continue to work with CRA and the Department of Finance on this important issue. If you should have any questions, please feel free to contact TEI's Vice President for Canadian Affairs, Rodney C. Bergen, at 604.488.5231 or bergen@jp-group.com. Alternatively, questions may be directed to Kim N. Berjian, Chair of TEI's Canadian Commodity Tax Committee, at 403.233.3807 or kim.n.berjian@conocophillips.com.

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