

Presentation to B&CRAO Implications of HST for Industry



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Presenter

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HST Implementation

AGENDA

- Overview of HST
- General Transition Rules
- Implications of HST for Real Estate/ Construction Sector
- HST Rules for Real Property Sector
 - Residential Construction Services
 - Non-residential Construction
- Preparing for Implementation

Ontario Announcements

- Effective July 1, 2010
 - Ontario to join federal HST system (13% HST)
 - Ontario PST eliminated
 - Canada Revenue Agency (“CRA”) will administer
 - One registration number (same as current GST number)
 - One GST/HST return, one audit

HST Overview

- Tax levied under the existing *Excise Tax Act*
- HST operation will broadly mirror that of GST (with certain exceptions)
- HST has broader base than RST – so consumers will pay more tax directly (e.g., on services).
- Businesses also pay more, but can claim ITCs for HST paid on inputs.
- E-filing – July 1, 2010

HST – Implications for Businesses Overview

Supplies to Consumers

PST taxable

Was: 5% + 8%

Now: 13% (no Change)

PST savings to supplier

Supplies to Taxable Businesses

PST taxable

Was: 5% + 8%

Now: 13%, but ITC to buyer (8% saving)

PST savings to supplier

Supplies to Consumers

PST exempt

Was: 5%

Now: 13% (8% increase)

PST savings to supplier

Supplies to Taxable Businesses

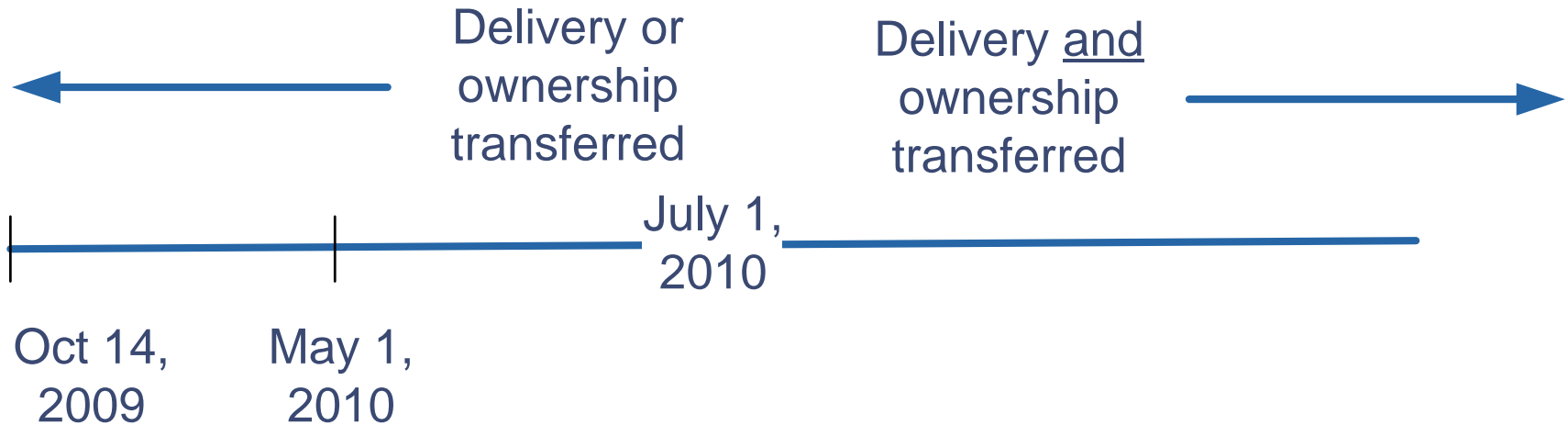
PST exempt

Was: 5%

Now: 13%, but ITC to buyer (no change)

