



INVESTMENT INDUSTRY ASSOCIATION OF CANADA

ASSOCIATION CANADIENNE DU COMMERCE DES VALEURS MOBILIÈRES

## Summary of September 30, 2011 Announced “Full” Harmonization of TVQ and GST

Consistent with statements made in Quebec’s March 2011 budget and affirmed in the Conservative platform for the 2012 election, the federal and Quebec governments announced, on September 30, 2011, the signing of a memorandum of agreement (MOA) to harmonize the tax de vente du Québec (TVQ) with the GST. Until now, the two tax systems both had a value-added tax approach, but were not fully harmonized, and particularly not harmonized in the case of the treatment of financial services.

The Quebec system, in place since 1992, does not apply tax to financial services and allows financial institutions to obtain a full refund of the TVQ paid on their purchases. Instead, a compensatory tax is applied to keep the financial institutions’ tax burden constant compared with what it was before the reform of the sales tax 20 years ago. The 2010 Quebec Budget implemented a temporary increase in the compensatory tax on financial institutions. The original and increased rates to apply for taxation years ending after the date of the 2010 budget and beginning before April 1, 2014 are as follows:

<b>TVQ on:</b>	<b>Original rate</b>	<b>New rate</b>
• Salaries paid by a bank, loan company trust company or securities trading company	2.00%	3.90%
• Salaries paid by a savings and credit union	2.50%	3.80%
• Salaries paid by any other person	1.00%	1.50%
• Insurance premiums and amounts established regarding insurance funds	0.35%	0.55%

The MOA includes provisions for:

- Negotiation of a Canada-Quebec Comprehensive Integrated Tax Coordination Agreement (CITCA) by April 1, 2012 (*this was also the process for Ontario and B.C.*)
- Implementation of the amended TVQ on January 1, 2013.
- Payments by Canada to Quebec of \$2.2 billion – an equivalent payment was or would have been made to all other harmonizing provinces, including the three harmonizing Atlantic provinces, Ontario and B.C. (*we are monitoring the situation in B.C. where a referendum called for the reversal of harmonization*).
- Ongoing harmonization of the tax base for GST and the amended TVQ subject to variances from the GST base not exceeding 5% of the estimated GST base for Quebec, however, GST will be removed from the base for the TVQ (*Quebec has to date charged TVQ on the GST-*

*inclusive price – this will result in some savings, however, these savings will likely be offset by increased irrecoverable TVQ costs).*

- **Application of the GST/HST rules with respect to financial services and financial institutions in Quebec as of January 1, 2011 as follows:**
  - Refunds for the TVQ paid by and the compensatory tax on financial institutions will be eliminated.
  - The temporary increase in the compensatory tax introduced in the 2010 budget will be maintained until March 2014 (*we understand this to mean that a 1.9% compensatory tax on securities firms – 3.9%-2.00% – will continue to apply for securities dealers; according to sources, the existing compensatory taxes will be eliminated entirely for effect January 1, 2013, however the government will create a new deficit reduction surtax on financial institutions to apply from January 1, 2013 until March 31, 2014 in the amount of the extra compensatory taxes that were applied in the 2010 Budget).*
  - The TVQ will continue *not* to apply to financial services (*services that are GST-taxable will be TVQ-taxable*).
  - The GST/HST place-of-supply rules will apply in Quebec.
  - The effect of the above is commissions and other currently GST-exempt financial services provided to Quebec residents and businesses will now be TVQ-exempt rather than zero-rated with a compensatory tax (*this will leave member firms worse off as compared to the 1992 to 2010 period and very possibly worse off compared to currently depending on their business models*).
  - Both governments will examine the issues of avoidance of instances of double taxation or the absence of taxation and maintenance of the neutrality of the tax system for businesses in the financial sector (*the latter is understood to be reference to complaints of some parts of the financial industry that their sectors are overtaxed: mutual funds due to the taxation of advice combined with the funds' trust structure, as well as insurance companies that in some provinces are subject not only to irrecoverable GST, but also to premium taxes. The federal Finance Department has committed verbally to review a number of aspects of the now 20-year-old GST, including financial services, starting this Fall*).
- Continued administration of the GST/HST and TVQ in Quebec by Revenu Québec with the exception that GST/HST and TVQ with respect to Selected Listed Financial Institutions (SLFIs), which includes securities firms, and financial institutions that would be SLFIs if Quebec were a participating province, will be collected and administered by the CRA.
- In addition to financial-service-specific provisions, the changes will start phasing out the restrictions on claims by large businesses for input tax credits on certain expenditures. That is, the full refund of taxes paid by businesses on their purchases of most telecommunications services, meals and entertainment and some other items acquired by large businesses whose taxable sales in Canada exceed \$10 million will not be available until as of January 1, 2021 (eight years following the implementation date of the “more harmonized” TVQ).

After all transitional provisions are worked through, the Quebec government says that the TVQ system will be the same as that applied in Ontario since the implementation of the harmonization agreement with the federal government in 2010.