

# TAX BULLETIN

April, 2010

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## Government Announces New GST/HST Self-Assessment and Rebate Rules

On February 25, 2010 the Department of Finance released a Backgrounder entitled *Place of Supply, Self-Assessment and Rebate Rules for the Harmonized Sales Tax (HST)*, which outline substantial changes to the place of supply rules. With the release of these rules and the fact that the HST will now consist of three provincial rates (i.e., 7% in BC, 8% in Ontario, New Brunswick and Newfoundland and Labrador and 10% in Nova Scotia beginning on July 1<sup>st</sup>) changes were necessary to the self-assessment and rebate rules.

This bulletin will outline changes that have been proposed to the self assessment and rebate provisions. As well, it will also summarize the consequential changes that have also been proposed to the imported taxable supply rules. These rules help ensure that the provincial component of the HST applies consistently regardless of whether a supply is made in or outside of Canada.

## Self-Assessment

Self-assessment of the provincial component of the HST may be required in circumstances where a supply of property or a service is made in a non-participating province (i.e. Alberta, Saskatchewan, Manitoba, Quebec, Prince Edward Island and the three territories), but consumption, use or a subsequent supply of that property or service will be in a participating province (i.e. BC, Ontario, New Brunswick, Nova Scotia and Newfoundland and Labrador). Conversely, a rebate of the tax may be available in circumstances where a supply of property or a service is made in a participating province, but consumption, use or a subsequent supply of that property or service will occur in a non-participating province. These rules were already in existence with the introduction of the HST in the Atlantic Provinces in 1997, but needed to be refined to help ensure that the HST legislation functions properly with the varying provincial rates.

However, before we begin discussing these rules in detail, it is worth reviewing the current self-assessment rules. The requirement for profit-oriented entities to self-assess would generally only be triggered when property or services are acquired by an entity that is not entitled to a full Input Tax Credit (ITC) for the property or services acquired. This generally is an issue for entities providing supplies of exempt goods or services. These rules will not change.

- Under the new HST rules for Ontario and BC, ITC's will be restricted during the first 5 years of the new HST system for financial institutions and businesses with taxable sales in excess of \$10 million annually, and after that, full ITCs will be phased-in over 3 years. These restrictions will apply to ITCs related to the following:
  - ◆ Energy (except for energy used for farming or the production of goods for sale);
  - ◆ Telecommunication services other than internet access or toll-free numbers;
  - ◆ Road vehicles weighing less than 3,000 kilograms and related fuel, parts and certain services; and
  - ◆ Food, beverages and entertainment.

When the old and new rules are combined, entities receiving a full ITC on property or services acquired will not have to self-assess HST. In contrast, if the property or services acquired relates to one of the restricted items noted above or if the property or service is used to make an exempt supply, then self-assessment may be required (subject to the rules discussed below).

### Tangible Personal Property

In general, the existing rules for tangible personal property dictate that the value on which tax is required to be self-assessed is the lesser of the consideration paid for the tangible personal property and the fair market value of the tangible personal property.

The expanded self-assessment rule for tangible personal property would also capture situations where tangible personal property is brought into a participating province from another participating province where the provincial component of the HST is lower (e.g., goods that move from BC to Ontario or any participating province to Nova Scotia). If a person is required to self-assess under this proposed rule, the amount of tax owing would be determined by multiplying the difference between the provincial components of the HST (e.g., 1% between BC and Ontario) by the lesser of the consideration paid for the property or the fair market value of the property at the time of bringing it into the province.

*Example 1: An unincorporated business owner engaged exclusively in GST/HST-exempt activities in Ontario (e.g., a day care) purchases a new computer for \$600 while vacationing in Alberta. The business owner would be required to pay the 5% GST at the time of purchase (\$30) and self-assess the Ontario HST ( $\$600 \times .08\% = \$48$ ) upon bringing the computer into Ontario. An input credit for both the original GST and the self-assessed Ontario HST would not be available. Generally, the existing exemptions from the requirement to self-assess would continue to apply under the proposed rules – for example, self-assessment is not required when the person is entitled to claim full ITCs as discussed above. However, this exemption does not apply if the person uses a streamlined method such as the Quick Method to report net tax under the GST/HST. In addition, under the new rules, it is proposed that a person be relieved from the requirement to self-assess if the amount of tax that is payable by the*

person under these rules in a calendar month is less than \$25.

### Services and Intangible Personal Property

Under existing rules, self-assessment is required on services and intangible personal property if a person resident in a participating province acquires intangible personal property or a service in a non-participating province for consumption, use or supply primarily in the participating provinces. In these situations, the person is generally required to self-assess the provincial component of the HST (as HST would have already been paid).

The self-assessment rules have been expanded for services and intangible personal property, and will now apply when intangible personal property or a service is acquired in a province for consumption, use or supply "significantly" (generally, 10% or more) in participating provinces for which the provincial component of the HST is higher than the provincial component of the HST in the province of acquisition. For the purpose of this determination, the provincial component of the HST for a non-participating province will be regarded as being 0%.

