

SALES TAX HARMONIZATION

*Planning for the HST in Ontario
and British Columbia*

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HST IN ONTARIO AND BRITISH COLUMBIA



Agenda

- Basic Concepts
- Place of Supply Rules
- Transitional Rules
- ITC Restrictions
- Planning and Preparing for HST
- Impact on the Construction Industry



BASIC CONCEPTS

Ontario and British Columbia harmonize with the GST

- effective July 1, 2010
- administered by CRA/CBSA
- GST tax base adopted
- exceptions
 - point of sale rebates
 - phase in ITCs for certain items

- The provinces of Ontario and British Columbia have announced the harmonization of their provincial sales tax with the federal GST, effective July 1, 2010. This new Harmonized Sales Tax (“HST”) will operate in much the same way as HST in the participating provinces of Newfoundland and Labrador, Nova Scotia, and New Brunswick. However, the HST in each province will have distinct differences.
- The cornerstones for this sales tax harmonization are the Memoranda of Agreement between Canada and the provinces of Ontario and British Columbia that set out the framework for the new HST. Under these agreements, both levels of government have agreed to conclude deals, subject to legislative approval, that will:
 - provide the policy framework for the application of a single, value-added sales tax in Ontario and British Columbia, effective July 1, 2010, which will be administered by the Canada Revenue Agency and the Canada Border Services Agency;
 - enable both provinces to:
 - provide consumer exemptions (through point-of-sale rebates) on a limited number of items;
 - phase in certain input tax credits (“ITCs”) over a transitional period of up to eight years; and
 - establish provincial rebate rates and thresholds for items such as new housing and public service bodies;
 - negotiate possible employment arrangements with the federal government (in Ontario and British Columbia) for provincial employees affected by the change; and
 - provide the provinces with federal transfer payments (\$4.3 billion to Ontario and \$1.6 billion to British Columbia).

BASIC CONCEPTS



2010 Ontario Sales Tax Harmonization

- rate - 13%
 - federal component - 5%
 - provincial component - 8%
- temporary ITC restrictions
- point of sale rebates
- public service bodies

- The proposed HST in Ontario will have a combined tax rate of 13%, consisting of a provincial component of 8% (which matches the existing general rate of the Ontario Retail Sales Tax (“ORST”)) and a federal component of 5% (the current GST rate).
- As for QST, the legislation will restrict the recovery of the provincial component of HST by large businesses and financial institutions on telecommunications expenses (excluding internet access and 1-800 numbers), meals and entertainment expenses, fuel for licenced road vehicles, licenced road vehicles under 3,000 kilograms (and associated parts and certain services), and energy not used to manufacture goods for sale or in farming operations.
- Ontario will provide point of sale rebates for children’s clothing and footwear; children’s car seats and booster seats; diapers; feminine hygiene products; books (including certain audio books); print newspapers; and prepared food and beverages costing not more than \$4.
- Rebates of the provincial component of the HST will be available to public service bodies, although the rebate rates will differ from the rates available for the federal component of the HST. The rebate rates available for the two components of the tax are noted below.

| | Provincial Component of Ontario HST | GST |
|-------------------------------|--|------------|
| Municipalities | 78% | 100% |
| Universities and colleges | 78% | 67% |
| School boards | 93% | 68% |
| Hospitals | 87% | 83% |
| Charities and qualifying NPOs | 82% | 50% |

2010 Ontario Sales Tax Harmonization

- Ontario commodity taxes still exist
 - insurance
 - motor vehicles
 - alcohol
 - fuel and gasoline
 - tobacco

- After the implementation of the HST, Ontario will continue to levy a tax of 8% on certain types of insurance, such as premiums paid on group insurance policies, which are currently subject to ORST, but will be exempt from HST. However, there will be no change to the sales tax exemption on automobile insurance.
- The government has announced that it will retain a retail sales tax on private transfers of used motor vehicles. Therefore, the new Ontario HST will not create inequities between motor vehicles sold privately and sales by used car dealerships. This tax treatment will be consistent with the other HST provinces.
- Under the ORST system, tax is collected on alcohol sold at a licenced eating establishment at a rate of 10%, and at a rate of 12% on alcohol sold through retail stores. With the introduction of the new HST, the tax rate on these products will decrease to 8%.
- In order to maintain its current revenue level, the Ontario government has indicated that it will adjust the fees, levies and charges that currently apply to alcohol products to compensate for the decreased tax rate. In addition, the government is proposing to replace other alcohol fees and charges with taxes in order to augment their operational structure and improve clarity.
- In addition, Ontario will continue to levy separate commodity taxes on fuel, gasoline and tobacco.

BASIC CONCEPTS



2010 B.C. Sales Tax Harmonization

- rate – 12%
 - federal component – 5%
 - provincial component – 7%
- temporary ITC restrictions
- point of sale rebates
- public service bodies

- The HST in British Columbia will have a combined rate of 12%, comprised of a federal component of 5% (the current GST rate) and a provincial component of 7% (the current general rate for Social Service Tax purposes).
- British Columbia has elected to implement temporary input tax credit restrictions on the provincial component of the HST paid in respect of certain types of expenses, similar to Ontario, with the exception of fuel for licenced road vehicles which escapes British Columbia HST due to the point of sale rebate noted below.
- British Columbia will provide point of sale rebates for the provincial portion of the tax on fuel, books, children's sized clothing and footwear, children's car seats and booster seats, diapers, feminine hygiene products and residential energy consumption.
- Certain public service bodies will be entitled to a rebate of the provincial component of the HST. As in Ontario, the rebate rates available will differ from the rates that are available for the federal component of the HST. The announced rebate rates for eligible institutions are:
 - 75% for municipalities
 - 87% for school authorities
 - 75% for universities and public colleges
 - 58% for hospital authorities
 - 57% for registered charities and qualifying NPOs.

2010 B.C. Sales Tax Harmonization

- British Columbia commodity taxes still exist
 - motor vehicles
 - alcohol
 - carbon tax

- The province will retain a retail sales tax on private transfers of used motor vehicles. This is consistent with the other HST provinces. In this way, the new British Columbia HST will not create inequities between motor vehicles sold privately and sales by used car dealerships.
- Licenced establishments will only be required to collect British Columbia HST at a rate of 12% on all sales of liquor products. However, the mark-ups on liquor at retail stores will be increased to maintain the shelf price of liquor at its current level. Liquor sold at retail stores in British Columbia is currently subject to a 10% provincial sales tax.
- The carbon tax, which was recently introduced in British Columbia, will be unaffected by the implementation of HST in the province and will continue to be applied to certain purchases of fuel.

PLACE OF SUPPLY RULES

PLACE OF SUPPLY RULES



Supply made in Canada?

- goods
 - sale
 - lease
- services
- intangibles
- real property

- First, it is necessary to determine if a supply has been made in Canada. If so, a second set of rules determines whether or not the supply is considered to be made in a province in the harmonized zone. Where this is the case, HST at either 12% or 13% may apply to the transaction.
- Goods are considered sold at the place where the goods are delivered or made available to the recipient. Thus, goods supplied by way of sale that are delivered to the U.S., but invoiced to an Ontario address, would not be subject to GST/HST. However, the terms of sale can impact where the sale takes place, irrespective of the actual delivery point. If title changes at the premises of a US vendor, the sale will be considered to take place outside Canada, even if the vendor arranges shipping on behalf of the purchaser.
- Where goods are supplied by lease, the supply is deemed to be made (for the entire lease period) where possession or use of the goods is first given to the recipient, regardless of the billing address of the recipient.
- Services performed in whole or in part in Canada are subject to GST/HST. Only where a service is performed entirely outside Canada, will GST/HST not apply. For example, the place of supply for most consulting services provided by a Canadian organization will be Canada, even if a majority of the work is done outside Canada, since a portion of the service will likely be performed in Canada.
- A supply of intangible personal property is considered to be made in Canada if the property may be used in whole or in part in Canada, or the property relates to real or tangible personal property, or a service to be performed in Canada. For example, the place of supply for the worldwide distribution rights for a product will be Canada, since the intangible can be used in whole or in part in Canada.
- For GST/HST purposes, a supply of real property, or a service in relation to real property, is considered to be made in Canada if the property is situated in Canada.

PLACE OF SUPPLY RULES



Supply made in a participating province?

