



TAX EXECUTIVES INSTITUTE, INC.

2009-2010 OFFICERS

NEIL D. TRAUBENBERG

President

Sun Microsystems, Inc.
Broomfield, Colorado

PAUL O'CONNOR

Senior Vice President

Millipore Corporation
Billerica, Massachusetts

DAVID M. PENNEY

Secretary

General Motors of Canada
Limited
Oshawa, Ontario

CARITA R. TWINEM

Treasurer

Briggs & Stratton Corporation
Milwaukee, Wisconsin

SHERRIE ANN POLLOCK

Vice President-Region I

RBC Dexia Investor Services
Toronto, Ontario

PAUL HELLER

Vice President-Region II

Royal Bank of Canada
New York, New York

JOHN A. CONLEY

Vice President-Region III

Citigroup, Inc.
Greenwich, Connecticut

GARY W. DONER

Vice President-Region IV

Libbey Inc.
Toledo, Ohio

PAUL J. WESTMAN

Vice President-Region V

GKN America Corp.
Lisle, Illinois

PATRICIA DIANA YOST

Vice President-Region VI

Whole Foods Market, Inc.
Austin, Texas

LYNN B. JORDAN

Vice President-Region VII

Performance Food Group
Company

Richmond, Virginia

DAVID E. STEVENS

Vice President-Region VIII

Movie Gallery
Wilsonville, Oregon

PETER H. TAYLOR

Vice President-Region IX

Du Pont de Nemours
International
Geneva, Switzerland

TIMOTHY J. MCCORMALLY

Executive Director

ELI J. DICKER

Chief Tax Counsel

MARY LOU FAHEY
General Counsel

November 3, 2009

Please Respond To:

Ms. Sherrie Ann Pollock

Head, Taxation

RBC Dexia Investor Services

155 Wellington Street West, 10th Floor

Toronto, ON M5V 3L3 Canada

416.955.7373

sherieann.pollock@rbcdexia.com

Ms. Lise Potvin

Director

Department of Finance

ST-Director's Office

140 O'Connor Street

Ottawa, Ontario

K1A 0G5

Dear Ms. Potvin:

In connection with Tax Executives Institute's December 9, 2009, liaison meeting with representatives of the Department of Finance, I am pleased to enclose the Institute's questions and comments on pending commodity tax matters.

I am also enclosing a copy of the Institute's submission to Canada Revenue Agency in connection with our 2009 liaison meeting with its representatives. If you should have any questions about either agenda, please do not hesitate to call either Diana M. Spagnuolo, Chair of TEI's Canadian Commodity Tax Committee, at 403.237.2948 (diana.m.spagnuolo@esso.ca.), or me at 416.955.7373 (sherrieann.pollock@rbcdexia.com).

TEI looks forward to meeting with the representatives of the Department of Finance on December 9th.

TAX EXECUTIVES INSTITUTE, INC.

Respectfully submitted,



Sherrie Ann Pollock
Vice President for Canadian Affairs

cc: Diana M. Spagnuolo
Rainer Nowack
John Sitka

TAX EXECUTIVES INSTITUTE, INC.

EXCISE TAX QUESTIONS

Submitted to

THE DEPARTMENT OF FINANCE

DECEMBER 9, 2009

Tax Executives Institute, Inc. (hereinafter “TEI” or “the Institute”) welcomes the opportunity to present the following questions on Canadian commodity tax issues, which will be discussed with representatives of the Department of Finance during TEI’s December 9, 2009, liaison meeting. If you have any questions about the agenda, please do not hesitate to call Sherrie Ann Pollock, TEI’s Vice President for Canadian Affairs, at 416.955.7373, sherrieann.pollock@rbcdexia.com; or Diana M. Spagnuolo, Chair of TEI’s Canadian Commodity Tax Committee, at 403.237.2948, diana.m.spagnuolo@esso.ca.

TECHNICAL QUESTIONS

1. HARMONIZATION

A. *Update.* TEI supports the decisions of the Provinces of Ontario and British Columbia to harmonize their provincial sales taxes (PST) with the federal goods and services tax (GST), but continues to believe that financial services should be zero-rated. During the liaison meeting, please provide an update on developments concerning the adoption of a harmonized sales tax (HST).

B. *Place of Supply Rules for Services and Intangibles.* As the HST is introduced in additional provinces, significant issues will arise relating to the current place of supply rules for services and intangibles. TEI recommends that the following principles be used as a basis for revising these rules:

If the supply for services or intangibles is considered to be made in Canada under the current federal Excise Tax Act (ETA), the location (*i.e.*, address) of the customer as evidenced by the business agreement should be used to determine the tax to charge. If the customer is located in one of the harmonized provinces, then the HST would apply.

The government may consider exceptions to the rule to attribute the supply to a province other than that in which the customer is located if it relates to tangible personal property or real property located in that other province, or if the supply is made to an individual who is in a province at the time it is performed and had contact with the supplier (similar to sections 7 and 10.1 of Part V of Schedule VI of the ETA). These exceptions, however, should be as limited as possible in order to simplify HST administration.

