

**Strafford**

*presents*

# **Canadian Sales Tax Compliance Challenges for U.S. Companies**

## **Mastering New Provincial Harmonized Sales Taxes, Nexus Standards, and Other Critical Topics**

### **A Live 110-Minute Teleconference/Webinar with Interactive Q&A**

**Today's panel features:**

Alan Kenigsberg, Partner, **Stikeman Elliott**, Toronto, ON Canada  
Kal Ruprai, Partner, Indirect Taxes, **Meyers Norris Penny**, Toronto, ON Canada  
Rod Butcher, Director, Tax Advisory Services, **Ryan**, Mississauga, ON Canada

**Wednesday, March 31, 2010**

The conference begins at:

**1 pm Eastern**

**12 pm Central**

**11 am Mountain**

**10 am Pacific**

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**Canadian Sales Tax Compliance  
Challenges for U.S. Companies  
Webinar**

**March 31, 2010**

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# Today's Program

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*(Kal Ruprai, Rod Butcher and Alan Kenigsberg)*

Current Sales Tax Audit Issues In Canada      Slides 53-55

*(Kal Ruprai, Rod Butcher and Alan Kenigsberg)*

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# **Ontario And British Columbia HSTs, In Detail**

**Kal Ruprai, Meyers Norris Penny**

**Rod Butcher, Ryan**

**Alan Kenigsberg, Stikeman Elliott**

# Introduction



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- Effective July 1, 2010, Ontario and BC PSTs are no longer applicable
- Ontario and BC will “harmonize” their sales taxes with the GST
- The HST will be administered by the federal government and will follow the GST rules



# Introduction (Cont.)



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- GST at 5% applies in all Canadian provinces and the territories
- HST at 13% applies in most of the provinces on the East Coast
- PST applies in five provinces
- Quebec sales tax (QST)



# Introduction (Cont.)



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- PSTs inefficient, increase costs
- Different application of PST in each PST province
- Going forward for HST provinces: One return, one legislation, one administration
- Many winners with HST, but some losers as well



# Transitional Rules



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- Apply to transactions that straddle the implementation date
- Released on Oct. 14, 2009
- May 1, 2010 where amounts are prepaid
- July, 1, 2010 is the “big day” (implementation)
- Nov. 1, 2010 is the final date where remittances must be made, but due with July return



# Transitional Rules (Cont.)

## Goods

- If consideration is due or is paid before becoming due after June 30, HST
- Consideration after April 2010 and before July, ownership and delivery after June 30, HST to be charged by seller
- Consideration after Oct. 14, 2009 but before May 2010, seller charges 5% GST; but, certain purchasers must self-assess the provincial component of the HST



# Transitional Rules (Cont.)

- The following are required to self-assess for prepayments
  - Non-consumers acquiring for use or supply in activities that are not exclusively commercial activities
  - Items that are exclusively for commercial activities, but the item is subject to recapture (electricity)
  - Non-consumers using a simplified GST method
  - Selected listed financial institutions, which use the special attribution method



# Transitional Rules (Cont.)

## Goods - Example

- Sale of furniture (i.e. payment made) on Oct. 20, 2010 – delivered to customer on July 20, 2010
- What rate of tax is charged?
- Vendor is not required to charge HST, as delivery and possession occur after July 1, 2010 and invoice date is prior to May 1, 2010



# Transitional Rules (Cont.)

- Subscriptions to newspapers and periodicals, prepaid funeral services – GST only if paid prior to July 1
- Services – HST on proportion of services to be performed after June 30
- Leases and licenses – Rent, royalties or similar
  - IPP where payment varies with use, commercial RP
  - Where lease interval begins before July and ends prior to July 31, GST applies
  - HST on the part of the lease interval after June 30



# Transitional Rules (Cont.)

- IPP – Intellectual property or contractual rights; includes memberships and admissions
  - General rule is that HST applies if consideration is due or is paid before due date after June 30
  - Memberships – See services rules
  - Lifetime memberships – Special rule involving 25%
  - Admissions deemed to be a service – See service rules