PST savings to supplier

Transitional Rules – Sale of Goods

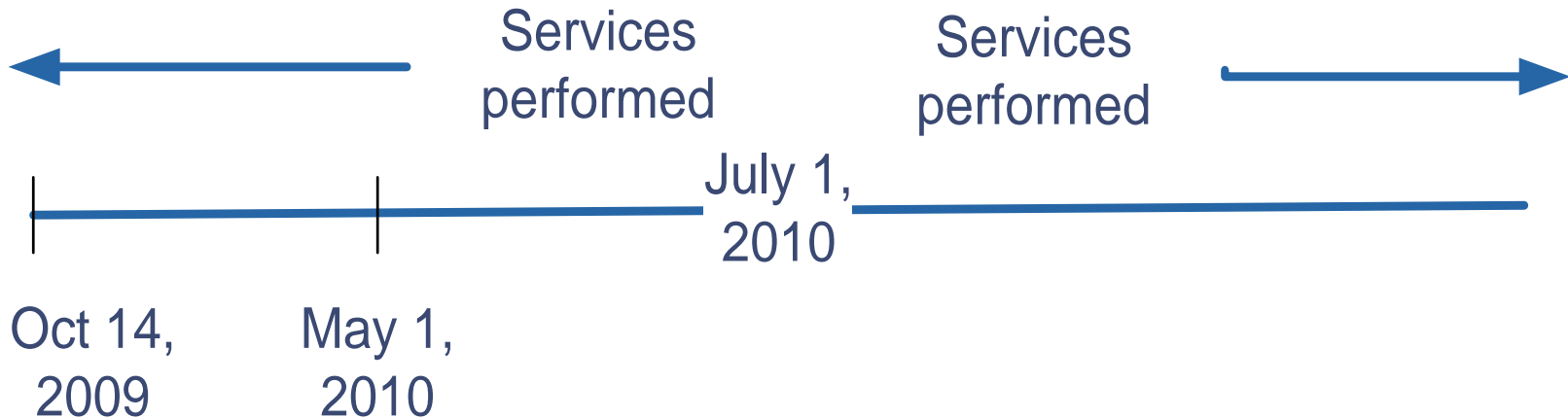


1) **Basic Rule:** focus on delivery and ownership

2) **Prepayments:**

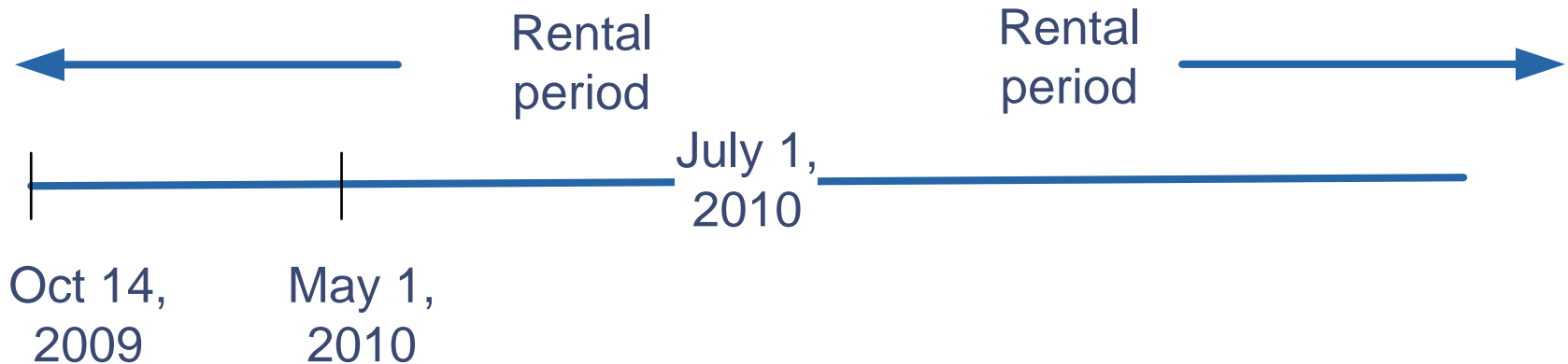
- i. Vendor charges HST (no Ontario RST) on consideration billed or paid on or after May 1, 2010 for goods delivered after June 2010
- ii. Billings October 15, 2009 – April 30, 2010 for goods delivered post June 2010, RST if charged to consumers. No RST for charges to non-consumers. Some businesses may have to self-assess OHST.

Transitional Rules – Most Services



- 1) **Basic Rule:** focus on when services are performed
- 2) **Special Rule:** if $\geq 90\%$ performed before July 2010, no OHST
- 3) **Prepayments:**
 - i. Vendor charges HST (no Ontario RST) on consideration billed or paid on or after May 1, 2010 for services performed after June 2010
 - ii. Billings October 15, 2009 – April 30, 2010 for services post June 2010, RST (if applicable) if charged to consumers. No RST for charges to non-consumers. Some businesses may have to self-assess OHST.

