

FOOD AND BEVERAGE

GST/HST TIPS AND TRAPS FOR FOOD & BEVERAGE PROCESSORS



One area often overlooked by food and beverage processors is the handling of the GST/HST.

In our recent [Food & Beverage Report](#), we found that industry consolidation, vigorous competition and a scarcity of experienced and qualified talent are creating a perfect storm of challenges that has food and beverage processors looking beyond their existing markets for future success. As these businesses seek to diversify and transform to remain competitive, there are some key areas they need to be concerned about when it comes to managing their GST and/or HST.

Sale or purchase of a business

Food and beverage processors may sell or purchase a business without paying special attention to the GST/HST implications. On the sale of a business, the seller generally is required to collect GST or HST on the assets (equipment, inventory, intangible property) even though the purchaser may be entitled to full input tax credits ("ITCs"). The cash flow implications can be great where the sale of the business is for a substantial amount.

Where the sale of a business includes real property, the seller is not required to collect tax on the value of the real property where the purchaser is registered for GST as it is the purchaser who is required to self-assess the GST or HST on the value of the property. Where the purchaser is engaged in commercial activities, the purchaser is entitled to a corresponding ITC.

For assets other than real property, subsections 167(1) and (1.1) of the *Excise Tax Act* ("ETA") provides relief by eliminating the obligation to pay tax on the sale of a business.

In order for the seller and purchaser of a business or part of a business to elect to not have tax apply to the sale of a business, several conditions must be met. These conditions are summarized as follows:

- A seller makes a supply of a business or part of a business;
- The business or part of the business was carried on by the seller or was established by the seller (several other relationships but these are the main two);
- The purchaser is acquiring ownership, possession or use of all or substantially all (generally considered to be 90%) of the property that can reasonably be regarded as necessary for the purchaser to be capable of carrying on the business or part of a business as a business; and
- The purchaser is a GST registrant where the seller is registered for GST.

ABOUT US

BDO recognizes that it is critical to both build and protect your brand, as well as to take advantage of recent developments in innovation and technology. Our professionals understand the varying priorities and concerns for food and beverage organizations in Canada. As a leader in serving the food and consumer products subsector, we help clients grow their revenue in new markets, build their brands, and control costs to maximize profitability.

For more information, please [contact your local BDO advisor](#) or a member of our Food and Beverage Team below:

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Provided these conditions are met, the seller and the purchaser can jointly elect (using form GST 44 - Election Concerning the Acquisition of a Business or Part of a Business) to have no tax apply to the sale of the business.

The election must be filed by the purchaser in the period in which the GST or HST would have been payable, if the election was not in place. Food and beverage processors must determine whether they are purchasing a business or part of a business or whether they are just purchasing a few assets in which tax would be payable.

Recapture of input tax credits

Effective July 1, 2010, large businesses in Ontario are required to repay or recapture the provincial component of the HST on specified property and services. "Large businesses" are businesses with taxable supplies made in Canada in excess of \$10 million (including associated registrants) annually. This requirement has been in effect for 8 years and began to be phased out on July 1, 2015 by allowing registrants to reduce the required recapture by 25%.

Some large food and beverage processors fail to meet this recapture requirement as they forget to include all associated registrants when calculating the \$10 million threshold. Where a corporation determines that they meet the large business threshold in a particular fiscal year, the large business is required to begin recapturing in the following recapture period (July 1 of following year until June 30 of the next year).

The specified property and services include:

- Qualifying motor vehicles (passenger vehicle and small trucks) and fuel for these vehicles;
- Specified energy (electricity gas and steam);
- Specified telecommunications (excluding internet); and
- Specified meals and entertainment currently subject to a 50% restriction of input tax credits.

Where energy is purchased for use in production and manufacturing of tangible personal property for sale, the requirement may not apply where the energy can be shown to be used in production.

Generally the usage of energy can be supported in one of two ways. Registrants can conduct an engineering study or they can file a production proxy with the Canada Revenue Agency ("CRA"). The production proxy for food and beverage processors is 13% (proxy percentage available for food manufacturing), which means a food and beverage processor would only be required to recapture 13% of the provincial component of the HST, instead of the full 8%, where the proxy has been filed with the CRA.

An issue arises where a food and beverage processor acts as though the proxy is in place but has failed to file the proxy with the CRA. If discovered upon audit, the auditor may assess a food and beverage processor for the amount that was not recaptured, due to the proxy.

Closely related elections

There have been changes to the requirements for closely related elections which may affect food and beverage processors. Where a processor has an arrangement, whereby the real property and building is in a holding corporation ("Holdco") and the Holdco leases the real property and building to an operating company which is closely related, HST must be collected on the lease payment, unless an election has been filed with the CRA. This would also apply where a management fee is paid between a parent corporation and its wholly-owned subsidiary.

For elections in place prior to 2015, electing entities must have the previous election (Form GST 25) on file with the electing entities, books and records and must have filed the new election (RC4616) with the CRA prior to December 31, 2015. For new elections entered into after January 1, 2015, the electing entities must complete form RC4616 and file it with the CRA prior to the due date of the GST return covering the period in which the election was made.

If discovered upon audit, food and beverage processors may be assessed for the tax which was not collected where the elections were not filed with the CRA. Although the assessed corporation can collect the assessed tax from the other corporation, penalties and interest may apply.

Amalgamations

When an amalgamation occurs between two food and beverage processors, the new processor is generally deemed to be the same person as the preceding corporations for purposes of the GST/HST. Provided certain conditions are met (two or more corporations are merged or amalgamated), the new corporation is entitled to input tax credits that the predecessors were entitled to.

Therefore, if it was determined that input tax credits were not recovered in a predecessor corporation (prior to amalgamation), the new amalgamated corporation could recover the missed input tax credits provided the period in which input tax credits are allowed (generally 4 years from invoice date) has not expired.

Proper handling of GST and HST up front can minimize risks of future repayment and flow directly to the bottom line for Food and Beverage processors looking to maximize profits and cash flow to sustain their next phase of growth.

About BDO

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