

ACCOUNTING FOR GST ABSORBED BY TRADERS

INTRODUCTION

1. Generally, as a consequence of the introduction of the 3% GST, there is a one-off price increase equal to the GST imposed. Take, for example, the case where the cost of goods of a trader before 1 April 1994 was \$80 and the sale price was \$100, thereby achieving a gross profit of \$20.
2. On 1 April 1994, assuming that this trader, who is GST-registered, wished to maintain the same profit margin, he would raise the price of goods which he previously sold for \$100 by 3% to \$103. The output tax of \$3 he has to account to the Comptroller of GST is found simply by applying the factor of 3/103 to the GST-inclusive price of \$103. Exhibit 1 shows the full details of how the profit is arrived at and GST accounted for.

Exhibit 1 : Post-GST prices with the same profit margin and GST payable

Selling price	\$	103.00	Output tax	\$	3.00
Less:					
Purchase price		82.40	Input tax		2.40
		————			————
		20.60	Net GST Payable to Comptroller		0.60
					====
Less:					
Net GST payable to Comptroller		0.60			
		————			
Profit		20.00			
		=====			

3. To maintain competitiveness and customer goodwill, some GST-registered traders have announced that they will absorb the GST of the customers who buy from them by paying the tax on their behalf. Questions have been raised on how GST is to be properly accounted for when a GST-registered trader decides to absorb GST ie. not to pass the effect of the price increase due to the imposition of GST to his customer.

- The purpose of this Practice Note is to illustrate the correct method of accounting for GST by taxable traders who wish to absorb the GST on their sales.

ADMINISTRATIVE PRACTICE

- With effect from 1 April 1994, if a supply of goods or services is made for a consideration in money, its value shall be taken to be such amount as, with the addition of the tax chargeable, is equal to the consideration. This is clearly provided under section 17(2) of the GST Act. Therefore where a GST-registered trader charges or receives a sum of money for full payment of goods sold, the amount charged or received has to be regarded as being inclusive of the GST payable on the sale. This “price-inclusive” principle has to be applied to all taxable sales, including sales where the traders wish to “absorb” the GST.
- A GST-registered trader who wishes to fully absorb the GST on his sales will not raise his price. Using the example cited earlier, his sale price remains at \$100. However, pursuant to section 17(2) of the GST Act, as this \$100 is now inclusive of GST at 3%, it actually comprises a reduced price of \$97.09 plus GST of \$2.91. This is the correct way of accounting for GST by a trader who wishes to absorb the customers’ GST. Exhibit 2 shows the computation of the profit where the price is not increased after the imposition of GST and how GST is accounted for.

Exhibit 2 : Post-GST prices where the GST is absorbed and the GST payable

Selling price	\$	100.00	Output tax	\$	2.91
Less:					
Purchase price		82.40	Input tax		2.40
		_____			_____
		19.60	Net GST Payable to Comptroller		0.51
					====
Less:					
Net GST payable to Comptroller		0.51			

Profit		19.09			====

- Therefore, where a GST-registered trader wishes to absorb the GST on his sales, the correct method of accounting for GST is to treat the price paid by the

customer as inclusive of GST. Exhibit 3 shows how the price-inclusive method is correctly applied in a transaction for GST purposes while Exhibit 4 shows the correct accounting entries.

Exhibit 3 : Correct method of accounting for GST where the GST is absorbed

Selling price	\$ 97.09
Add:	
Output GST	2.91

Total amount due from customer	100.00
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Exhibit 4 : Accounting entries under the correct method of accounting for GST where the GST is absorbed

Dr Cash	\$ 100.00	\$
Cr Sale of item		97.09
Cr Output tax		2.91

8. IRAS understands that some traders who absorbed the GST on their sales have adopted an alternative method of accounting for GST. Instead of treating the price paid by the customer as **inclusive** of GST, they have treated it as **exclusive** of GST. Using the same example of \$100 received, they have accounted for GST at \$3 and charged this as an expense. Exhibit 5 shows what is done incorrectly under this method and Exhibit 6 shows the accounting entries when this method is used.

Exhibit 5 : Incorrect method of accounting for GST where the GST is absorbed

Selling price	\$ 100.00
GST at 3%	3.00

Amount inclusive of GST	103.00
Less:	
GST absorbed (Expense)	3.00

Total amount due from customer	100.00
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Exhibit 6 : Accounting entries under the incorrect method of accounting for GST where the GST is absorbed

	\$	\$
Dr Cash	100.00	
Dr Expense (GST paid on behalf of customer)	3.00	
Cr Sale of item		100.00
Cr Output tax		3.00

9. Since section 17(2) requires GST-registered traders to regard the consideration received on their sales as inclusive of the GST chargeable, the GST-exclusive method referred to at paragraph 8 is, therefore, incorrect and cannot be used. Traders who have adopted the GST-exclusive method are to take steps immediately to switch to the correct method. In the meantime, any tax invoice issued by a trader adopting the incorrect GST-exclusive method in accounting for the GST chargeable will not be accepted by the Comptroller of GST as a tax invoice for GST purposes. In other words, the purchaser will not be able to claim input tax on that purchase from such a trader. A sample of such an unacceptable "tax invoice" is given at Exhibit 7.

Exhibit 7 : Sample of an unacceptable invoice issued by a trader using the incorrect GST-exclusive method

	TAX INVOICE	Gallery Photo Supplier
		888 Jalan Ang Teng
Customer's name		Singapore 1953
Photo Studio		GST Ref No : MX-1234567-X
899 Scott Rd		Date: 6/6/94
Singapore 0923		Invoice No: 01234

Description	Total (\$)
Yashica (1 unit)	100.00
GST	<u>3.00</u>
Total amount payable	103.00
Less GST credit	<u>3.00</u>
Net amount payable	100.00
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Thank you. We look forward to being of service to you again.