In some respects, similar rules now exist in the exceptions to the place of supply rules within the regulations (*e.g.*, for computer-related services, Internet, and trustee services for registered retirement savings plans (RRSP), registered retirement income funds (RRIF), and registered education savings plans (RESPs)).

C. *Exceptions to the Place of Supply Rules for Services.* If the place of supply rules for services are not revised, the implementing regulations should be expanded. Currently, the statute provides that place of supply is generally based on the place of performance of the service, with consideration given to the place of negotiation of the contract. Exceptions to this general rule are set forth in the regulations (entitled *Place of Supply GST/HST Regulations*).

Current examples of services not falling within the general rule relate to memberships supplied to individuals (which are taxed based on the mailing address); trustees' services in respect of a RRSP, RRIF, or RESP (which are taxed based upon the subscriber's address); and Internet-access or computer-related services (which are taxed based upon the recipient's address if tracked, or the mailing address of the customer if the recipient's location is not tracked).

TEI recommends that financial planning, investment management, custodial services, and other trustee services be added to the regulations with the place of taxation based on the normal address of the customer. Call centre services outside of those provided in respect of computer services (which are already covered by the regulations) should also be included in the regulations with tax applying based on the location of the recipient, if tracked, or the mailing address of the customer.

During the liaison meeting, please provide an update on the place of supply rules.

2. REPORTING OF RESTRICTED ITCs UNDER THE HST

During TEI's 2009 Annual Canadian Tax Conference, Finance explained that monthly reporting of restricted input tax credits (ITCs) under Ontario's HST regime may

be required. An administratively easier alternative is for full ITCs to be claimed during a calendar year with the appropriate repayment of disallowed amounts by February 28 of the succeeding year. What is the current status for this rule? Is the alternative being considered? If not, what are the policy reasons for requiring monthly reporting? Will whatever rule is adopted also be applied to British Columbia's HST?

3. HST TRANSITIONAL RULES

There are special rules for determining amounts that a selected listed financial institution (SLFI) must include in a special attribution method (SAM) that serves as a proxy for the appropriate amount of the provincial component of the HST (*i.e.*, the 8-percent component) that should be borne by the SLFI on property and services it consumes in its exempt activities.

The transitional rules released on October 14, 2009, require self-assessment of tax on supplies paid after that date and before May 1, 2010, where the supply will be received or consumed on or after the July 1, 2010, implementation date.

Although the SAM formula rules for this transition period have not been released, the rules in place during the 1997 harmonization required a company to base the HST payable on a proration of the total GST paid during the fiscal year. Thus, all GST paid during the fiscal year formed the basis for the calculation of the provincial component of the HST. This resulted in SLFI's paying the provincial component of the HST on both a self-assessment basis and again under the prorated SAM formula.

To ensure that double taxation does not occur in the upcoming transition, the calculation of the provincial component of the HST should be based only on GST incurred on or after July 1, 2009. Is Finance considering adjusting the SAM formula in this manner?

4. POINT OF SALE REBATES

British Columbia has announced that it will provide an automatic point-of-sale rebate on the provincial portion of the HST for purchases of gasoline and diesel for motor vehicles. Finance has stated it will zero-rate the provincial portion for these products, permitting consumers to pay only the GST portion when they purchase gas and diesel at the pump. Other goods, however, such as natural gas, electricity and home heating, will bear the full HST.

British Columbia has subsequently proposed an HST rebate for energy. Will Finance also consider zero-rating these products?

5. FINANCIAL INSTITUTIONS

A. *Special Attribution Method (SAM)*.¹ Currently, the SAM formula allows an adjustment to net tax under ETA section 225.2 (“HST liability”) to be reduced only by the provincial component of HST paid or payable in the current fiscal year. Thus, where the HST is not identified in a company’s financial records in the year in which it is incurred, it may be inadvertently excluded from the HST paid amount.

TEI recommends that the SAM formula be amended to permit a reduction of the final HST liability by the provincial component of the HST paid or payable in the current or previous year, so long as this amount was not included in the SAM calculation in the prior year. This change would be consistent with the two-year window that is currently available to SLFIs to claim ITCs.

B. *The Australian Approach*. Currently, Australia permits a 75-percent ITC for specific processing (*i.e.*, outsourced) services used to further exempt financial activities. Australia’s ITC methodology permits financial institutions to take advantage of the cost and productivity savings that can be derived from outsourcing. This approach could also provide relief to mutual fund trusts in respect of their management and administration fees.

The Australian approach recognizes that, in making the decision to outsource, financial institutions must consider replacing non-taxable salary costs with taxable services provided by a third party. It helps financial institutions deal with these increased costs and encourages them to take advantage of the cost and productivity savings resulting from outsourcing.

Australia also permits an enhanced ITC on supplies made between related parties, which is helpful for financial institutions receiving outsourced services from a non-resident related entity with which they are not permitted to elect to treat the services as exempt supplies under ETA section 150. This expanded treatment allows financial institutions to take advantage of global synergies and the development of centres of excellence. In Canada, it could be expanded to cover management and administrative fees paid by mutual fund trusts if determined to be in the nature of outsourced services.