Transitional Rules – Property Rentals



- 1) **Basic Rule:** portion of rental period post June 2010
- 2) **Special Rule:** no OHST if period starts before July 2010 and ends before July 31, 2010
- 3) **Prepayments:**
 - i. Vendor charges HST on consideration due or paid on or after May 1, 2010 for any period or portion thereof after June, 2010
 - ii. After October 14, 2009 and before May 1, 2010: OHST self-assessment if not acquired for exclusive use in commercial activities, or if ITCs restricted

Ontario ITC Recapture

- Major difference from operation of GST.
- Recapture of ITC for Ontario portion of HST (8%) only. Federal (5%) portion unaffected.
- Will apply for first 5 years, then phased out over three years
 - 25% yr 6; 50% yr 7; 75% yr 8
- Applies to
 - Businesses with more than \$10 million in taxable supplies (including zero-rated supplies) AND
 - Financial institutions
- Information released indicates many similarities to Quebec Sales Tax system

* on associated group basis

Page 11

May 19, 2010

Ontario ITC Recapture

Recapture of ITCs applies to following categories:

- Electricity, gas, combustibles and steam (except for use in manufacturing goods for sale and farming)
- Telecommunication Services (excluding internet access or toll-free numbers)
- Road vehicles < 3,000 kg (and related parts and services in particular circumstances)
- Fuel for such road vehicles
- Food, beverages and entertainment

ITC Recapture

- Tax cost and compliance cost for businesses
- Manual exercise vs. segregation on supplier billings
- Segregation on GST/HST returns – separate line
- IT changes necessary to implement
- Training
- Policies and procedures

Note:

- If simply do not report ITC/ RITC, penalties will nevertheless apply for failure to report RITC.
- Can't simply ignore.

Electronic Filing of Returns

New electronic filing requirements

Applies to:

- Reporting periods ending on or after July 1, 2010

Applies to:

- GST/HST registrants with greater than \$1.5 million in annual taxable supplies
- Registrants subject to ITC Recapture Rules
- Builders subject to transitional housing measures announced in BC and Ontario (i.e., rebates, transitional tax adjustments)

The above entities will NOT be permitted to file a paper return

Electronic Filing of Returns

E-filing options

- GST/HST NETFILE
- GST/HST Telefile
- GST HST EDI
- GST/HST internet File Transfer (GIFT)

Restrictions – following entities must use NETFILE

- Large businesses subject to RITC
- Certain builders who sell grandfathered housing
- Entities that are required to account for the transitional tax adjustment in their net tax calculation
- Business that are reporting provincial transitional new housing rebates

Electronic Filing of Returns

Payment options

- Traditional payments will continue to be accepted
- Businesses are encouraged to pay on-line (CRA's "My Payment" Service)
- Telephone banking , internet banking, or automated banking machines

Penalties

- Penalties may apply if a registrant files a paper based return when an electronic return is required

B&CRAO – Categories of Members

B&CRAO Members

1. Manufacturers/ Suppliers
2. Contractors
3. Engineers

B&CRAO – Manufacturers/ Suppliers

1. Manufacturers/ Suppliers

- Registered for GST
- Generally registered for Ontario RST.

Current System

- Charge GST (5%) and Ontario RST (8%) on sales of building materials, equipment (no RST on production equipment).

HST System

- Charge 13% HST for sales in Ontario.

B&CRAO – Contractors

2. Contractors

- Registered for GST
- Generally not registered for Ontario RST.

Current System

- Purchase building materials, equipment - taxable for both GST (5%) and ORST (8%).
- Claim ITC for GST paid on inputs
- ORST on materials becomes cost to contractor.
- Charge GST only on labour/ materials

B&CRAO – Categories of Members

2. Contractors (cont.)

HST System

- Pay 13% HST when purchase building materials, equipment from suppliers.
- Claim ITC for 13% on purchases on inputs (including tools, equipment, repair services, etc.)
- Charge 13% HST on entire charge for labour/ materials
- Where customer is registered for GST/HST – customer claims ITC for HST charged (e.g., non-residential owner)
- Where customer is not registered for GST/HST – e.g., residential landlord/ condo corp., no ITCs.

