

ACC/AFA 100: Journal Entries with Taxes

TRAIN TO LEARN EFFECTIVELY: TIP SHEETS

What are taxes?

Currently in the province of Ontario we have the HST (Harmonized Sales Tax) at 13%. The Harmonized Sales Tax (HST) was introduced in Ontario on July 1, 2010. The purpose of this tax is to combine the federal Goods and Services Tax (GST) of 5% with the Provincial Sales Tax (PST) of 8%.

Example:

When we purchase a pencil for a price of \$1.00, the tax for the item is $\$1.00 \times 0.13 = \0.13 . We add the tax to the price to determine the total amount we pay $\$1.00 + \$0.13 = \$1.13$. The total can also be found by $\$1.00 \times 1.13 = \1.13 .

When should we record journal entries with taxes?

Businesses pay taxes when making purchases and collect taxes when making sales. It is important that when recording transactions that taxes also be recorded within journal entries when stated.

How should we account for HST?

1. Sales

When making a sale a business collects taxes from customers **BUT** this money is not the business's to keep, it must be remitted to the government. A separate account called HST Payable is used to record the amount of taxes collected from customers that is then owed to the government. When we sell an item, we must collect sales tax at the set percentage and send it to the government. Businesses must collect and remit the HST and receive a HST Registration Number.

As a seller, we

- 1) Calculate the tax
- 2) Collect tax
- 3) Accumulate this tax money in a separate account.
- 4) Pay the money to the government on a regular basis.

2. Purchases

When a business purchases goods and services they have to pay HST. However, a business is often entitled to recover the amount of taxes paid. A separate account called HST Recoverable is used to record the amount of taxes paid by businesses that they are owed back from the government. This new account is an Asset account because it

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represents money owed to the business by the government. We will assume that all HST paid by the business for expenses is recoverable. Recoverable taxes will be placed in an account called "HST Recoverable".

Examples:

The transactions below show how we will calculate sales and purchases with the HST rate at 13%.

Transactions for Sales:			
July 8 <i>Sales Invoice</i> No. 50 to J. Greenley, \$250 for services performed, plus HST			
08-Jul	A/R - J. Greenley	282.50	
	Fees Earned		250.00
	HST Payable		32.50
July 18 <i>Cash Sales Slip</i> No. 100 to E. Webb, \$85.50 plus HST			
18-Jul	Bank	96.62	
	Fees Earned		85.50
	HST Payable		11.12
Transactions for Purchases			
July 3 <i>Cheque Copy</i> No. 105, Chamber Bros., payment for car repairs 750 plus HST			
03-Jul	Automobile Expense	750.00	
	HST Recoverable		52.50
	Bank		802.50
July 5 <i>Purchase Invoice</i> from Glen Printing, \$100 for office supplies plus HST			
05-Jul	Office Supplies	100	
	HST Recoverable		13
	Accounts Payable		113

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Remitting the HST

HST must be remitted (sent) to the government at a later point (normally monthly). The business will have both HST Payable and HST Recoverable. The HST Recoverable is subtracted from the HST Payable and the balance (leftover amount) is paid to the government. If the result is negative, then the business receives that amount from the government.

What are the advantages of HST?

The key advantages of the HST for businesses are:

- 1) Simplifies paperwork - there is only one tax system to keep track of (HST), not two (PST and GST).
- 2) Increased refunds - businesses are eligible to get a refund on the HST that has been spent on business-related expenses. Since the HST is 13%, businesses are eligible for more refunds.

The key advantages for the federal and provincial governments is:

- 1) More tax revenue - the HST is collected on a wider range of goods and services, so there is more tax revenue that is collected.
- 2) Less administration - the former tax system is now merged and collected together, so only one tax administration agency is needed.

End consumers of goods and services must pay more money in taxes, so one could argue that they do not benefit from the HST. On the other hand, since more money is available for governments to provide services such as roads and schools, one could argue that the end consumer does benefit from the HST.