- substantive changes effective May 1, 2010
 - services
 - intangibles

- On February 25, 2010, the Department of Finance released the details of the proposed amendments to the HST place of supply rules, the self-assessment and rebate rules and the imported taxable supply rules related to the provincial component of HST. The changes will generally apply to taxable supplies made in Canada on or after May 1, 2010, and any supply made after February 25, 2010 and before May 1, 2010 if the consideration for the supply has not become due and has not been paid before May 1, 2010.
- These amendments were required as many of the current HST place of supply rules for services and intangibles contained a default rule that applied where it was not the case that a service was supplied in a single province. This rule selected the location of the supplier to determine whether a sale is subject to the provincial component of the HST. This was perceived to create an unacceptable bias to Ontario.
- These amendments propose that the HST place of supply rules for intangible personal property and services be changed so that there is less emphasis on the supplier's location and greater emphasis on where the purchaser of the intangible personal property or service is located. These changes will also help to accommodate different rates of the provincial component of the HST.
- The place of supply rules for tangible personal property and real property will not be affected significantly by these proposed amendments.

PLACE OF SUPPLY RULES



HST place of supply rules

- goods supplied by way of sale
 - destination based
 - based on where the goods are delivered or made available
 - includes delivery by mail or courier

- The general rule for goods is that tax follows the goods. In other words, the supply of tangible personal property by way of sale is considered to be made in a participating province if the goods are delivered or made available in one of those provinces.
- The F.O.B. point under any contract for the sale of the goods is irrelevant in determining the delivery point of the goods. Regardless of where the supplier or recipient are located, the place of supply is determined based on where the goods are made available to the recipient.
- These rules encompass delivery by mail or courier, and also include the transfer of goods to a common carrier retained on behalf of the recipient to ship the goods to a participating province.
- For example, a Toronto parts manufacturer ships components from its Ontario warehouse to a customer in Moncton, New Brunswick. If the delivery is by its own truck, the shipment will be subject to 13% HST since the supply would be considered to have been made in New Brunswick. If the manufacturer contracts with a common carrier to deliver the goods to New Brunswick on a prepay and charge basis, the sale will also be subject to HST. This is the case even if the manufacturer sells the goods F.O.B. its own shipping dock.
- If these same goods were sold by the manufacturer today, the terms were F.O.B. shipping point, but the customer arranged to have the parts picked up, the place of supply would be Ontario and the transaction would be subject to GST only. However, after July 1, 2010, where an Ontario manufacturer sells goods from its Toronto warehouse, F.O.B. its shipping dock, to a customer anywhere in Canada, and the customer arranges to have the parts picked up by its own truck or by common carrier, HST at 13% will apply to the sale, since the supply is considered to have been made inside a participating province.

PLACE OF SUPPLY RULES



HST place of supply rules

- goods supplied by ST/LT lease
 - rental (3 months or less)
 - where possession transferred
 - lease (over 3 months)
 - ordinary location at start of each lease interval
- real property

- The place of supply rules for HST relating to tangible personal property supplied otherwise than by way of sale varies depending on the lease term.
- Short-term leases (for a period of three months or less) are taxed based on the location where possession or use is made available to the recipient.
- For example, a rental of a truck for a move from Mississauga, Ontario to Calgary, Alberta will be subject to HST at 13% on or after July 1, 2010, even though more than 50% of the use of the truck will be outside the participating province of Ontario.
- Where goods are leased for a term in excess of three months (other than the supply of a specified motor vehicle), each lease interval (i.e., the period covered by a lease payment) is considered to be a separate supply, and the place of supply will be the ordinary location of the goods at the beginning of each lease interval.
- For example, the lease of a computer ordinarily located in Vancouver, British Columbia for the first 14 months of a 36-month lease will be subject to 12% HST on the first 14 lease payments. If, midway through the 15th month, the computer is transferred to Toronto, Ontario, the lease payment covering the 15th month will continue to be subject to HST at 12%, but subsequent payments will be subject to 13% HST.
- In the case of motor vehicles leased for a period in excess of three months, it is the province of registration which determines the place of supply.
- Real property is considered supplied in a province if the property is situated in that province. Any supply of property situated in more than one province and/or outside Canada will be considered separate supplies of the property situated in each province and outside Canada.

PLACE OF SUPPLY RULES



HST place of supply rules

- Services in relation to tangible personal or real property
 - if property primarily located in HST province
 - TPP not remaining in same province

- Certain types of services have specific HST place of supply rules, and the general rules will not apply to them. There are specific place of supply rules currently in place for these type of services, and they will remain largely unchanged. We have provided a list of these services later.
- The supply of a service in relation to property will be made in a participating province if the property is situated primarily (more than 50%) in the participating provinces when the Canadian element of the service begins. The supply of the service is proposed to be made in the participating province in which the greatest proportion of the property is located.
- Where services are performed in relation to tangible personal property situated primarily in the participating provinces, and the property does not remain situated in one province or those provinces for the duration of the performance of the service, the service will be considered to be made in a participating province if the service is performed primarily in participating provinces. In that case, the service will be considered supplied in the participating province where the greatest proportion of the service is performed.
- Where a service is performed in relation to real property and the real property is situated in Canada and outside Canada, only the proportion of the service that relates to real property located in Canada may be deemed to be made in a participating province.
- Tie-breaker rules exist to select the appropriate participating province in the event that no single province can be determined under the above rules. The rule essentially means that 13% must be collected until a province harmonizes with a rate of something other than 8%.
- “In relation to” – drawing up specs, testing, inspecting, appraising, inventorying, enhancing value, securing, buying or selling.

PLACE OF SUPPLY RULES



HST place of supply rules

- Services in relation to tangible personal property
 - example 1 – property remains
 - example 2 – property moves between provinces

Example 1

- A national company headquartered in Ontario is hired by an Alberta company to store its corporate documents in archives, for a period of one year, for a single fee. The part of the archives situated in Alberta when the service begins to be performed and that remains stored in Alberta throughout the year is 40% of the total archived collection. The portion of the archives that is located in Ontario when the service begins and remains stored in Ontario throughout the year is 60%.
- The tangible personal property is situated in Alberta and Ontario when the service begins and remains situated in those provinces for the entire service period. Furthermore, the tangible personal property is situated primarily in the participating provinces when the storage service is performed and the participating province where the greatest proportion of the property is situated at that time is Ontario. The supply of the service is considered to be made in Ontario, and HST at 13% would apply.

Example 2

- A company in New Brunswick is hired by another company in New Brunswick to conduct tests on a vehicle. The proportion of the service that is performed in New Brunswick is equal to 60% and the proportion of the service performed in Quebec is 40%. The vehicle is situated in New Brunswick when the New Brunswick portion of the service is performed and is situated in Quebec when the Quebec portion of the service is performed. However, the vehicle is moved from New Brunswick to Quebec after the New Brunswick portion of the service is performed.
- The tangible personal property does not remain in the same province while the service is performed. Furthermore, the tangible personal property is situated primarily in the participating provinces when the New Brunswick portion of the service is performed, the services as a whole are performed primarily in participating provinces, and the greatest proportion of the service that is performed in the participating provinces is performed in New Brunswick. As a result, the supply of the service is considered to be made in New Brunswick and subject to HST at 13%.

PLACE OF SUPPLY RULES



HST place of supply rules

- Services in relation to real property
 - example 1 – property in two provinces
 - example 2 – property in/outside Canada

Example 1

- An Ontario company hires another Ontario company to provide maintenance services with respect to two of its buildings in Ontario and one of its buildings in Alberta, all of which are of equal size. The real property that is situated in Canada to which the services relates, is situated primarily in the participating provinces and the greatest proportion of the real property is located in the participating province of Ontario. The supply of the service is considered to be made in Ontario and subject to HST at 13%.

Example 2

- A survey company in Alberta is hired by a firm located in British Columbia to survey land that borders British Columbia and the United States. The land in British Columbia represents 15% of the total land and the land in the United States represent 85% of the total land.
- The real property to which the service relates that is situated in Canada (i.e., 15%) is situated in the participating provinces, and the participating province where the greatest proportion of the real property is situated is the participating province of British Columbia. The proportion of the supply of the service that relates to real property in Canada is deemed to be made in British Columbia and would be subject to HST at 12%. The proportion of the service that relates to real property situated outside Canada is deemed to be made outside Canada and, therefore, is not subject to GST/HST.

PLACE OF SUPPLY RULES



HST place of supply rules

- personal services
 - other services
 - province of address of recipient
- OR
- HST province in which greatest proportion of service is performed

- A personal service (one where the service is performed in the physical presence of the individual to whom it is rendered) performed primarily in the participating provinces will be considered supplied in the HST province where the greatest proportion of the service is performed. Personal services exclude advisory, consulting or professional services.
- Where the supplier of a non-personal service has obtained, in the normal course of business, the recipient's business or residence address in Canada that is most closely connected with the supply, the supply will be considered made in that province. If the supplier does not obtain the home or business address of the recipient, the supply will be considered made in the province where any other address is obtained that is most closely connected with the supply. If no address is obtained, and the service is performed primarily in the participating provinces, the supply will be considered made in the province where the greatest proportion of the service is performed.
- Tie-breaker rules apply where no one participating province can be determined under the above rules, which essentially mean that tax must be collected at 13%.