*Example 2: A business that resides in BC operates retail outlets both in BC and Ontario. The retail outlets make both exempt and taxable supplies. The business acquires the services of an accounting firm located in BC for a yearly fee of \$6,500 (these services were not acquired for substantial use in commercial activities). The accounting firm has determined that the place of supply of the service is BC. However, when the work performed is reviewed, it is determined that 60% of the service relates to the business' retail outlets in Ontario and the remainder of the service relates to the person's retail outlets in BC. In this situation, the business would be required to self-assess tax in the amount of \$39 (i.e.,  $(8\% - 7\%) \times \$6,500 \times 60\%$ ) for the service.*

It is important to note that if a person is required to self-assess under this proposed rule, an amount would be determined in respect of each particular participating province in which the intangible personal property or service will be consumed, used or supplied for which the provincial component of the HST is higher than the provincial component of the HST for the participating province in which the

intangible personal property or service was acquired.

The exemption for under \$25 per calendar month previously discussed also applies to supplies of services and intangible personal property.

### Imported Taxable Supplies

An "imported taxable supply" is generally a supply that enters Canada without having to be reported to the Canada Border Services Agency (e.g., a service or intangible personal property).

Under the current rules, a person (excluding financial institutions) is generally required to self-assess the GST on taxable supplies of services and intangible property that are imported into Canada that are not for use all or substantially (90% or more) in commercial activities.

The imported taxable supply rules will be expanded to require self-assessment when intangible personal property or a service is acquired outside Canada for consumption, use or supply "significantly" (generally, 10% or more) in participating provinces.

If a person is required to self-assess under the proposed rule, an amount of tax would be calculated with regard to the extent to which the intangible personal property or the service will be consumed, used or supplied in each participating province.

The Department of Finance has stated that the proposed changes to the self-assessment and imported taxable supply rules described above would apply to:

- any tangible personal property brought into a participating province on or after July 1, 2010; and
- any supply of intangible personal property or a service if all or part of the consideration for the supply becomes due or is paid on or after July 1, 2010.

### Rebates on the Provincial Component of the HST

Special rebate mechanisms are currently in place, that, apply where property or services are acquired in participating provinces, and the property is removed, or the services are for use, outside these provinces by certain persons that are not able to

claim full ITCs. This may include certain public sector bodies such as charities and non-profit organizations, and businesses involved in making exempt supplies such as day care services, certain exempt health services and residential rent. These rebate mechanisms are expanded to apply to situations where tax is paid on property or a service in one province and is moved or used in a province with a lower provincial component.

### Tangible Personal Property

Under the current rebate provisions, to qualify for the rebate, the tangible personal property that was acquired must be for consumption, use or supply exclusively (90% or more) outside the participating provinces. In addition, the following conditions must be met:

- The tangible personal property must also be removed from the participating province to a non-participating province within 30 days after the tangible personal property is delivered to the person,
- The person must provide proof that applicable provincial retail sales tax, in the province to which the tangible personal property were taken, has been paid (e.g., if property is moved from Ontario to Manitoba proof of payment of the PST in Manitoba would be required), and
- The application must be filed within one year from when the property is removed from the participating province.

Expanded rebate provisions will now apply to tangible personal property that is moved from any participating province to BC and from Nova Scotia to any of the other participating provinces.

*Example 3: A non-GST/HST registrant dentist in Vancouver, BC purchases supplies from a manufacturer in Markham, Ontario, for use in the dentist's practice in Vancouver. While in Ontario attending a conference, the dentist picks up the supplies and returns with them to Vancouver. Since the dentist is not entitled to ITCs, the dentist may be eligible to claim a rebate of the difference between the provincial component of the HST paid for the supplies (the 8% Ontario component of the HST) and the provincial component of HST that would have been payable had the supply been made*

*in the destination province (the 7% BC component of the HST).*

It is proposed that to qualify for a rebate in respect of a movement of tangible personal property, the amount of the rebate would have to be at least \$5. In addition, the total amount of tax for which a single application for rebates in respect of the movement of property between provinces is made must be \$25 or more.

### Services and Intangible Personal Property

An expanded rebate rule for services and intangible personal property will provide for the recovery of all or a portion of the provincial component of the HST paid in respect of a supply made in a participating province where the intangible personal property or service was acquired for consumption, use or supply "significantly" (generally, 10% or more) in provinces for which the provincial component of the HST is lower than the provincial component of the HST for the province in which the intangible personal property or service was acquired.

The proposed changes to the rebate provisions described above would apply to:

- any tangible personal property removed from a participating province on or after July 1, 2010; and
- any supply of intangible personal property or a service if all or part of the consideration for the supply becomes due or is paid on or after July 1, 2010.

*Example 4: A non-GST/HST registrant association with offices in Ontario engages a professional hockey player to speak to minor hockey players and their parents in Toronto, Calgary and Vancouver. The hockey player is a registrant and determines that the place of supply of the supply of the service is Ontario and charges HST at a rate of 13% for his service. The service is in fact supplied and consumed equally in Ontario, BC and Alberta.*

The association may apply for a rebate of 1/3 of the provincial component of the HST paid (8%) for the service provided in Alberta (as it is a non-participating province). Also, for the 1/3 of the service provided in BC, the business can claim a rebate equal to the difference (1%) between the provincial component of the HST paid in Ontario on

that part of the service and the tax that would have been payable in BC had the supply been made in BC.

## Summary

The changes proposed to the self-assessment and rebate provisions help ensure that the HST rules function properly on interprovincial transactions. As well, the consequential changes that have been proposed to the imported taxable supply rules help ensure that the provincial component of the HST applies consistently regardless of whether a supply is made in or outside of Canada. However, the calculations required will be complex for some business, such as those that provide exempt goods or services in different provinces. Contact your BDO advisor to determine how these new rules will impact your business.

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The information in this publication is current as of April 30, 2010.

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