

The GST Drop From 6% to 5%

After the Economic Statement of October 30, 2007, reduction of the GST rate by one percentage point was implemented effective January 1, 2008 from 6% to 5%. On July 1, 2006 we saw a drop in the rate from 7% to 6%. The Canada Revenue Agency has indicated that the approach used in implementing the previous rate reduction will be followed again this time around for the purposes of simplicity and consistency.

Transitional Issues

One of the biggest considerations will be how to deal with supplies being made that straddle the implementation date of January 1. The transitional rules will not always lead to the 5% rate applying when consumption of the supply is made after January 1. In some instances, the 6% rate will still apply, depending on when the arrangements for the supply were negotiated and/or paid for.

Services and Tangible Personal Property

The general transitional rule is based on the time at which the GST becomes payable:

- If GST becomes payable, or is paid without having become payable, before January 1, 2008, then the old 6% rate will apply.
- If GST becomes payable on or after January 1, 2008, without having been paid before that date, then the 5% rate will apply.
- If GST is paid on or after January 1, 2008, without having become payable before that day, then the 5% rate will apply.

Existing GST provisions dictate that GST becomes payable on the earlier of the date an invoice is issued, or the date of that invoice, or if no invoice is issued, then on the date payment is called for in a written contract.

Real Property

There are two factors that dictate which rate will apply to the sale of real property (land and buildings, including commercial space and new homes). The first factor is the



Examples of Application of the General Transitional Rules

- If you buy a new appliance and are invoiced for it on December 31, but don't take delivery of the appliance until January 1, the rate of GST would be 6%.
- If a national member organization invoices its members for the 2007/08 membership fee that covers the period from July 1, 2007 to June 30, 2008 and the invoice is issued prior to January 1, 2008, then the rate of tax is 6%.
- A landlord invoices a tenant for property tax escalations for the calendar year 2007. The invoice is issued January 1, 2008 and the due date is January 31, 2008, then the rate of tax is 5% notwithstanding the fact that the charges relate to a point in time prior to January 1, 2008.
- If you buy an airline ticket or concert ticket before January 1 for travel or a concert after December 31, the 6% rate will still apply.
- For accounting or legal services provided before January 1, but not invoiced until after December 31st, the entire bill will be subject to GST at the reduced rate of 5%.

date that the agreement of purchase and sale was entered into. The second factor is the date on which ownership or possession of the property is transferred.

Ownership or Possession transferred before January 1, 2008 = 6%

Ownership and Possession transferred on or after January 1, 2008 and agreement entered into after October 30, 2007 = 5%

Ownership and Possession transferred on or after January 1, 2008 and agreement entered into after May 2, 2006 and on or before October 30, 2007 = 6% for residential properties and = 5% for commercial properties.

New Housing Transitional Rebate

For new houses, condos and other new residential units where ownership and possession transfers on or after January 1, 2008 and the agreement was entered into on or before October 30, 2007, the 6% rate will apply, but the purchaser will be entitled to file a claim with CRA to be paid a Transitional Adjustment that effectively reduces the rate from 6% to 5%, taking into account the GST new-housing rebate that would already have been paid.

This rate reduction rebate is not available with respect to commercial space. The Transitional Rebate cannot be assigned to the builder.

Other Factors to Consider Resulting from Rate Reduction

GST New Housing Rebates

Purchasers of new homes are currently entitled to a rebate equal to the lesser of 36% of the GST paid and \$7,560. The rebate begins to be reduced when the price of the purchased home exceeds \$350,000 and is eliminated for homes costing \$450,000 or more. With the GST rate reduction from 6% to 5%, the rebate percentage of 36% and the value thresholds of \$350,000 and \$450,000 remain unchanged but the maximum rebate available drops, from \$7,560 to \$6,300.

GST to remit on Auto Benefits

Employers who provide a company vehicle to an employee are required to calculate a taxable benefit with respect to the personal use of that vehicle. The benefit amount includes a GST component. For 2007, the employer was required to remit GST at the rate of 5/105 of the standby charge portion of the benefit and at the rate of 4% of the operating cost benefit. These remittance rates will be reduced to 4/104 and 3% respectively for 2008 and subsequent years.

Public Service Body Rebate Percentages

The rebate percentages used by charities, NPO's, Municipalities, School Boards, Universities, and Hospitals will not change. For example, the rebate for charities remains at 50% of the amount of GST paid.