PLACE OF SUPPLY RULES



HST place of supply rules

- services
 - example 1 – consulting services
 - example 2 – legal services
 - example 3 – online services

Example 1

- A tax consulting firm located in Edmonton, Alberta is hired to conduct a tax savings review of a company with a business address in Chilliwack, British Columbia. During the course of the work, 70% of the work is performed in Edmonton, while the remaining 30% is performed at the company's Chilliwack address. As the supplier obtains the recipient's British Columbia business address, the service will be subject to HST at 12%, as the supply will be deemed to be made in British Columbia.

Example 2

- A law firm with offices in a number of provinces across Canada is hired to supply legal services in Ontario and Quebec for a U.S. based company. The service provider does not obtain a Canadian business address or any other address in Canada that is used by the U.S. based customer. 60% of the services performed in Canada are performed in Ontario. The services will be subject to HST at a rate of 13%, as the greatest portion of the services performed in participating provinces are performed in Ontario.

Example 3

- An online service provider, with branch offices in British Columbia, Ontario and New Brunswick specializes in the provision of editing and translation services to clients electronically over the internet. The clients send electronic versions of the documents by email to the service provider to be edited or translated with the resulting documents returned to the email address of the clients. The services are performed by employees of the service providers in any of the three locations. The services are typically provided 30% in British Columbia and 35% in each of Ontario and New Brunswick. The service provider does not obtain the address of its clients.
- The Canadian element of the service is performed primarily (50% or more) in the participating provinces, but no one province has the greatest proportion. An equal portion of the service is performed in Ontario and New Brunswick, which have the same HST rate of 13%. As indicated by Rule 3, the service provider will be required to charge HST at the rate in effect in each of those two provinces, which is 13%.

PLACE OF SUPPLY RULES



Special rules

- repair services
- brokerage services
- litigation services
- personal services
- services provided at location specific events
- trustee services to registered plans
- telecommunication services
- computer-related services and Internet access
- passenger, freight and mail delivery services

- Special place of supply rules exist for repair services. Where a service provider receives tangible personal property of another person for the purpose of repairing, maintaining, cleaning, adjusting or altering the property, the place of supply of the service, and any parts supplied in conjunction with the service, is the province to which the goods are returned to the recipient.
- For example, a Vancouver-based company sends equipment to a repair shop in New Brunswick. The goods are repaired and shipped back to the company in Vancouver. HST at 12% applies to the service and/or any goods supplied in conjunction with the service, as the place of supply will be British Columbia. Alternatively, if the goods in question were sent from Manitoba and returned to that province after the repair, GST only (and possibly provincial sales tax) will apply.
- Conversely, where goods are repaired in Manitoba and subsequently shipped back to a recipient in Nova Scotia, 13% HST applies, even though the service is performed entirely outside the participating provinces.
- A maintenance service contract is considered to be the supply of a service (the parts are considered incidental to the service) made where the property is located when the contract is entered into. Where there is a single supply of maintenance contract that covers equipment or real property located in both a participating province and a non-participating province, the rules on services in respect of tangible personal property, or services in respect of real property, will apply based on the location of the property at the time the agreement is entered into.

PLACE OF SUPPLY RULES



Intangible personal property

- IPP primarily used in participating provinces
 - greatest proportion of use
 - value and physical presence
 - recipient address

- The place of supply of IPP in Canada where the rights can only be used in a single participating province can be determined quite easily (i.e., supply made in that particular province). However, in many cases the supply of IPP encompasses a number of provinces within Canada which may complicate the determination of the place of supply.
- Where Canadian rights are primarily limited to the participating provinces, the rights will be considered supplied in the participating province with the greatest proportion of use of the rights.
- If there is no limitation on the use of the rights, the value of the consideration is \$300 or less, and if the supply is either made in the presence of a recipient or his agent at the supplier's permanent establishment or through a vending machine in a participating province where the IPP can be used, the supply will be regarded as having been made in that province.
- If the previous rule does not apply, then if the supplier of the rights has obtained, in the normal course of business, the recipient's business or residence address in Canada that is most closely connected with the supply, and the rights can be exercised in the province, the supply will be considered made in that province. If the supplier does not obtain the home or business address of the recipient, the supply will be considered made in the province where any other address is obtained that is most closely connected with the supply, and the rights can be exercised in that province.
- If the previous rule does not resolve the place of supply issue, a tie-breaker rule applies that requires the supplier to collect 13%.

PLACE OF SUPPLY RULES



Intangible personal property

- No limitation on use of rights in Canada
 - value and physical presenceOR
 - recipient address

- Rights under an agreement may not be limited to the participating provinces and in many cases may be granted throughout Canada. Where the rights are not primarily used in the participating provinces but may occur anywhere in Canada, the place of supply rules will differ from those discussed previously.
- Where the value of the consideration is \$300 or less, and if the supply is either made in the presence of a recipient or his agent at the supplier's permanent establishment or through a vending machine in a participating province where the IPP can be used, the supply will be regarded as having been made in that province.
- Otherwise, if the supplier obtains the recipient's address (home or business or an address closely connected with the supply), and the address is located in a participating province where the supply can be used, the supply is deemed to be in that province.
- A tie-breaker rule will apply to require the supplier to collect 13% if needed.

PLACE OF SUPPLY RULES



Place of Supply Rules

- example 1 – event tickets
- example 2 – travel pass
- example 3 – golf passes
- example 4 – memberships

Example 1

- A person has purchased season tickets to the symphony, including ten concerts in Ontario, three concerts in Nova Scotia and one in Quebec. Since the supply of the IPP can only be used primarily in the participating provinces and the greatest proportion of the IPP can only be used in Ontario, the place of supply will be in Ontario at a rate of 13% HST.

Example 2

- An unlimited bus pass is sold for \$500 which allows the traveler to use a bus service anywhere in Nova Scotia and New Brunswick. The traveler has provided a home address, which is in New Brunswick, at the time of the purchase. The place of supply will be in New Brunswick based on the recipient's home address.

Example 3

- A person purchases a golf pass from an Ontario golf course allowing the player 20 rounds of golf at any of their related golf courses situated across Canada, for the cost of \$250. Since the value falls under the \$300 limit, the pass can be used less than primarily in or outside the participating provinces, the rights include Ontario and the pass was purchased from the supplier at an Ontario permanent establishment, the deemed place of supply would be in Ontario, and the golf pass would be subject to HST at 13%.

Example 4

- An individual in Ontario acquires a membership costing more than \$300 in a professional organization. The membership rights can be exercised in any province. The organization acquires the home address of the individual to which the membership card and invoice can be sent. Since the membership rights can be exercised less than primarily in or outside the participating provinces, the supply is deemed to be made in Ontario, where the purchaser resides, requiring the supplier to charge HST at 13% as noted above.

PLACE OF SUPPLY RULES



Intangible personal property (HST)

- Special rules for:
 - IPP relating to tangible personal property
 - IPP relating to real property
 - IPP relating to services

- A supply of IPP related to real property and tangible personal property is generally considered made where the property is primarily situated.
- IPP related to services is deemed supplied in one province where the services are all performed in that province. Where the supplier cannot determine where these services will be provided, the registrant must go back to the general rules applicable to determining the place of supply for intangibles to apply the correct rate on such supplies.



TRANSITIONAL RULES

TRANSITIONAL RULES



General rules

- consideration paid or payable on or after July 1, 2010
- “payable”
 - date consideration becomes due (invoice date or due date under agreement)
 - override rule

- HST will generally be payable at 13% in Ontario, and 12% in British Columbia, where the consideration for a taxable supply becomes payable or is paid without becoming due on or after July 1, 2010.
- Under the general timing of liability rule, GST/HST on the consideration for a supply is payable on the earlier of the day payment is made and the day the supplier issues an invoice. The payment terms on an invoice are irrelevant.
- However, if there is an undue delay in issuing an invoice, GST/HST becomes payable when the invoice would have been issued if there had been no delay. In addition, if either the date of an invoice or the payment date under a written agreement is earlier than the date the invoice is issued, GST/HST becomes payable on the earlier date.
- An override rule stipulates that if GST/HST is not otherwise payable by the last day of the calendar month after the calendar month in which any of the following events takes place, it becomes payable on that day:
 - in the case of a sale of tangible personal property (other than a sale referred to below), the buyer acquires ownership or possession of the property;
 - in the case of a sale of tangible personal property on approval, consignment, sale-or-return basis or similar terms, the buyer acquires ownership of the property or re-supplies it to someone other than the seller; and
 - in the case of a supply under a written agreement for construction, renovation, alteration or repair of real property, or of a ship or other marine vessel when the work is reasonably expected to last more than three months, the work is substantially completed.