# Transitional Rules (Cont.)



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- Supply and install
  - If goods to be supplied and installed, and delivery of the goods made prior to July 1 but installation after, PST and GST on the goods and HST on the installation service



# Transitional Rules (Cont.)

- Returns and exchanges
  - If full refund, RST is refunded
  - If no \$ returned or charged, no RST or HST consequences
  - If exchange and partial refund, no HST on replacement; RST refund on amount of refund paid
  - If exchange and additional payment, no RST but HST on additional



# Transitional Rules (Cont.)

- Returns and exchanges
  - If RST did not apply on original, and then exchange takes place, provincial component of HST applies to the replacement
  - If property returned after Oct. 31, no point of sale adjustment but RST refund application



# POS Rebates



## POS rebates common to BC and ON

- Printed books
- Children's clothing
- Children's footwear
- Diapers
- Children's car seats and car booster seats
- Feminine hygiene products

# POS Rebates (Cont.)



POS rebates unique to ON

- Newspapers
- Prepared food and beverages with an individual sales price of not more than \$4

# POS Rebates (Cont.)



## POS rebates unique to BC

- Motor fuels
- Residential energy credit (provincially administered)

# ITC Restrictions



## Overview

- Temporary ITC restrictions for provincial component
- Large businesses - \$10M in taxable supplies, including affiliates
- Restrictions similar to those in Quebec
- “Recapture”-restricted ITCs
- Simplified reporting method election

# ITC Restrictions (Cont.)



## Telecommunications services

- Internet access and Web site hosting
- 1-8XX and other toll-free services
- Telecommunications equipment
- Equipment repairs and maintenance
- Non-telecommunication services
- Proxy rates

# ITC Restrictions (Cont.)



## Restricted meals and entertainment

- Expenses subject to the 50% income tax limitation
- Exceptions to the 50% income tax limitation

# ITC Restrictions (Cont.)



## Energy – Electricity, gas, steam or other fuel

- Restriction does not apply to manufacturing goods for sale
- Apportionment is possible
  - Energy study
  - Elect for proxy rates

# ITC Restrictions (Cont.)



## Energy

- Natural gas
  - “Buy-sell” agreement
  - Sales contract
- Electricity
  - Lease of commercial office space

# ITC Restrictions (Cont.)



## Licensed road vehicles

- Road vehicles < 3,000 kg licensed for use on public highway
- Repairs and maintenance
- Fuel acquired in Ontario

# Electronic Filing



## Electronic filing requirements

- Effective July 1, 2010 for those with:
  - Annual taxable supplies > \$1.5 million
  - Subject to temporary ITC restrictions
  - Subject to transitional housing rules
- Four methods available
- New information fields for NETFILE

## Background

- “Financial services” as defined in s.123 of the ETA are generally exempt from GST
- The CRA lost a number of recent cases on financial services (e.g. *Canadian Medical Protective Association* and *Costco*)
- Dec. 14, 2009 backgrounder stated changes would be made to the definition of “financial services” to “clarify” the CRA’s position and essentially reverse the *CMPA* and *Costco* cases.

### CRA notice 250 issued in February 2010

- Went beyond “clarifying”
- Reversed a number of CRA published positions
- No examples were provided of what will still be considered a financial service
- Has created much uncertainty in the financial sector

## CRA notice 250 (Cont.)

- Examples of activities where the CRA has reversed longstanding positions to say that the services are now taxable include:
  - Trailer fees or commissions
  - Automobile dealership finance departments arranging for the issuance of loans
  - Business broker services
  - Certain services of distributing and helping complete credit card applications

## Budget - March 4, 2010

- Proposed new, extremely broad exclusions from the definition of "financial services"
- Effective as of Dec. 14, 2009
- May extend back even further (up to Dec. 17, 1990) if:
  - Any service under the agreement was ever treated as taxable, or
  - A supplier previously collected GST and stopped remitting GST at some point (such as after *CMPA*)
- CRA can go back beyond the usual four-year limitation period for a one-year period after legislation receives royal assent