Quick Method Remittance Rates

New Quick Method remittance percentages will apply to reporting periods that begin on or after January 1, 2008. For reporting periods that straddle January 1, 2008, the existing percentages will apply to consideration that becomes due, or is paid without becoming due, before January 1, 2008 and the new remittance rates will apply to the balance of the consideration. Therefore, unless the registrant has a reporting period ending on December 31st (as all monthly filers and most quarterly filers would) then two different rates will apply to the reporting period. As a result, any annual filers that do not have a December 31 reporting year end will have to do an extra calculation for 2008.

For service-based businesses located in Ontario, the old rates were 3.3% of the first \$30,000 of GST-included sales per year and 4.3% on the balance. The new rates will be 2.6% on the first \$30,000 and 3.6% on the balance.

For remittance rates for businesses that mainly purchase goods for resale, and for supplies made in participating provinces, other percentages apply.

Employee Allowances

GST registrants can usually claim ITC's for reasonable expense allowances paid to employees (eg mileage allowances, meal allowances etc.). Prior to the rate change, the ITC was calculated as 6/106 of the amount of the allowance. The new calculation will be 5/105 (13/113 for HST) for allowances paid on or after January 1.

Employee Expense Reimbursements

ITC's for GST paid on employee expense reimbursements will be claimed based on the actual amount of GST being reimbursed – regardless of the date on which the reimbursement takes place.

If, however, the company uses the 5/105 factor to claim ITC's for certain categories of expenses reimbursed to employees, then the new factors will be 4/104 for GST and 12/112 for HST, and will apply to all reimbursements paid to the employee on or after January 1, 2008 regardless of when the underlying expense was incurred or the expense report was submitted.

Employee and Partner Rebates

When preparing the personal income tax return for employees or partners, a GST rebate is available with respect to employment or partner expenses that are deductible for income tax purposes. The amount of the rebate is currently 6/106 of the tax-paid expenditures. For 2008 and subsequent years, the rebate percentage is 5/105.

Coin Operated Devices

The amount of GST that must be remitted in respect of sales made through coin-operated devices is based on the date the money is removed from the machine. For money removed prior to January 1, 2008, the rate of tax is 6/106. For money removed after December 31, 2007, the rate of tax is 5/105.

Anti-Avoidance Rules

Rules have been introduced to deem the tax rate to be 6% where an agreement has been modified or annulled and replaced with a new agreement prior to January 1, 2008 where the purpose of the new agreements was to take advantage of the new 5% tax rate. These anti-avoidance rules apply only where the parties to the agreement are not dealing with each other at arm's length.

Tips and Traps

Purchasing Real Property

If you can't claim an ITC for the GST paid when acquiring land or a building, consider working with the vendor to enter into a new agreement that delays the closing until after December 31, 2007, to obtain the lower 5% rate.

System Changes – Effective Date versus Transaction Date

Many computer systems will have to be modified, not only to take into account the rate reduction from 6% to 5%, but also to take into account the date the transaction is posted into the system. If, for example, an invoice is dated in December 2007, but entered in the system in January 2008, the rate of tax is likely 6%, but the system may automatically (in error) default to a 5% entry rate.

Automatic Calculations of GST paid to claim ITC's

Many software programs automatically calculate the GST input tax credit assuming that the rate of tax paid is 6%. These software programs will have to be modified to reflect the lower GST rate. Once the modification is made, it will still be necessary to over-ride the calculation, for example, when an old invoice on which GST is paid at 6% is entered in the system after the system has been updated to the new 5% rate. Businesses will have to be careful to maximize their ITC claims.

Employee Expense Claims

Pay employee allowances prior to January 1 to obtain an ITC at the rate of 6/106 instead of 5/105. The factor to apply is based on when the allowance is paid, and not on the date that the underlying expenses relate to, or the date on which the expense claim is submitted to the employer.

If using the simplified method to claim ITC's for employee reimbursements, pay the reimbursements prior to January 1 to be able to claim the ITC at the rate of 5/105 instead of the new rate of 4/104 (12/112 for HST).

Bad Debts and Price Adjustments

Businesses that claim relief from GST on bad debts will be able to claim back the actual amount of GST that has become uncollectible. This will be 7/107 for supplies made before July 1, 2006, 6/106 for supplies made between July 1, 2006 and December 31, 2007 and 5/105 for supplies made after December 31, 2007.

Similar logic will apply to price adjustments after December 31, 2007 for original sales made prior to January 1, 2008.

For more information about the reduction in GST contact a professional at Welch LLP or visit us at www.welchllp.com

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