TRANSITIONAL RULES



Transitional rule dates

- key dates for HST:
 - announcement date: October 14, 2009
 - specified pre-implementation date: May 1, 2010
 - implementation date: July 1, 2010

- The “announcement date” is the date on which the transitional rules were released. The purpose of the announcement date is to grandfather any existing contracts that may have been formalized prior to the notice of the intended change in sales taxes, similar to a grandfathering provision. HST will generally not apply to consideration that becomes due, or is paid without having become due, on or before October 14, 2009.
- The “implementation date” of July 1, 2010 is the date on which the HST comes into effect. Any taxable supplies made on or after this date will be subject to HST.
- Consideration that is paid or becomes due on or after May 1, 2010 will generally be subject to HST where the goods are delivered or services are performed on or after July 1, 2010. For example, where a company has purchased a specialized piece of machinery and has prepaid for the machinery after May 1, 2010, but before July 1, 2010, with delivery of the machinery taking place after July 1, 2010, HST will still apply to the transaction.
- Payment terms are irrelevant for purposes of the HST timing rules.

Tangible personal property

- delivery and transfer of ownership on or after July 1
 - if invoiced from May 1, HST
 - if invoiced or paid before May 1, no HST
- delivery or transfer of ownership before July 1, no HST

- HST will not apply to tangible personal property supplied by way of sale where the consideration is paid or has become payable prior to July 1, 2010, and the property is delivered and ownership has transferred prior to that date.
- Where the transfer of ownership and the delivery of the tangible personal property takes place on or after July 1, 2010, HST will generally apply to the supply. This includes situations in which the consideration for the supply becomes due, or is paid without having become due, on or after May 1, 2010 and before July 1, 2010.
- The HST on any prepayments made for tangible personal property is determined by the “specified pre-implementation date” (i.e., May 1, 2010) and not the implementation date. For payments made on or after May 1, 2010, where the delivery and transfer of ownership of the goods takes place on or after July 1, 2010, these payments will be subject to HST.
- For example, the purchase of a piece of machinery that is paid for on June 1, 2010, with delivery and the transfer of ownership to the purchaser occurring on July 15, 2010 (post-implementation), will be subject to HST.
- This provision is, in essence, an anti-avoidance rule put in place to deter taxpayers from prepaying for a supply in advance of the implementation date in order to avoid paying the provincial component of the HST on the purchase.

Examples

- sale of tangible personal property
 - example 1 – deferred payment
 - example 2 – progress payments

Example 1 – deferred payment

- A customer in Ontario entered into an agreement to purchase production machinery in May 2010, without having to make any payments until August 2010. Would GST or HST apply to this sale? The customer actually receives ownership and possession of the machinery in June 2010, but will not receive an invoice for payment until August 2010.
- In this situation, since the production machinery is delivered to the customer in June 2010, HST will not apply to this purchase.

Example 2 – progress payments

- In June 2010, Company A, located in British Columbia, contracts with Company B to produce a mould for use by Company A. Under the written agreement, Company A must make six equal monthly payments from June 2010 to November 2010. Possession and ownership of the mould will be transferred in November 2010. Does GST or HST apply to the payments made?
- Since ownership and possession of the mould is transferred on or after July 1, 2010, HST applies to the total consideration for the mould, including the payment made in June 2010.

TRANSITIONAL RULES



Services

- performed on or after July 1, 2010 – HST
- substantially all (90% or more) performed before July 1, 2010 – no HST
- straddle implementation date – prorate

- Generally, the HST will apply to services supplied on or after July 1, 2010. However, the HST will not apply if all or substantially all (90% or more) of the service is completed before July 1, 2010.
- Services performed on or after July 1, 2010, for which the consideration becomes due or is paid on or after May 1, 2010 and before July 1, 2010 would also be subject to HST. The HST paid on these services must be filed with the GST/HST return for the reporting period that includes July 1, 2010.
- Apportionment may be required for services that straddle the July 1, 2010 implementation date, where all or substantially all (90% or more) of the service is not complete by July 1, 2010. For example, if a consultant is hired to perform a service for four months starting in June 2010 and the service is completed in September 2010, what rate of tax would apply? HST would apply to the services performed in July, August and September, which would be 75% of the total consideration.

TRANSITIONAL RULES



Intangibles

- intangible personal property
 - e.g., intellectual property or contractual rights
- memberships
 - lifetime memberships

- Generally, the HST will apply to consideration that becomes due or is paid without having become due, on or after July 1, 2010 for supplies of intangible personal property by way of sale. For example, if a person purchases the right to reproduce certain portions of a book in July 2010, the HST will apply to the transaction.
- On the other hand, HST will not apply where consideration is paid or becomes due for the supply of intangible personal property before July 1, 2010. To extend the above example, the same book rights paid for in June 2010 would not be subject to HST.
- Memberships are generally defined as a right, which is intangible personal property. However, for purposes of the transitional rules, enrollment in a club, association or organization is considered a supply of a service. Therefore, the purchase of a membership will follow the transitional rules laid out for services.
- One variation from the general rules applies to the consideration for a lifetime membership in a club, organization or association any part of which becomes due, or is paid without having become due, after October 14, 2009 and before July 1, 2010. In such cases, where that part exceeds 25% of the total consideration for the membership, the amount in excess of the 25% portion will be treated as having become due on, and not to have been paid before, July 1, 2010, and will be subject to HST.

Examples

- services and intangibles
 - example 1 – partial payment
 - example 2 – advance payments
 - example 3 – annual subscriptions

Example 1 – partial payment

- We receive a partial payment of \$10,000 on May 22, 2010 for computer services that will be performed in Ontario after July 1, 2010. The total consideration for the services is \$50,000. The invoice for these services will be issued in August 2010 and the customer will pay the remaining balance once they receive the invoice. Does GST or HST apply the computer services performed?
- HST applies to the partial payment of \$10,000 and the outstanding \$40,000 balance paid by the customer in August 2010, since the services are being performed for the customer in the harmonized zone after July 1, 2010.

Example 2 – advance payments

- We entered into an agreement for the provision of computer hardware maintenance services for a computer located in British Columbia on May 1, 2010. The payments are due on the last day of the previous month for each particular month covered by the agreement. As a result, the monthly payment for the July 2010 services is due on June 30, 2010. Does GST or HST apply to the payment made on June 30, 2010
- Since the service is performed in the harmonized zone and the actual services will be performed on or after July 1, 2010, the payment made on June 30, 2010 will be subject to HST, since it is consideration for services provided after the implementation date.

Example 3 – annual subscriptions

- We have purchased an annual subscription to an information service that will commence on May 1, 2010 and we are required to make four payments for this service. The payments for this service are due on May 1, 2010, June 1, 2010, July 1, 2010 and August 1, 2010. We will not make these payments before they are actually due. Will HST apply to any payments made for the information subscription?
- HST does not apply to the payments made on May 1, 2010 and June 1, 2010, since the payments became due prior to July 1, 2010. The payments made on July 1, 2010 and August 1, 2010 will be subject to HST, since they only became due after the HST implementation date of July 1, 2010.

Commercial real property and Leases

- reverse collection rules
- sale
- lease, licence or similar arrangement

- Generally, a taxable sale of real property includes any sale of real property other than used residential real property and certain personal-use real property sold by individuals. On taxable sales (as opposed to leases, licences, or other similar arrangements) of real property, GST/HST is generally not collected by the vendor; instead, the tax is self-assessed and remitted by the purchaser where the recipient of the supply is a GST/HST registrant or the supplier is a non-resident of Canada. These rules are referred to as the “reverse collection rules”.
- HST will apply to the consideration for the sale of taxable real property (other than residential housing) where both possession and ownership of the property is transferred on or after July 1, 2010. Where the possession or ownership of taxable real property is transferred prior to July 1, 2010, the transaction will not be subject to HST.
- For leases of real property (including commercial parking passes), HST will apply to the part of a lease interval in respect of a lease, licence or similar arrangement that occurs on or after July 1, 2010 if invoiced on or after May 1.
- It should be noted that a concession is made where the lease interval commences prior to July 1, 2010 and terminates before (not *on*) July 31, 2010. In this case, HST will not apply to the consideration for that lease interval.
- Similar rules apply to the lease or licence of tangible personal property.
- The HST will also generally apply to consideration that becomes due, or is paid without having become due, on or after May 1, 2010 and before July 1, 2010, for a supply of property by way of lease, licence or similar arrangement, to the extent that the consideration is for the part of a lease interval that occurs on or after July 1, 2010 (except if the lease interval terminates before July 31, 2010).