## HST

- As of July 1, 2010 in BC and Ontario (already exists in Nova Scotia, Newfoundland and New Brunswick)
- Currently, HST has payment-and-refund mechanism to account for out-of-province purchasers and where services are provided
- New approach for mutual funds and others in the financial sector is in the works – may need to calculate amount of HST payable based on residence of beneficial owners

## Industry concerns in funds sector

- Requirement to treat all unit holders equally
- Impractical to implement the HST changes, especially before July 1
- Additional complexities for multi-tiered ownership structures (e.g. funds-of-funds)
- Reluctance by dealers to provide residency data could deter sales

## Introduction

- > Why have place of supply rules?
  
- > HST participating provinces, as of July 1, 2010
  - Newfoundland, New Brunswick, Nova Scotia, Ontario, PEI (13% HST)
  - British Columbia (12% HST)
  
- > The place of supply rules are changing

### Real property/tangible personal property

- > Real property supplied in province in which it is situated
  
- > Tangible personal property supplied in province where it is:
  - Delivered or made available
  - Received, if shipped
  - Ordinarily located, if possession is given for more than three months (e.g. lease of equipment)
  
- > No change to these rules

## Services: Current rules

- 1) Is 90% or more of the service performed in one province?
  - If yes, that province is place of supply
  - If no, then go to 2
- 2) Is the province where the supply was negotiated known, and is at least 10% of the service provided there?
  - If yes, that province is place of supply
  - If no, then go to 3
- 3) If service is performed primarily in participating provinces, participating province where greatest part of service provided is place of supply

## Services: Proposed general rules

- 1) Has supplier obtained recipient's address?
  - If yes, address generally determines place of supply
  - If no, then move to question 2
- 2) Was service performed primarily in participating provinces?
  - If yes, then move to question 3
  - If no, then HST does not apply
- 3) Was greatest part of service performed in a single participating province?
  - If yes, then that participating province is the place of supply
  - If no, then move to question 4
- 4) Place of supply is participating province with highest rate of HST

## Services: Services in relation to real property

- > Rules based on location of property
- > HST applies if property is located primarily in participating provinces
- > If HST applies, place of supply is:
  - 1) Participating province where greatest part of property located
  - 2) If (1) cannot be determined because property is equally located in two or more provinces, participating province with highest rate of HST

### Services: Services in relation to tangible personal property (TPP)

- > HST applies if TPP is located primarily in participating provinces while service performed. If not primarily in participating provinces, no HST
- > If TPP remained in the same participating province(s) while service performed:
  - First look to where greatest portion of property is situated; if this cannot be determined, then use highest provincial HST rate
- > If TPP moved between provinces while service performed:
  - First look to location where greatest portion of service performed; if this cannot be determined, then use highest provincial HST rate

### Services: Computer-related services and Internet access

- > Current rule based on where end-user is ordinarily located when using the service
- > If the location of end-users is not known, place of supply is mailing address of recipient (e.g. reseller)
- > No changes to this rule

**Intangible personal property that can be used only primarily outside participating provinces**

> Not subject to HST

### **Intangible personal property that can be used only primarily in participating provinces**

- > If rights can be used only in one province, that is place of supply
- > If rights can be used in multiple provinces, place of supply is province where greatest proportion of use of rights would occur if all rights were exercised
  - (Note special rules in this case for certain property <\$300)
- > If above rules insufficient, place of supply is address of recipient (if supplier has obtained one)
- > Otherwise, highest applicable provincial HST rate applies

## Other Intangible Personal Property

- > Includes all intangible personal property that is not primarily limited to either participating or non-participating provinces
  1. Special rules for certain local purchases under \$300
  2. If (1) does not apply, the place of supply is generally the address of recipient, if supplier has obtained one
  3. If no address is obtained, highest applicable HST rate applies