B&CRAO – Engineers/ Consultants

3. Engineers/ Consultants

- Registered for GST
- Generally not registered for Ontario RST.

Current System

- Charge GST (5%) for services, no Ontario RST
- Claim ITC for GST paid on inputs
- In some cases purchase services of contractors, and recharge to building owner.

B&CRAO – Categories of Members

3. Engineers/ Consultants (cont.)

HST System

- Pay 13% HST on purchases of inputs
- Claim ITC for HST paid on inputs (including software, computers, etc.)
- Charge 13% HST on charge to building owner
- Owner claims ITC for HST charged (non-res. owner)
- Where customer is not registered for GST/HST – e.g., residential landlord/ condo corp., no ITCs.

Manufacturer/Supplier – Charge for Materials to Contractor

	Pre- July 2010' "GST"	Post- June 2010' "HST"
Material Price	100	100
GST	5	-
PST	8	-
HST	-	13
Total Charge to Contractor	113	113
Input Tax credit by Contractor	(5)	(13)
Cost of Materials after ITC	108	100

Contractor – Charge to Building Owner

	GST/PST System		HST System	
	Pre-July 2010		Post-June 2010	
Cost of Materials	\$	113	\$	113
Less ITC		<u>5</u>		<u>13</u>
Net Cost		108		100
Labour		50		50
Profit		<u>42</u>		<u>42</u>
Before Tax Charge		200		192
GST/HST		<u>10</u>		<u>25</u>
Invoice		210		217

Contractor – Charge to Building Owner

Non-Res Building Owner

Cost	210	217
Less: ITC	(10)	(25)
Net Cost	200	192
	(4% decline in cost)	

Res. Building Owner

Cost	210	217
	(3.5% increase in cost)	

*Change in cost depends on proportion of value due to materials

Overview of Impact on Sector

- Where ultimate purchaser (building owner) is GST/HST registered and able to claim ITCs:
 - HST is beneficial -- PST is removed from cost structure.
 - Non-Residential construction industry (and their clients) is major beneficiary of HST.
- Where ultimate purchaser (building owner) is not registered and unable to claim ITCs:
 - HST results in higher costs – PST (narrow base) replaced by broader based HST.
 - Residential construction industry (and clients) will bear more tax (mitigated somewhat by new housing rebate).

Construction Services – Transitional Rules

Construction Services

- Performance of service pre-July 1, 2010 – old rules.
- Performance on or after July 1 – HST applies.
- May have to apportion invoice for services straddling implementation date.
 - GST or HST implications for milestone payments will be based on when the services were performed

Residential Construction Services – Transitional Rules

EXAMPLE

- Renovation begins June 1, 2010, finishes August 15, 2010.
- One invoice – charge (pre-tax) = \$40,000.
- 60% of work (performed pre-July 1, 40% after)
- Apply GST@5% to \$24,000; HST@13% to \$16,000.

Residential Construction Services – Transitional Rules

Deposits

- Deposit versus Prepayment
- No GST/HST on deposits
- GST or HST depending on when deposit is applied

Progress Payments

- GST on progress payment related to pre-July 2010 services.
- HST applies on progress payments in respect of post-June 2010 services (unless billed/ pre-May 2010).
- If pre-billed in period Oct. 15, 2009 – April 30, 2010, for services post June 2010, purchaser is required to self-assess if it is engaged in non-taxable GST/HST activities (e.g., res. landlord).

Residential Construction Services – Transitional Rules

EXAMPLE 2

- Renovation begins June 1, 2010, finishes August 15, 2010.
- Total charge (pre-tax) = \$40,000.
- 60% of work (performed pre-July 1, 40% after)
- On \$40,000 renovation, client pays progress payment of \$10,000 on starting date, \$10,000 on June 30, and final \$20,000 on completion.
- GST applies to first two payments.
- August 15 invoice apportioned: \$4,000 subject to GST, \$16,000 subject to HST.