TRANSITIONAL RULES



Real and tangible personal property

- examples

- example 1 – commercial property
- example 2 – rental of office space
- example 3 – vehicle leases

Example 1 – commercial property

- A registrant purchases a commercial building in Ontario that is fully leased to retail tenants. The registrant entered into the agreement of purchase and sale with another registrant prior to May 1, 2010, and will receive ownership and possession after July 1, 2010. Will the HST tax rate apply to the acquisition?
- The taxable supply of the commercial building is subject to HST at 13%, since ownership and possession are transferred after July 1, 2010. The exception to this general rule only applies to the purchase of a new or substantially renovated residential complex and not to commercial real property.

Example 1 – rental of office space

- Rent for office space is paid on the 15th of every month for the next month. We have issued post-dated cheques to our landlord for the entire lease period, ending December 31, 2010, and have included GST at 5% with each post dated cheque. Would GST or HST apply to the payment dated June 15, 2010 that covers the rent for the month of July 2010?
- Since the lease interval for the office space being rented begins on July 1, 2010, HST applies to the June 15, 2010 payment. This is because the consideration for the July lease interval becomes due on July 1, 2010 and, as a result, HST applies to that portion of the lease.

Example 2 – vehicle leases

- We entered into 36-month leases for passenger vehicles for use by our employees in April 2010. A lease payment is due on June 1, 2010 for the lease interval covering the period June 1, 2010 to June 30, 2010. The terms of the lease payment are net 30, so we will not make the lease payment for the June lease interval until July 2010. Does HST apply to the payment that we make for the June lease interval?
- The lease payment made in July 2010 is in respect of the June 2010 lease interval. Since this lease interval occurs before July 1, 2010, it will not be subject to HST.

Miscellaneous items

- subscriptions
- continuous supplies
 - straddle implementation date
- deposits

- HST on subscriptions for newspapers, magazines and other periodicals will be applied differently from other tangible personal property delivered after the implementation date. Where a lump sum amount is prepaid for a subscription before July 1, 2010 and the subscription period continues on past July 1, 2010, HST will not apply. The prepayment for subscriptions is unlimited, but the total payment must be received prior to July 1, 2010. Where a reader has a subscription agreement signed prior to the implementation date, but the payments are made at regular intervals (e.g., monthly), HST will apply to any charges after July 1, 2010
- A continuous supply is a service provided through a wire, pipeline or a similar conduit or satellite or other telecommunications facility, such as electricity, gas, cable and telephone services. Continuous supplies will not be subject to HST where the supply has been delivered prior to the implementation date, even where the invoice is paid or becomes payable after July 1, 2010.
- Where the supplier cannot reasonably determine the actual delivery date of a continuous supply, the consideration for the supply will be prorated in equal parts based on the number of days in the period to which the consideration is applicable. For example, on an invoice for telecommunication services billed from June 16, 2010 to July 15, 2010, HST would apply to 50 per cent of the amount payable, based on a prorated period of 15 days in July.
- Where a deposit is given in respect of a supply, the deposit is not regarded as consideration for the supply unless and until the supplier applies the deposit against an amount payable for that supply. It is only at that time that tax becomes payable on the amount placed as a deposit. The CRA administratively defines a deposit to be an amount given by a recipient as security for the performance of an obligation. This rule applies whether or not the deposit is refundable.

TRANSITIONAL RULES



Miscellaneous items

- admissions
- transportation services
- progress payments/holdbacks

- An admission to a place of amusement, seminar, activity or other event is considered a supply of a service for HST implementation purposes. Where an advance ticket is sold on or after May 1, 2010 and prior to July 1, 2010, with the event held on or after July 1, 2010, HST will apply to the sale or to those events.
- Notwithstanding the general transitional rules for services, HST will not apply to the consideration for freight and passenger transportation services that are performed on or after July 1, 2010 if the service is part of a continuous journey or freight movement that begins before July 1, 2010. For example, if an individual purchases a ticket to fly from Toronto to Ottawa on June 29, 2010, and returns from Ottawa on July 3, 2010, HST would not apply to the ticket price.
- A special rule applies to passenger transportation passes, under which the HST does not apply to the supply of a transportation pass if the pass period begins before July 1, 2010 and ends before August 1, 2010.
- Progress payments that become due, or are paid without having become due, after October 14, 2009 and before July 1, 2010, in respect of a contract to construct, renovate, alter or repair real property will be subject to HST to the extent that the progress payment can reasonably be attributed to property or services delivered on or after July 1, 2010. The supplier must remit the HST provincial component related to the post-June 2010 property or services in the GST/HST return that includes July 1, 2010.
- Similarly, a holdback from a progress payment will also be subject to HST, to the same extent that any part of the progress payment itself can reasonably be attributed to property or services delivered on or after July 1, 2010.
- Where a real property contract will take more than 3 months to complete, the portion of consideration not otherwise due before the last day of the calendar month that follows the month in which the construction is substantially (90%) complete, becomes due and payable on that day. Notwithstanding this timing rule, the portion of that payment that is attributable to construction that takes place on or after July 1, 2010 will be subject to HST.

TRANSITIONAL RULES



Refunds and exchanges

- full refund
- consideration exceeds original price
- consideration less than original price
- on or after November 1, 2010

- It is inevitable that some goods purchased prior to the implementation of the HST in Ontario and British Columbia will later be returned by the customer or exchanged for similar or different goods.
- Goods that were subject to retail sales tax at the time of purchase prior to July 1, 2010, and that are exchanged on or after July 1, 2010 and before November 2010, are subject to three possible outcomes:
 - If a full refund, refund the GST and the PST
 - If the replacement good costs less than the returned good, refund partial GST and PST
 - If the replacement good costs more than the returned good, charge HST on the difference.
- If retail sales tax did not apply when the goods were purchased prior to July 2010, and the goods are exchanged on or after July 1, 2010 for goods of greater value requiring a payment, then the three outcomes are:
 - If a full refund, refund the GST
 - If the replacement good costs less than the returned good, refund the GST charge HST on the full value of the replacement good
 - If the replacement good costs more than the returned good, charge HST on the full value of the replacement and credit the GST
- Any consideration that is paid for an exchange that is made on or after November 1, 2010 will be subject to HST. No adjustments for retail sales tax will be available at the point of sale for goods returned on or after November 1, 2010. However, the purchaser is entitled to claim a refund for tax paid in error.

Rebates

- RST rebate for residential real property
- goods and services used in commercial activities
- goods and services for SLFIs and others required to self-assess

- A RST rebate is available to residential real property contractors in British Columbia and Ontario for RST paid on construction materials that are purchased or produced for the contractor's own use, held in inventory as of close of business on June 30, 2010, and used in residential real property contracts that are subject to HST. This rebate will not apply if the contractor or another party is able to recover the RST. Contractors will be required to file the rebate claim with the British Columbia Ministry of Finance or the Ontario Ministry of Revenue on or before December 31, 2010.
- A refund is available for PST paid on goods and services acquired after October 14, 2009 and before May 1, 2010, that are delivered or performed on or after July 1, 2010, and that are exclusively for use in the course of commercial activities. If HST had been applicable to such purchases, a full recovery would typically be available, so a rebate is provided to remove the extra charge for the provincial retail sales tax.
- A refund of the PST paid on goods and services acquired after October 14, 2009 and before May 1, 2010, that are delivered or performed on or after July 1, 2010, is available to organizations required to self-assess the provincial component of the HST under the transitional rules.
- The purpose of the refunds is to prevent a double counting of the provincial tax due on such supplies.
- Refunds must be filed by December 31, 2010.

TRANSITIONAL RULES



Returns and general refunds

- final RST returns
- refunds for tax paid in error

- Both British Columbia and Ontario final retail sales tax returns must be filed on July 23, 2010. Supplemental returns will be due on the 23rd day of the month following the month in which BCSST and ORST have been paid or collected. Ontario requires all supplemental RST returns to be filed by November 23, 2010. As previously noted, all outstanding RST will be considered payable on October 31, 2010. BC requires all supplemental returns filed by January 23, 2011.
- Both ministries have confirmed that refunds will continue to be available for the 4-year period in the case of tax paid in error.



