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SUBJECT RESTRICTED EXPENSES UNDER 67.1 AND GST
SECTION 67.1
SECTION 248(16)
SECTION 12(1)(x)
SECTION 21(h)(h)
SECTION
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Please note that the following document, although believed to be correct at the time of issue, may not represent the current position of the Department.

Prenez note que ce document, bien qu'exact au moment émis, peut ne pas représenter la position actuelle du ministère.

PRINCIPAL ISSUES: Should the restriction on the 67.1 expenses be based on the amount paid (including GST) without any offset for the GST input tax credit?

POSITION: Yes. Also, the GST input tax credit must be included in income or used to reduce the expense after application of the 50% restriction.

REASONS: There is no provision that reduces "the amount actually paid or payable" for the expenses in question.

December 8, 1998

Mr. Bryan Dath
Director
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HEADQUARTERS
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Section 67.1

XXXXXXXXXX has asked us to review our position with respect to the calculation under section 67.1 of the Income Tax Act (the Act), particularly as it applies to the Goods and Services Tax (GST) on expenses for food, beverages or entertainment.

A taxpayer who purchases food, beverages or entertainment in the course of the taxpayer's business is restricted by section 67.1 of the Act on the amount to be claimed for such expenses. However, in view of the treatment of the GST on such expenses, there has been some inconsistency in our responses to questions on how the restriction is calculated.

This is best illustrated by an example of a meal costing a taxpayer \$107.00 which includes GST of \$7.00. The taxpayer would be entitled to obtain a GST input tax credit of \$7.00 which is in effect the return of the \$7.00 paid in respect of the meal. Subsection 248(16) of the Act deems the input tax credit to be assistance from a

government in respect of the property or service received by the taxpayer. Such assistance is included in the taxpayer's income pursuant to paragraph 12(1)(x) of the Act. Section 236 of the Excise Tax Act requires a recapture of 50% of the \$7.00 input tax credit in respect of the meal. This recapture, according to subsection 248(18) of the Act, is deemed to be assistance repaid in respect of the property or service pursuant to a legal obligation to repay all or part of that assistance. Such a repayment, \$3.50 in our example, becomes a deduction pursuant to paragraph 20(1)(hh) of the Act. To summarise the example, the taxpayer paid \$107.00 for the meal and \$3.50 was effectively returned to the taxpayer.

Assuming the cost of the meal was reasonable, paragraph 67.1(1)(a) of the Act deems the amount paid or payable for the meal to be 50% of "the amount actually paid or payable in respect thereof". Although we have previously permitted taxpayers to calculate the 50% restriction on the net amount (\$103.50 in our example) of the meal, the better view is that the 50% restriction should be calculated on the gross amount (\$107.00 in our example) and the net input tax credit included in income (\$3.50 in our example). It is the better view since there is no provision to reduce the "amount actually paid or payable" in respect of the meal by the net input tax credit received on the GST paid in respect of the meal. In our example, this will result in a net allowable deduction of \$50.00 (a deduction of \$53.50 for the meal and an income inclusion of \$3.50 in respect of the net GST input tax credit) as opposed to a net allowable deduction of \$51.75 (50% of \$103.50 [\$107.00 for the meal less the income inclusion of \$3.50]). XXXXXXXXXXXX

A similar result would be obtained if a taxpayer elected under subsection 12(2.2) of the Act to deem an outlay or expense to be reduced by an amount up to a government inducement received in respect of the outlay or expense. Such a deemed reduction in the outlay or expense is not a deemed reduction of "the actual amount paid or payable" in respect of the outlay or expense.

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