Residential Construction Services – Transitional Rules

Holdbacks

- A holdback from a progress payment is considered part of the progress payment from which it was held back and would be taxed in the same manner as the progress payment
- Therefore holdbacks relating to progress payment/ invoice for services performed pre-July 1, 2010 (subject to GST) would be subject to GST, even if holdback is payable or paid after June 2010.

Residential Construction Services – Transitional Rules

Rebate for Inventory Held for Residential Renovations/ Repairs

- RST rebates for construction materials held on June 30, 2010 for use in residential renovation/ repair contracts that are subject to the HST.
- This rebate will be filed by the contractor and will be available for construction services in respect of residential housing, condominium and apartment buildings and long-term residential care.
- Note – not available for contractors supplying services to developers of new home construction.

Supply and Install Contracts Straddling July 1, 2010

- “Single supply” of good and service supplied together
- If ownership or possession of good transfers to purchaser before July 1, 2010, then supply of good deemed to be separate supply from services.
- Consequently, GST (and PST) applies to the good if it is installed or ownership is transferred pre-July 2010. Services portion of contract is pro-rated based on proportion performed pre-versus post-July 1, 2010.

Supply and Install Contracts Straddling July 1, 2010

EXAMPLE

- Installation by contractor of elevator

Elevator – cost before tax \$200K

GST \$ 10K

RST \$ 16K

Total \$226K

Less ITC (10K)

Net cost \$216K

Markup 10% 22K

Total cost \$238K

Labour Cost \$100K

Total Charge \$338K

Supply and Install Contracts Straddling July 1, 2010

Scenario a) Install elevator pre- July 1, 2010

50% of labour pre-July 1, 2010, 50% post June 2010.

Taxes

GST on elevator \$11.9

GST on labour \$ 2.5 (pre-July 1)

HST on labour \$ 6.5 (post June 30)

Scenario b) Commence installation of elevator post July 1, 2010

50% of labour pre-July 1, 2010; 50% post June 2010

HST on elevator \$30.9

GST on services \$ 2.5 (pre-July 1)

HST on services \$ 6.5 (post June 30)

Supply and Install Contracts Straddling July 1, 2010

Points to Note

Non-residential Building (certain exceptions – FI's)

- Non-residential building owner is eligible for ITCs – HST is not cost
- RST savings if contractor purchases and receives delivery of elevator on or after July 1, 2010.
- HST would apply to value of installed elevator, but non-residential owner recovers through ITC.

Residential Building

- Residential building owner is ineligible for ITCs – HST is cost.
- Tax savings if contractor installs elevator prior to July 1, 2010.
- Then 8% RST applies only on cost of elevator to contractor, not on marked up value.
- Note if contractor acquires elevator pre-July 1, but not yet installed, can recover RST paid to avoid double tax.

Planning for Harmonization

Analysis of impacts and budgeting:

- Analyze impact - inputs/revenues, cash flow impacts
- Incorporate into Budgeting process
- Review existing contracts:
 - Review contracts –renegotiate with suppliers to pass on RST savings (e.g., on building materials).
 - Review contracts – ensure not precluded from charging HST on contract (i.e., not all-taxes included).
 - Government contracts

Planning for Harmonization

Timing of Purchases

- Purchases currently exempt from RST
 - Little change in tax impact if buyer can claim ITCs.
 - No incentive to defer or accelerate purchases.
- Purchases subject to RST
 - Incentive to defer purchases/ run down inventory until after July 1, 2010.
 - Key issue for contractors engaged in supply and install contracts.
 - Also for capital purchases, (e.g., taxable equipment, tools)
 - Possibly lease to facilitate deferral.

Preparing for Implementation

Systems Impacts

- Sales system
 - Tax and rates
 - Disclosure requirements?
 - Transitional and Place of supply rules
- Purchase system
 - Ensure can capture HST to claim ITCs
 - ITC Recapture Rules

Preparing for Implementation

- E-filing
- Pricing/Customer literature/website information
- Customer communication
- Expense reports
- Taxable benefits
- Contracts with sub-trades
- ITC Documentation requirements
- Damages/termination payments

Preparing for Implementation

RST Issues – They're Not Gone Yet

- RST refunds – get them while you can
- Ontario RST on insurance to continue
 - Cannot claim ITC
- RST Audits and Assessments
 - 4 year window for assessments
 - When will they stop auditing?

Thank you.