BREAK

ITC RESTRICTIONS

ITC RESTRICTIONS



Overview

- temporary ITC restrictions for provincial component
- large businesses - \$10M in taxable supplies, including affiliates
- restrictions similar to those in Quebec
- “recapture” restricted ITCs
- simplified reporting method election

- Both ON and BC’s sales tax harmonization plans included temporary restrictions on the claiming of ITCs on a number of expenses by “large businesses”. These ITC restrictions will apply only to the provincial component of the HST and will be in place for five years, after which they will be phased out equally over the next three years. Both provinces agreed to limit restrictions to those currently applicable in Quebec (none such in NB, NS or Nfld.& Lab).
- A “large business” is a business with taxable sales made in Canada, or outside Canada through an establishment in Canada, including those of any associated affiliate, and including zero-rated sales, in excess of \$10 million in the last fiscal year before the recapture period, and certain FIs or persons related to a FI. Supplies of capital real property, financial services and goodwill are excluded from the calculation, and, unlike in Quebec, public service bodies are not subject to the ITC recapture rules. The recapture period is a year beginning July 1 and ending June 30. Special rules exist to deal with businesses that become LBs during the year, that acquire control of other businesses that are not LBs, that amalgamate, that acquire substantially all the assets and business operations of another business or that become related to a restricted FI.
- LBs will be required to recapture ITCs claimed for the provincial portion of the HST paid in ON and BC by reporting gross ITCs on one line, with two separate recapture fields being added for the restricted provincial component, one for ON and one for BC. LBs cannot merely forego claiming the ITCs. LBs subject to the recapture will be required to file their GST/HST returns using NETFILE. Recapture must happen in the reporting period when the ITCs may first be claimed.
- A LB may make an election to use an estimation, installment and reconciliation approach to account for the recapture of ITCs. The election must be filed with the CRA after the end of the LB’s fiscal year and would apply for at least one year, as follows:
 - estimate the amount of recaptured ITCs for the fiscal year based on the ITC recapture requirement during its most recently completed fiscal year, along with any ITC recapture requirement anticipated due to business changes from the previous fiscal year;
 - make installment payments in each reporting period of an installment year, beginning three months after the start of the fiscal year and ending three months after the end of the year, based on the estimate of recaptured ITCs; and
 - at the end of the fiscal year, reconcile any differences between the estimated and actual amount of recaptured ITCs during the year, and make any adjustment on the return for the last installment reporting period.
- Rules exist to require self-assessment if restricted expenses are pre-purchased before the HST comes into effect or items are imported from outside BC or ON.

Telecommunications services

- internet access and web site hosting
- 1-8XX and other toll-free services
- telecommunications equipment
- equipment repairs and maintenance
- non-telecommunication services
- proxy rates

- Although LBs will generally be restricted from claiming ITCs on the provincial component of HST in respect of telecommunication services, they will not be restricted in respect of the following expenses:
 - Internet access services and web-site hosting services (telecommunication services provided wirelessly which include Internet access or access to electronic mail are not considered to be “Internet services” and, consequently, are subject to the ITC restrictions, e.g., Intranet, Blackberry or similar featured services);
 - “1-8XX” toll-free service (which includes the related line rental) as well as optional services such as long distance call routing, overflow routing, interactive voice response and calling number identification;
 - purchase, lease and rental of telephone systems (but not lines), paging equipment and any associated installation, parts, and repairs for such equipment;
 - non-telecommunication services, including directory advertising, building surveillance or protection services, news services offered by press agencies, telephone order management services, database access services, services provided through 1-900 lines and directory assistance services;
- If a LB receives an invoice that includes both specified telecommunication services and other services and/or goods that are not subject to recapture, but the vendor has not clearly indicated the portion of the provincial component of HST that is subject to restriction, certain proxies may be used to determine the appropriate portion to claim. In ON, there are three proxies as follows:
 1. If the invoice includes telecommunication services, other services and goods, 14% of the consideration is deemed attributable to other services and goods
 2. If the invoice includes telecommunication services and other goods (but no other services), 11% of the consideration is deemed attributable to the goods
 3. If the invoice includes telecommunication services and other services (but no goods), 4% of the consideration is deemed attributable to the other services.
- BC has announced only one proxy rate: if an invoice includes telecommunications services **and** other services and/or goods, then 5% of the consideration is deemed attributable to the other services and/or goods.
- Currently, some telecommunication suppliers indicate on their invoice the recoverable and non-recoverable portions of the QST charged on their services. It is anticipated that they will provide a similar indication of the ON and BC breakdown between supplies that are not restricted and supplies that will be subject to the ITC recapture.

Restricted meals and entertainment

- expenses subject to the 50% income tax limitation
- exceptions to the 50% income tax limitation

- GST recovery is generally restricted to 50% of the tax paid with respect to meals and entertainment expenses, where the deductibility of the expense is restricted to 50% under the *Income Tax Act*. These same M&E expenses will be the focus of the temporary ITC restrictions that have been placed on the provincial portion of the ON and BC HST paid by LBs.
- Unlike other recapture provisions, if the organization is repaying 50% of the M&E-related GST after the year end, that is when the recapture of the provincial component must be recognized.
- In addition to common business meal expenses, also included within the scope of the restrictions are: tickets to sporting events; tickets to theatres and concerts; admissions to places of amusement; and the cost of box rentals at arenas and stadiums.
- There are seven main exceptions to the 50% income tax restriction, for which full ITCs are available for both the federal and provincial portions of the HST:
 - where M&E are made generally available to all employees at a particular location (limited to 6 occasional events per year – e.g., annual picnic, golf day, Xmas party);
 - M&E for which a taxpayer is compensated by another party, and the amount for M&E is specified on the billing to the other party;
 - where these expenses are made on behalf of employees at a remote or special work site;
 - M&E provided by a registered charity as a fund-raising event;
 - M&E on an airplane, train or bus, which are included in the fee for travel;
 - where the amount is required to be included in an employee's taxable benefit calculation; and
 - where the provider is in the business of providing M&E, and would normally provide them for compensation (i.e., the restrictions do not apply to restaurants, caterers, nightclubs, etc.).

Energy – electricity, gas, steam or other fuel

- restriction does not apply to manufacturing goods for sale
- apportionment is possible
 - energy study
 - elect for proxy rates

- Energy must be used directly in the manufacturing process to be excluded from restriction. Test is similar to previous retail sales tax exemption - power used in equipment for air conditioning, lighting, heating or ventilation of the production site will be restricted as these uses are not considered to be directly related to manufacturing.
- Where energy is used for dual purposes, LBs can apportion usage between qualifying and restricted uses. An engineering study may be required (approx \$4k) to apportion the costs between the restricted and unrestricted uses if separate metering capabilities are unavailable.
- As an alternative to an energy study, ON and BC each allow the use of a production proxy as a simplified method to determine the specified energy attributed directly to the production process.
- If a LB's most significant business activity falls into one of 24 categories based on the North American Industry Classification System for 2007 (NCAIS Canada 2007), it would be eligible to use one of three fixed percentages to determine the portion of specified energy considered to be used directly in the production of tangible personal property for sale. The percentages reflect the average production activities in a particular industrial sector.
- For LBs whose most significant business activity falls within the first grouping, the production proxy would be 96%. Examples in this category include oil and gas extraction and chemical manufacturing. The second category includes food manufacturing and fabricated metal product manufacturing, with a production proxy of 87%. The final group of categories include clothing manufacturers, printing and related support activities and miscellaneous manufacturing, with a production proxy of 70%.
- In order to use the proxy instead of tracking the actual energy used in manufacturing activities, a large business must file an election with the CRA before the beginning of the recapture period. LBs whose most significant business activity does not fall within the 24 categories or whose production activities are primarily outside of ON or BC would not be entitled to use the proxy.
- SR&ED activities that qualify for income tax purposes will also qualify for recovering the provincial component of the HST paid on energy consumed in those activities. Either actual consumption or the use of a proxy formula based on salaries and wages will be permitted to recover the qualifying portion. If a business is also using a mfg. proxy, the SR&ED proxy is applied first, with the production proxy applied to the balance.