Has Finance considered implementing a similar approach in Canada? What concerns, if any, have been identified with the proposal?

C. *Future Approaches*. Although TEI continues to believe that financial services should be treated as zero-rated supplies, the federal government should consider developing a methodology for taxing financial services. To mitigate the cascading tax on financial services, other countries have implemented solutions under which financial services are taxable when supplied to business customers (who, in turn, are eligible for ITCs based on their level of commercial activities). This is similar in operation to

¹ Excise Tax Act, R.S.C., ch. E-15, § 225.2 (1985).

Canada's treatment of exported financial services, the supply of which entitles financial institutions to recover ITCs on purchases made in respect of those zero-rated supplies.

TEI welcomes Finance's reaction to this approach, especially in the area of supplies made to business.

D. *Proposed Legislative Changes.* On September 23, 2009, Finance released draft legislation, explanatory notes, and a backgrounder on several measures aimed at improving and streamlining the application of the GST to the financial services sector. The proposal includes changes in the following areas:

- Pension expenses;
- Deadline for filing annual returns for financial institutions;
- Imported supplies;
- GST/HST Annual Information Schedule (GST111); and
- ITC allocation methodology.

Please provide a brief overview of what Finance considers to be the most important changes in the draft legislation and how the changes will streamline and simplify the law.

6. TRADING EMISSION ALLOWANCES AND CARBON CREDITS

Certain European countries are moving to either zero-rating or exempting the trading of emission allowances and carbon credits. Please confirm the current treatment of these supplies in Canada. Are changes contemplated?

7. NON-RESIDENT INSTALLATION SERVICES

In the agenda for the 2005 TEI/Finance Liaison meeting, TEI recommended that section 252.41 be amended to grant an extended filing period for the rebate, as follows:

Section 252.41 of the Excise Tax Act (ETA) requires a non-resident, non-registered recipient of an installation service to file for a rebate "within one year after the completion of the service" in order to receive a rebate of the tax paid by the recipient in respect of the supply of the service. Subsection 252.41(1)(b) of the ETA protects against revenue loss owing to inappropriate rebates or input tax credits (ITCs) by non-commercial activities that acquire such supplies, so why only allow one year for applying for a rebate rather than the common two-year period allowed for other rebates, or even a four-year period consistent with the standard audit period?

As an example, consider the following scenario: A Canadian registered supplier who installs tangible personal property into real property at a site in Canada for a non-resident, non-registered recipient is required to invoice the tax in respect of the supply. If the supplier fails to invoice the recipient, and on audit it is determined that the tax should have been invoiced, Canada Revenue Agency (CRA) will assess the supplier for the applicable goods and services taxes (GST) and harmonized sales taxes (HST). If the supply was made within the most recent year of the audit, a rebate may still be available if the time limit has not expired. But if the supply was made before the most recent audit year, it is likely that the one-year period will have expired.

Would the Department consider extending the time period?

At the 2005 meeting, Finance expressed support for TEI's recommendation, but, to date, no change to section 252.41 has been forthcoming. In light of harmonization efforts in Ontario and British Columbia, please provide an update on this issue, including whether any changes to the existing legislation are planned.

8. PROCUREMENT CARD WORKING GROUP

At the time of the March 2009 Ontario Budget Announcement regarding harmonization, the working group representing the TEI Commodity Tax Committee and its counterparts at Finance appeared to be very close to agreeing in principle to a more straightforward solution to claiming ITCs on procurement card purchases, as opposed to the existing rules outlined in GST Notice 199.

We understand that the announcements of the harmonization of two provinces prompted Finance to alter its priorities. What is the status of this project?

9. OECD DEVELOPMENTS

We would welcome an update on OECD developments and initiatives, especially in respect of the project relating to the application of VAT/GST to internationally traded services and intangibles.

10. CONTINUOUS TRANSMISSION COMMODITY

Currently, the place of supply rules do not work well with respect to "continuous commodity transmission" (CTC), such as oil or natural gas. There are provisions that prevent the recognition of a supply each time a CTC crosses the Canada-U.S. border in the normal course of its transmission through a pipeline or other conduit. CRA requires, however, clarification that this is not an import.

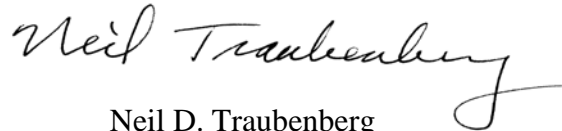
TEI has been working with Finance, CRA, and the Canada Border Services Agency to update the legislation. When can we expect to see the change introduced?

11. CONCLUSION

Tax Executives Institute appreciates this opportunity to present its comments and questions for discussion. We look forward to meeting and discussing our views with you on December 9, 2009.

TAX EXECUTIVES INSTITUTE, INC.

Respectively submitted,

A handwritten signature in cursive script that reads "Neil Trautenberg". The signature is written in black ink and is positioned to the left of the printed name.

Neil D. Trautenberg
International President