Tax Bulletin
The Wilkinson Tax Group

The New Harmonized Sales Tax

The province of Ontario announced in its March 2009 Budget that it would harmonize the retail sales tax (the Ontario RST) with the federal Goods and Sales Tax (GST). The effective date for implementation of this harmonization is July 1, 2010.

Both the federal and provincial governments passed the enabling legislation on December 15, 2009. While the laws have been enacted, many of the details are just now being released which will impact the actual implementation of these rules.

Overview

In simple terms, the harmonization means that the old RST will disappear as of July 1, 2010 and the HST will commence on that same day. For the sale of many goods, there will be no change to the consumer. If the previous sales tax that applied to the sale of goods was 5% GST and 8 % RST, then the total tax of 13% is replaced by an HST of 13%. The major change will apply to the provision of services and the sale of real estate that did not previously attract the RST. The tax on services and real estate will rise from a GST rate of 5% to a rate of 13%.

While there will be an increase in the total tax to consumers of services and newly constructed homes (net of the applicable rebates), the increased revenue to the province will be offset by a reduction in personal and business taxes. The decrease in the personal tax is created by a reduction in the lowest tax bracket rate. The decrease will come to the business community in two measures. Corporations will face a lower tax rate payable in Ontario and the old RST paid on goods will now be replaced by a refundable HST as an input tax credit.

While the government may advertise the harmonization as “revenue neutral”, the implementation of these measures will not affect all of Ontario residents equally. The rules that will implement these provisions will not be simple. In fact, the old adage “the devil is in the details” will be the applicable rule of the day.

The Ontario RST

Effective July 1, 2010, the old RST will no longer apply to transactions in Ontario (with some exceptions such as a special 8% tax on insurance premiums). The cessation of the RST on transactions on July 1, 2010 will be met with the imposition of the HST on exactly the same day. The province will provide that the old RST vendor’s compensation will terminate for periods ending after March 31, 2010 and be replaced by a one-time Small Business Transition Credit of up to $1,000. Larger businesses that have annual sales in excess of $2,000,000 per annum will not be eligible for the Small Business Transition Credit.

The HST

The HST will be 13% and applied to the supply of goods and services after June 30, 2010. The HST will be levied on any transaction that was previously subject to the 5% GST. Certain items that were exempt from RST such as children's clothing will be eligible for an HST point-of sale rebate for the 8% provincial portion of the HST. The HST will be submitted to the federal government as one tax and the purchaser will be eligible for an input tax credit (ITC) on the full 13% if it was entitled to a full input tax credit before. The provincial portion of the HST (that is the additional 8%) will be accounted for by the federal government and it will pay this tax to the province.

The General Transitional Rules

The RST will terminate and the HST will commence after June 30, 2010. The HST will apply to the sale of goods or the provision of services after June 30, 2010. This is an oversimplification because the rules embody several technicalities which are introduced to ensure that taxpayers cannot manipulate transactions to obtain the best tax result.

There are key dates that affect the transitional rules are as follows:

July 1, 2010

> The provision of goods and services after June 30, 2010 will be assessed HST. The traditional GST and the RST will apply to the provision of goods or services before July 1, 2010 under the old rules.

May 1, 2010

> The payment for goods or services after this date and before July 1, 2010 will attract the HST rather than the GST and RST if the goods or services are provided after June 30, 2010. For payments received after April 2010 that are subject to the HST, the vendor of the supply is responsible to collect the HST, not the old GST and the RST.

October 14, 2009

> Any prepayments made by a purchaser that is not a consumer and that is restricted in some way in claiming normal ITC's will have to self-assess the provincial portion of the HST if the payment or invoice is after October 14, 2009 and on or before April 30, 2010 and the service or good is provided after June 30, 2010.

June 18, 2009

> Any sale of new residential housing that has a written and signed agreement before this date and that would otherwise be subject to HST because the earlier of the possession or ownership of the residence takes place after June 30, 2010 will be grandparented and not subject to HST.

The transitional rules are best analyzed as those pertaining to goods, services, leases and other periodic payment contracts and the sale of new residential housing. The general transitional rules are discussed under the following headings:

Sale of goods:

> The sale of goods will not attract the HST [but will be subject to the GST and the RST if applicable] if the earlier of the possession or ownership takes place before July 1, 2010. This will be regardless of when the consideration becomes due (ie. it is invoiced) or is paid without becoming due.

Provision of services:

> The provision of services will not attract the HST [but will be subject to the GST and the RST if applicable] if all or substantially all (considered to be 90% or more) of the service is provided before July 1, 2010. If less than 90% of the service is provided before July 1, 2010 then the provider will have to allocate the percentage of completion at June 30, 2010 and assess GST on the pre- July 1, 2010 component and assess HST on the post-June 30, 2010. Again, the payment or due date for payment based upon the invoice is not relevant in determining the application of the HST.

Leasing:

> The treatment of leases is determined by the lease interval, not the date that the lease originated. The lease interval can best be described as the monthly or other periodic payment. The lease interval will attract HST if the lease interval commences after June 30, 2010. If the lease interval commences before July 1, 2010 and it ends before July 31, 2010, it will not attract HST.

Self-assessment rule for certain purchasers

Because some “non-consumers” such as exempt suppliers, charities and small business that have elected under the “Quick Method” do not get the full ITC on their inputs, there is a special prepayment rule. If the purchaser pays for, or is invoiced for, goods and services between October 14, 2009 and April 30, 2010, and the goods or services are to be provided after June 30, 2010, then the purchaser must account for and self-assess the provincial portion of the HST. This self-assessment must be completed for the reporting period that includes July 1, 2010 or if the purchaser is not a registrant, then on a special form to be filed before November 2010.

Temporarily Restricted Input Tax Credits

Large businesses with annual taxable supplies over $10 million will face restricted input tax credits for certain costs. These enterprises are businesses (not charities and other public sector bodies) that will be restricted in calculating these ITC’s for 5 years and after that a reduced restriction phased-in over a 3 year period. The restriction will be on the Ontario portion of the HST (the 8%) on purchases of:

- Energy (except where purchased by farms or used to produce goods for sale)
- Telecommunication services (except internet and toll free numbers)
- Road vehicles weighing less than 3,000 kg, and the related fuel (except diesel), parts and service for these vehicles
- Food, beverages and entertainment expenses.

Place of Supply

Three provinces have previously adopted the HST. Sales of goods and services to residents of those provinces have had to have HST charged on the supplies. Now, with Ontario and British Columbia adopting the HST, we will have to be more cognizant of sales outside of the province.

Exports outside of Canada do not attract GST, and will not attract the HST.

Inside Canada, supplies of goods will attract the HST where the goods are delivered to a resident of a province that is a participating province and GST where they are delivered to a resident of a non-participating province. The key will be where legal ownership of the goods transfers. If the legal ownership is transferred in Ontario, another participating province or Quebec, the HST will apply. If the legal ownership is transferred in a non-participating province, then the GST rate will apply.

Administration

All clients will have to make administrative and accounting changes to accommodate the new HST. For example, changes will have to be made to invoicing, rebate calculations, returns and exchanges, the provincial portion of the HST that are restricted to the purchaser etc.

Recently, the federal government has announced that certain entities will have to electronically file their periodic GST/HST returns effective July 1, 2010. Those that will be affected by this rule will be those enterprises that have taxable supplies in excess of $1.5 million in the previous fiscal period, are subject to the Temporarily Restricted input tax credits mentioned above or are new home builders.

If you wish more information on any of these issues, please contact one of our partners or staff whom may assist you.

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