TRENDWATCH

HST in Canada: The Winners and Losers

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The provinces of Canada continue to integrate their provincial sales tax regimes with the federal Goods and Services Tax (GST). Most recently, British Columbia and Ontario announced plans to move to a single value-added tax (VAT) regime, with rates of 12 per cent in British Columbia and 13 per cent in Ontario. With effect from July 1, 2010, B.C. and Ontario will join the Atlantic provinces of New Brunswick, Nova Scotia, and Newfoundland and Labrador, all of which have levied the Harmonized Sales Tax (HST) since 1997; and Québec, which introduced its own value-added tax in 1991 in the form of the Québec Sales Tax.

The move to HST by Canadian provinces reflects a worldwide trend in consumption tax. VAT systems such as the HST and GST are now the world's most common method of taxing consumption, with 29 of the 30 member countries of the Organisation for Economic Co-operation and Development using a VAT/GST system, and some 130 countries worldwide having adopted this method of taxation.

The change from a provincial sales (or consumption and use) tax to a multi-stage value-added tax in the form of the HST should benefit many businesses, streamlining compliance by replacing two sets of transaction tax rules with a single, comprehensive regime. A single set of rules will save millions of dollars in compliance costs for business and in administration costs for the governments of British Columbia and Ontario.

Most businesses that currently make GST-taxable goods or services, or that supply them on a GST zero-rated basis for export, should be entitled to fully recover the higher HST they will pay on inputs into their businesses. These businesses will no longer pay unrecoverable provincial sales taxes on purchases of goods and certain services, and will not embed them in the costs of the goods and services they produce.

A significant winner will be the computer software and services industry as its sales will no longer be subject to unrecoverable provincial sales tax. This tax relief should provide some much-needed stimulus for this sector.

However, other aspects of the new HST regime in British Columbia and Ontario will be more costly.

On a limited range of inputs, all businesses making more than $10 million in GST/HST-taxable sales will be unable to claim input tax credits to recover the provincial portion of the HST (7 per cent in British Columbia and 8 per cent in Ontario). These inputs will include telecommunications services (other than Internet access or toll-free numbers), road vehicles under 3,000 kg (including parts, services and fuel), as well as food, beverages and entertainment. A restriction on the recoverability on inputs of energy should have the most significant impact, as energy inputs are currently fully exempt under the existing provincial sales tax regimes. By contrast, most energy sources will be treated as fully taxable supplies following harmonization. These developments will have a negative impact on many manufacturers and other significant users of energy.

The financial services sector, which recovers no GST/HST on inputs into the making of financial services will be subject to an increased burden as a result of the transition. In particular, insurance providers in Ontario will be affected, as Ontario will maintain its 8 per cent sales tax on premiums for property insurance other than automobile insurance. This is similar to the sales tax that Newfoundland and Labrador maintained on its insurance premiums until only a couple of years ago.

In addition, the so-called MUSH sector of municipalities, schools, universities and hospitals, which recovers only limited GST/HST by way of rebate, has had its rebate levels for the provincial component of the HST set, with the intent that it will incur no more unrecoverable HST than what it currently incurs in provincial sales tax.

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The new home construction industry will face a significant increase in tax on more expensive homes, which will bear the full 12 per cent HST in British Columbia on the value of new homes and condominiums above $525,000, and the full 13 per cent HST in Ontario on values above $400,000.

Increasingly, provinces that continue to maintain sales tax regimes—Manitoba, Saskatchewan and Prince Edward Island— are encouraged by the federal government to undergo the same transition and it is likely these hold-outs will follow suit in the coming years.

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