Energy

- natural gas
 - “buy-sell” agreement
 - sales contract
- electricity
 - lease of commercial office space

- ITCs are available on transportation charges if natural gas is being supplied under a “buy-sell” agreement. Under a “buy-sell” agreement, the purchaser acquires natural gas from a broker or producer and typically takes delivery of the gas at a point outside the province. The purchaser then enters into a buy-sell agreement with a distributor under which the distributor purchases the gas at a certain price, sells it back to the purchaser at the same price and agrees to deliver the natural gas to the purchaser in the province. In this case, the transportation charge is considered a separate supply, since the purchaser is only entering into an agreement with the distributor for the delivery of the gas, since they previously took possession of the gas outside the province.
- However, if the natural gas is being supplied under a “sales contract”, the provincial component of the HST paid by a large business will be restricted. Under a sales contract, a distributor sells natural gas to a purchaser and agrees to supply and deliver the gas to them. Even if the delivery or transportation charge is shown separately on the invoice, it is still considered to be one transaction – the supply of natural gas. In essence, the transportation charges are viewed as incidental to the supply of the natural gas and the HST provincial component applicable to the delivery charge is subject to the ITC restrictions.
- A tenant under a commercial lease of office space may agree that the rent includes a fixed amount and ancillary expenses, such as the cost of the electricity used by the lessee. It must then be determined if the cost of the electricity is included in the rent. This is governed by the intent of the parties when they entered into the lease. The landlord is considered the recipient of the electricity if it is determined to be included in the rent and where the landlord is a large business, it is subject to the restrictions on claiming an ITC for the HST provincial component paid to purchase the electricity. Under these circumstances, the tenant is entitled to claim an ITC in respect of the rent, including the portion of the rent that relates to the electricity provided by the landlord under the commercial lease of the office space. The landlord is restricted, and will typically pass the unrecovered tax on as additional rent.

ITC RESTRICTIONS



Licensed road vehicles

- road vehicles < 3,000 kg licensed for use on public highway
- repairs and maintenance
- fuel acquired in Ontario

- LBs will be restricted from claiming ITCs on the provincial component of HST related to the supply of a road vehicle that must be registered to travel on a public highway where the empty kerbside weight of these vehicles is less than 3,000 kilograms. Typically, the purchase of a passenger car would be restricted, as are the first series of light trucks and vans. There is no restriction applied to vehicles that are intended for exclusive use on private land or roads and never intended for public roadways, or to trailers, semi-trailers or detachable axles.
- Full ITCs are available on the HST paid for normal repair and maintenance performed on licensed road vehicles. However, ITCs must be recaptured on the provincial component of HST for parts that are not considered repair and maintenance parts (e.g., after-market equipment) and are purchased for a vehicle within 12 months of a car being purchased in or transferred into ON or BC.
- If a LB acquires a motor vehicle for resale, but uses the vehicle before reselling it, (e.g., dealership demonstrator), the business would be required to recapture 2% of the provincial component of the ITC attributable to the cost of the vehicle for each month or part thereof the LB uses the vehicle.
- Registrants in ON will be restricted from claiming ITCs on the provincial component of HST paid on the purchase of fuel for use in restricted vehicles. However, the purchase of fuel acquired for vehicles having a gross mass equal to or exceeding 3,000 kilograms is eligible for a full ITC. Additionally, full ITCs are available for the use of light diesel fuel (i.e., "fuel oil") regardless of vehicle weight. This restriction will not apply to any purchases of fuel for these same vehicles in BC since a point of sale rebate for the provincial component of the HST will apply to these supplies.
- ON, in its recent budget, has provided an energy tax credit partly to compensate for the increase in tax on fuel under the HST.



PLANNING AND PREPARING FOR HST

PLANNING AND PREPARING FOR HST



Impact on registrants

- systems
 - comprehensive review
 - identify resource requirements
 - test system changes
 - transitional issues
 - post-implementation review

- Organizations can prepare for the HST transition by being proactive. A comprehensive review of the impact of the HST implementation on all systems and procedures is strongly recommended. Custom software may require the assistance of a programmer to effect the changes. Businesses using “off-the-shelf” systems may find themselves relying on software developers to provide a “patch” to handle the changes.
- In either situation, once tax codes and tax tables have been updated, thorough testing of the system changes with sample transactions, in advance of the effective date, is necessary to ensure that billing and purchasing systems are working effectively to minimize potential exposures or customer issues.
- From a systems perspective, a major challenge facing organizations is the impact of the transitional rules on their systems. The retail sales tax rates may still be required for certain transactions. For example, a refund or adjustment made after July 1, 2010 could be subject to HST or retail sales tax depending on the date of the original purchase. However, many systems can only accommodate one tax rate, the current rate, for coding purposes. Consequently, these organizations must design and implement temporary manual procedures to identify situations when retail sales tax applies. This may be of particular concern to registrants who must remit the tax for HST purposes or credit an expense for retail sales tax.
- Following any major system modification or implementation, there should always be a post-implementation review to ensure that executed changes are working effectively. Organizations with software programs that produce exception or query reports can mitigate the risk associated with the understatement of recoveries by designing macros or queries to flag possible input tax credit errors or inconsistencies on purchases made after July 1, 2010. Simple reasonableness tests can also be performed on the purchase and sales journals as a means of identifying variances.

PLANNING AND PREPARING FOR HST



Impact on registrants

- updating systems
 - billing
 - A/R and A/P

- There are several key systems areas which require the attention of all registrants:
- **Billing systems**
 - Clearly, a top priority for all organizations is to adjust billing or invoicing systems, including point-of-sale terminals or cash register software, to ensure that the correct rates of GST and HST are charged and collected as of July 1, 2010.
 - Items to consider, when required, include the different GST/HST rates, 5%, 12% and 13%.
 - The tax status applied to products, services and intangibles may also change. Many supplies that were exempt under the retail sales tax rules are likely to be taxable for HST purposes.
 - In some cases, a point-of-sale rebate will be available for certain items identified as not previously taxable under the retail sales tax system, such as children's clothing, books and feminine hygiene products (in both British Columbia and Ontario).
 - Systems will need to provide for retail sales tax billings and billing adjustments on or after July 1.
- **A/P systems**
 - Tax tables and vendor tax codes used in accounts receivable and accounts payable systems must be adjusted to reflect the new tax rates.
 - Input tax credit restrictions may require systems to track the provincial and federal component of the HST.
 - Self-assessment processes must also be considered depending on the organization's activities. Retail sales tax required purchasers of taxable supplies to self-assess on the purchase price where tax was not charged by the vendor. This self-assessment will no longer be required by organizations in commercial activities. Self assessment will be required where restricted items are imported after July 1 or are prepaid before May 1 to attempt to avoid the restrictions.

PLANNING AND PREPARING FOR HST



Impact on registrants

- updating systems (continued)
 - credit and debit notes
 - purchase orders
 - journal entries and programmed payments

- **Credit and debit note systems**

- These systems may not be integrated with the A/R and A/P systems and require separate attention.
- Where refunds, rebates and adjustments are made on sales, the supplier decides if GST/HST is applied on a credit to a registered customer under certain conditions. Such transactions will require additional consideration to account for remittances that may be required on GST/HST credited back to registrants.
- Credit and debit notes issued to unregistered customers must contain an adjustment of all taxes charged on the original invoice. This may require an adjustment of retail sales tax after the July 1, 2010 transition.

- **Purchase orders**

- In many systems, the tax codes used to create purchase orders drive the tax status of transactions throughout the system, requiring these codes to be adjusted for the new rates.
- The place of supply rules for the various HST rates must also be considered when generating purchase orders, especially in situations where services or intangibles are involved.
- In many cases, purchase order systems also drive the journal entries for input tax credit claims for acquisitions. The programmer will need to consider the input tax credit restrictions in place for purchases by large businesses to ensure that the organization does not recover excessive HST on these purchases.

- **Journal entries and programmed payments**

- It is common for many organizations to use standard or recurring journal entries on automatic payments (e.g., monthly intercompany charges for rent, management fees, etc.) and equal billings. Where these items include a GST component, an adjustment may be required to account for the new HST that might apply to these transactions.
- The purchase or sale of an intercompany supply, where retail sales tax did not apply before, may now be subject to HST, such as in the case for legal fees in Ontario.

PLANNING AND PREPARING FOR HST



Impact on registrants

- updating systems (continued)
 - reimbursements and allowances
 - payroll

- **Employee expense reports and allowance reporting**

- Quite often, employee expense reports and allowances are handled in a completely separate accounting system, which increases the possibility that required changes to factors and rates used in these systems could be overlooked. Due diligence is required in this area, not only during the transition, but also later on when expense reports are submitted, to ensure that the new factors are being used. This is by far the biggest exposure area we have seen related to the tax transitions surrounding previous GST rate changes.
- Large businesses must be aware that the input tax credit restrictions will apply to employee expense reimbursements as well as to invoices billed directly to the employer.
- The special rules currently applied to ITCs including luxury automobiles and club membership fees, will also apply for HST purposes.

