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Canadian Indirect Tax News

July 27, 2009 (09-7)

BC harmonized sales tax

Premier Gordon Campbell and Finance Minister Colin Hansen have announced their intention to harmonize the BC social services tax (PST) with the federal goods and services tax (GST). This announcement comes just four months after Ontario announced its intention to harmonize its provincial sales tax with the GST. Both provinces intend to implement their harmonized taxes on July 1, 2010.

- Canada and British Columbia have entered into a Memorandum of Agreement for British Columbia to join a framework agreement for federal collection of a single sales tax.
- Starting July 1, 2010, the British Columbia PST will be converted to a value added tax structure and combined with the federal GST to create the BC harmonized sales tax (BC HST) at a rate of 12%. The provincial portion will be at a rate of 7% and the federal portion at a rate of 5%.
- The BC HST will generally use the same rules and tax base as the federal GST.
- The tax will be administered by the federal government.
- More details on the technical and transitional rules of the new tax will be published in the coming months.

Measures affecting businesses

- The BC HST will generally have a number of long term benefits for businesses including eliminating tax on business inputs and a reduction in compliance costs.
- Businesses selling taxable or zero-rated goods and services will be able to claim input tax credits (ITCs) on their purchases, as under the GST, with limited exceptions.
- Businesses selling tax-exempt goods or services will be unable to claim ITCs as under the federal GST rules. For example, most financial services are GST exempt and therefore ITCs may not be claimed in respect of these services.
- British Columbia's public service bodies (e.g., municipalities, charities and qualifying non-profit organizations) will be able to claim partial rebates for the provincial portion of the BC HST.
- Similar to the restricted ITC system in Quebec, large businesses (those with annual taxable sales in excess of \$10 million) and financial institutions will be unable to claim ITCs on certain items on the provincial portion of the BC HST. However, in British Columbia, these restrictions have been announced as being temporary. After the first five years of BC HST implementation, full ITCs, to the extent relating to taxable supplies, will be phased in over the subsequent three-year period.

- The temporary ITC restrictions for large businesses are:
 - energy, except where purchased by farms or used to produce goods for sale;
 - telecommunication services other than internet access or toll-free numbers;
 - road vehicles weighing less than 3,000 kilograms (and parts and certain services) and fuel to power those vehicles; and
 - food, beverages and entertainment.

Measures affecting individuals

- Goods and services will generally be subject to BC HST in the same manner as they are subject to GST.
- Point of sale rebates will be introduced for the provincial portion of the BC HST for the following items: books, children's clothing and footwear, children's car seats and booster seats, diapers and feminine hygiene products.
- An automatic point of sale rebate will be introduced for the provincial portion of the BC HST for purchases of gasoline, diesel fuel, marine diesel fuel and aviation fuel including any biofuel components, for motor vehicles, boats and aircraft.
- The new BC HST will apply to new home sales. However, purchasers of new homes will be able to claim a rebate equal to 5% of the purchase price up to a maximum of \$20,000. The government's stated intent is that new homes up to \$400,000 will not be subject to any additional tax burden than under the current regime. It is estimated that there is currently PST embedded in the cost of new homes equivalent to a 2% tax rate.
- Used or resale homes will not be subject to the BC HST just as they are not subject to GST.
- A new BC HST credit of \$230 per family member for individuals with income of up to \$20,000 and families with incomes up to \$25,000 will be paid quarterly with the GST and carbon tax credits to help low to middle income individuals and families. The credit will be phased out for incomes above those thresholds.
- The BC HST will apply to short-term accommodation replacing the hotel room tax. As a result, the tax on short-term accommodation should be reduced.

Stay tuned

At this point, we are awaiting further details in several areas, including:

- Transitional rules for implementing the BC HST for real property, tangible personal property and services (e.g., contracts straddling the implementation) have not yet been announced.
- Detailed information is required regarding transitional rules phasing out the current PST (e.g., audits, refunds) and phasing in the BC HST (e.g., registration obligations).
- Information as to whether there will be any new housing rebates with respect to multiple unit residential or senior care buildings as exist under the federal GST.
- Information on whether the provincial tax on liquor will decrease from the current 10% to the 7% provincial portion of the BC HST rate. Ontario has announced the tax on liquor will decrease in that province.
- It appears that financial services will be exempt as with the federal GST treatment. If British Columbia adopts the current HST approach followed in the HST provinces of Newfoundland, New Brunswick and Nova Scotia, the HST rules address inter-provincial activity. For example, under the HST there is a special attribution formula to calculate net tax for financial institutions operating both

inside and outside the harmonized provinces. For those financial institutions operating exclusively within the HST provinces, there are inter-provincial import rules. No such rules have yet been announced for British Columbia.

- Municipalities, which currently receive 100% rebates or ITCs federally, will have to revert to allocating inputs in order to recover the partial rebate for the provincial portion of the BC HST on input costs relating to exempt supplies.
- Certain public service bodies will have different federal GST and provincial component rebates, resulting in effective blended rebate rates for their operations.

Action steps for businesses

- Computer software systems changes will be required to account for charging, collecting, remitting and recovering the BC HST and for aspects of the tax unique to British Columbia (as compared to the federal GST treatment).
- Businesses will be required to consider the impact of these changes on their costing and pricing models.
- The time to consider tax planning opportunities and their impact relating to these new changes is now. Clearly, there are significant elements of the new BC HST still under development. However, the actions that your business takes today can enable you to prepare for, mitigate and possibly improve the impact of sales tax on your business, in areas such as capital acquisitions, lease versus buy considerations, importations, central purchasing and inter-provincial movement of goods.

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