### **Intangible personal property that relates to real property**

- > Same as rules for services in relation to real property
- > Rules based on location of property
- > HST applies if property is located primarily in participating provinces
- > If HST applies, place of supply is:
  - 1) Participating province where greatest part of property located
  - 2) If (1) not known because property equally located in two or more provinces, participating province with highest rate of HST

## Place Of Supply Rules (Cont.)

### Intangible personal property that relates to tangible personal property

- > Rules based on where TPP is *ordinarily* located
- > HST applies if property is ordinarily located primarily in participating provinces
- > If HST applies, place of supply is:
  - 1) Participating province where greatest part of property is ordinarily located
  - 2) If (1) not known because property equally located in two or more provinces, participating province with highest rate of HST

### **Intangible personal property that relates to services to be performed**

- > If supplier can determine that services would all be performed in a single province, place of supply is that province
- > Otherwise, general rules for intangible personal property apply

## Special rules

- > Personal services
- > Services rendered in connection with litigation
- > Passenger transportation services
- > Services supplied on board conveyances
- > Baggage charges and child supervision
- > Services related to a ticket, voucher or reservation
- > Freight transportation services
- > Postage and mail delivery services
- > Others ...

## Self-assessment of provincial portion of HST

- > Required where supply is made in a non-participating province, but consumption is in a participating province and not acquired for use exclusively in commercial activities
- > Tangible personal property
  - Self-assessment required when not acquired for use exclusively in commercial activities and importing into a participating province from either:
    - 1) A non-participating province, or
    - 2) A participating province with a lower sales tax rate

## Self-assessment of provincial portion of HST (Cont.)

- > Services or intangible personal property
  - Self-assessment required by residents of participating province who purchase services or intangible personal property not for use exclusively in commercial activities in either:
    - 1) A non-participating province, or
    - 2) A participating province with a lower sales tax rate
  - Amount based on extent to which use is made in participating provinces

### Self-assessment of provincial portion of HST (Cont.)

- > Imported taxable supplies
  - Residents of Canada required to self-assess on supplies made outside Canada for use in Canada, if not for use exclusively in commercial activities
  - Provincial component required on portion used in participating province if “significant” (>10%) use will be in participating province
- > Rule applies to:
  - TPP brought into a participating province after July 1, 2010
  - Supply of intangible personal property or service if consideration is paid or becomes due after July 1, 2010

## Rebates

### > Rebates available for:

- TPP taxed in participating province but moved to province with lower HST rate or no HST
- Services and intangible personal property supplied in a participating province for use elsewhere
  - Amount prorated for proportion of use in provinces with lower HST rate or no HST
- Imports of non-commercial goods, by residents of higher-rate province, into lower-rate province, for use exclusively in lower-rate province

## Rebates (Cont.)

- > Changes to rebate provisions would apply to:
  - TPP removed from participating province on or after July 1, 2010
  - Supply of intangible personal property if consideration payable or due on or after July 1, 2010
  - Any importation on or after July 1, 2010

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# **Current Sales Tax Audit Issues In Canada**

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# Provincial Audits

- Increasingly aggressive positions by provincial revenue agencies
  - Example: BC exemption on administrative materials mailed individually to recipients in BC
  - Example: Ontario and BC becoming more aggressive on RST assessments, since with Retail Sales Act disappearing, they are less concerned with adverse precedents
    - One Ontario audit involves client doing all accounting functions in U.S., with all sales records electronic
  - Example: Ontario auditing clients within four years, as Ministry tries to audit as many companies as possible right now
- Documentation trends
  - Example: Recent Quebec MRQ audit action on input tax refunds on auto manufacturers' incentive or rewards payments to dealers or captive finance companies
- Specific issues

# Federal GST/HST Audits

- Increasingly aggressive audit positions
  - Rumors of new attempt to extract GST/HST on a deemed re-supply to pension plans by those employers with defined benefit plans that pay suppliers, such as actuaries and investment counsel, from pension plan funds.
  - CRA harsh interpretation of the “in force” provisions of the proposed rules to make investment management fees taxable and counter the effect of the *CMPA* case.
- Documentation trends
- Specific issues