- **Payroll and taxable benefit calculations**

- The previous GST rate change created changes to rates and factors used to calculate GST/HST remittances on certain taxable benefits. The movement to HST in Ontario and British Columbia will also cause changes to the rates and factors that must be used to remit GST/HST on taxable benefits for employees located in these provinces, and these changes must be incorporated into payroll and taxable benefit systems.

PLANNING AND PREPARING FOR HST



Tax administration

- **simplified reporting**
 - all HST is reported with GST
 - fewer Ontario or British Columbia returns to be filed
- **separate disclosure of HST on invoice**
 - assist customer with applying ITC restrictions

- All GST and HST will be reported on a single GST/HST return. After the final Ontario and British Columbia sales tax returns are filed, it is anticipated that many taxpayers will no longer have to file sales tax returns with Ontario and British Columbia, resulting in an administrative savings for many registrants.
- Since Ontario will continue to collect sales tax on taxable insurance premiums and some organizations will continue to self-assess tax on insurance premiums charged by unregistered insurance providers or vendors, a return for the self-assessment of tax may be required. In addition, Ontario registered insurers will be required to file a return for the sales tax collected on taxable insurance premiums.
- Suppliers that sell goods or services that will be subject to the temporary ITC restrictions discussed above may wish to disclose the amount of the unrecoverable provincial component of HST included on the invoice that is issued to their customers. This will make it easier for the customer to identify the amount of HST they have paid that is unrecoverable for ITC purposes, and will eliminate any need for their customer to track the GST and HST portions of tax paid separately in their systems. These businesses, being experts in the services they provide, are also in a better position to determine the amounts of HST collected that would be subject to the ITC restrictions. This is especially true where a portion of their supplies would not be subject to the restrictions.
- It should be noted that many telecommunication service providers making taxable supplies in Québec already separately disclose the unrecoverable QST that is collected on their invoices, making it much easier for a customer to claim the correct amount of QST as an ITR.

Electronic filing requirements

- effective July 1, 2010 for those with:
 - annual taxable supplies > \$1.5 million
 - subject to temporary ITC restrictions
 - subject to transitional housing rules
- four methods available
- new information fields for NETFILE

- The CRA has announced proposed changes to the filing requirements for GST/HST registrants, which will be effective July 1, 2010. Currently, only certain registrants may file a GST/HST return electronically. As a result of the proposed changes, all registrants, including those registrants that file a return with Revenu Québec, will be able to file electronically.
- In addition, effective July 1, 2010, the following groups will be **required** to file their GST/HST returns electronically:
 - GST/HST registrants (including associates) with greater than \$1.5 million in annual taxable supplies (except charities);
 - all registrants required to recapture ITCs for the provincial portion of the HST on certain inputs in ON or BC; and
 - builders affected by the transitional housing measures announced by ON or BC.
- Organizations that are the subject to the proposed ITC restrictions will be required to file their GST/HST returns electronically using GST/HST NETFILE. Other than NETFILE, there are three electronic filing methods available to taxpayers: GST/HST TELEFILE; GST/HST Electronic Data Interchange (EDI); and the newly created GST/HST Internet File Transfer (GIFT).
- In addition, there will be new GST/HST reporting requirements that will be added to the GST/HST NETFILE return. All LBs and FIs that are subject to the ITC recapture rules will be required to report the gross ITCs on one line, with two separate recapture fields for the restricted provincial component of HST, one for ON and one for BC.
- The recapture must be reported in the period in which HST became payable (except for M&E where the recapture can match the GST reporting), and any failure to report recaptured ITCs must be corrected through an amended return. GST/HST registrants that are required to file electronically, as of July 1, 2010, but continue to file paper returns after this date may be subject to penalties.



IMPACT ON THE CONSTRUCTION INDUSTRY

IMPACT ON THE CONSTRUCTION INDUSTRY



Contract bid considerations

- real property supply and install services
 - “supply” element not subject to RST
 - full price subject to GST/HST
- RST no longer a cost for new contracts
- HST mostly recoverable

- Currently, in general terms, labour provided with respect to the supply and installation of fixtures and items in the construction of real property is not subject to tax. Further, the contractor is regarded as the end consumer for RST purposes, so construction materials and fixtures must be acquired tax-paid, or if manufactured by the contractor, tax must be self-assessed on the manufactured cost. The RST on these fixtures and materials will be passed on to the purchaser of the construction services as an added cost. Exceptions did apply for fixtures and materials that could be acquired exempt by the end user under a production equipment exemption.
- With the implementation of HST beginning July 1, 2010, contractors must collect HST on the full contract price, which will subject both the labour and fixture and materials to HST on the price billed to the purchaser. However, the RST will be eliminated from the cost of materials used in these contracts and contractors will be in a position to recover any HST that is paid on their inputs to the construction process, effectively reducing the net cost of materials.
- This is a significant change that must be considered when bidding on new construction contracts commencing on or after July 1, 2010. The eliminated RST that was previously incurred on construction materials should not be included in the bid contract’s estimate of costs, or the costs will be overstated and the bid may not be competitive with those prepared by other bidders.
- With the advent of the HST, construction contracts will appear on their face to be more expensive. For most purchasers engaged in commercial activity, the HST paid to contractors will be fully recoverable. This will not be the case for MUSH sector bodies – municipalities, universities, schools and hospitals – that cannot recover the provincial component of the HST fully.
- New housing rebates are available for landlords constructing new or substantially renovated residential rental properties. Otherwise, the provincial component would not be recoverable to a residential landlord.

IMPACT ON THE CONSTRUCTION INDUSTRY



Existing contracts

- RST embedded in materials on hand at June 30
- contracts subject to HST from July 1
- transitional residential rebates
- no rebates for other real property

- As noted on the previous page, a contractor is liable to pay the RST on any materials purchased or manufactured to be used in the construction process. In addition, the contractor must pay or self-assess RST on equipment used during the construction process, including equipment imported into the province for the purpose.
- A construction contractor will remain liable for the payment of RST on materials and equipment used in a construction contract from now until harmonization takes effect on July 1, 2010. On that date, RST will no longer be applied to purchases of material and equipment used in a construction contract.
- Any construction contracts undertaken in Ontario and British Columbia that are started prior to harmonization will have RST embedded in their cost. Where the contract is actually completed on or after July 1, 2010, it will be subject to HST. This has created a situation in which these contracts may, to some extent, be double taxed.
- Ontario and British Columbia have both announced that transitional housing rebates will be available to relieve the purchaser or builder of a portion of the additional costs attributable to the RST embedded in the value of new residential housing or apartments that is also subject to HST once the construction has been completed. Rebates are also available to contractors for the RST paid on inventories of materials on hand at June 30, 2010 for use in the construction of residential real estate, including rental real property.
- Neither province has announced that they intend to implement similar rebates for RST that may be embedded in the value of other real property that will be subject to HST when supplied after June 30, 2010. Customers can be expected to press for credits for contracts that straddle July 1, 2010 where the contract was bid on a PST-included basis.

IMPACT ON THE CONSTRUCTION INDUSTRY



Other considerations

- defer purchases
 - buy later – recover tax as ITC
- ITC typically claimed before tax paid
- accelerate collection of receivables

- Where a registrant is entitled to claim full ITCs on its purchases, and a particular acquisition would be subject to either ORST or BCSST if made prior to July 1, 2010, a deferral of the purchase until after June 30, 2010 may result in a cost savings due to the claiming of an ITC on the HST charged, rather than having to expense any RST that may have applied to the purchase. For example, the purchase of an expensive unlicensed construction or paving equipment currently is subject to RST. After July 1, 2010, fully recoverable HST will apply to the purchase.
- If an expense cannot be deferred, organizations should consider leasing, rather than an outright purchase, with an option to buy after July 1.
- An ITC is available for the GST/HST applicable to a supply at the time the tax becomes payable (i.e., the time an invoice is issued), and will typically be claimed on the return for the month of posting. Currently, businesses are stretching their payables 45, 60 or even 90 days after they become due. Therefore, since an ITC may be claimed almost immediately but the organization generally will not pay the GST/HST to their suppliers until well after it is due, the new HST applicable to purchases will likely have a positive cash flow impact.
- Conversely, any delay in receiving payment for an outstanding invoice issued to a customer may have a negative cash flow impact, since the tax payable on the invoice must be remitted to the Canada Revenue Agency with the GST/HST return for the month in which the invoice was issued. Therefore, it is imperative to stay on top of collections to minimize the impact of having to finance the tax.