# CRA/TEI LIAISON MEETING

## DECEMBER 8, 2009

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## AGENDA

**13:00 – 13:15 Opening / Introduction**

- Brian McCauley / Pierre Bertrand
- Neil Traubenberg / Timothy J. McCormally / Sherrie Ann Pollock

**13:15 – 14:45 Presentations – CRA & TEI**

- Harmonization in Ontario and British Columbia
  – Technical Overview (Costa Dimitrakopoulos)

- HST Management
  – An Industry Perspective ( Diana Spagnuolo)

**14:45 – 15:00 Refreshment Break**

**15:00 – 16:30 Technical Questions**

- Question # 2 (Debbie Emmerson / Michael Robillard)
- Question # 5 (Ted Gallivan)
- Question # 3 (Harold Howard)
- Question # 4, 7 (Marilena Guerra)
- Question # 10 (Chris Lewis)
- Question # 1 (Dawn Weisberg)
- Question # 6 (Roy Osudar)
- Question # 9 (Mark Hartigan)
- Question # 8 and Supplemental question (in binder)

**16:30 Closing Remarks**

# CRA / TEI
# LIAISON MEETING
# DECEMBER 8, 2009

## CRA ATTENDEES

### LEGISLATIVE POLICY & REGULATORY AFFAIRS BRANCH (LPRAB)

| | |
|---|---|
| **Brian McCauley** | Assistant Commissioner, LPRAB |
| **Pierre Bertrand** | Director General, Excise & GST/HST Rulings |
| **Ivan Bastasic** | Director, Financial Institutions & Real Property |
| **Phil Nault** | Director, Public Service Bodies and Governments |
| **Phil McLester** | Director, Excise Duties and Taxes |
| **John Sitka** | Director, General Operations and Border Issues |
| **Costa Dimitrakopoulos** | Director, PSTAR |
| **Christopher Lewis** | A/Manager, Goods |
| **Dawn Weisberg** | Manager, Financial Institutions |
| **Roy Osudar** | Manager, Government Sectors |
| **Mark Hartigan** | Manager, Excise Taxes and Other Levies |

### COMPLIANCE PROGRAMS BRANCH (CPB)

| | |
|---|---|
| **Susan Betts** | Director, *Technical Applications and Valuations* |
| **Cindy Negus** | Manager, *Provincial Sales Tax Administration Reform* |
| **Marilena Guerra** | A/Manager, *GST/HST Technical Applications* |
| **Rick Power** | A/Manager, *Voluntary Disclosures Program (VDP)* |
| **Harold Howard** | *Policy and Programs Coordinator (VPD)* |

### TAXPAYER SERVICES & DEBT MANAGEMENT BRANCH (TSDMB)

| | |
|---|---|
| **Michael Robillard** | Senior Program Officer, *Policy and Technical Services* |

### ASSESSMENT AND BENEFIT SERVICES BRANCH (ABSB)

| | |
|---|---|
| **Ted Gallivan** | Director, *Business Registration and Corporate Programs* |
| **Miro Raczylo** | Director, *Business Accounting Programs* |
| **Debbie Emmerson** | Manager, *Accounting Adjustments and Field Enquiries* |

# CRA / TEI
# LIAISON MEETING
# DECEMBER 8, 2009

## TEI ATTENDEES

**Timothy J. McCormally** *TEI Washington,* Executive Director
**Neil D. Traubenberg** *Sun Microsystems, Inc.* & TEI International President
**Eli J. Dicker** *TEI Washington,* Chief Tax Counsel
**Mary L. Fahey** *TEI Washington,* General Counsel
**Sherrie Ann Pollock** *RBC Dexia Investor Services & TEI* Vice President for Canadian Affairs

### CANADIAN COMMODITY TAX MEMBERS

**Diana M. Spagnuolo** *Imperial Oil Limited & Committee,* Chair
**Kim N. Berjian** *Conoco Phillips Canada & Committee,* Vice-Chair
**Carol Felepechuk** *TD Bank Financial Group & Committee,* Vice-Chair
**Richard Taylor** *Rogers Communications Inc. & Committee,* Vice-Chair
**Martina Krummen** *SNC Lavalin Inc.*
**Carol Nixon** *Laxness Inc.*
**Robert C Leprich** *Molson Canada*
**Phil W. Riley** *ArcelorMittal Dofasco Inc.*
**Diane M. Sekula** *CIT Financial Ltd.*
**Robert J. Smith** *Air Canada*
**Natalie St-Pierre** *Bell Canada*
**Michael J. Willis** *Lafarge Canada Inc.*

## QUESTION # 1: Form GST111

A. *Update*. TEI members recently submitted the Form GST111, *Financial Institution GST/HST Annual Information Schedule*. In September, several changes to the form were announced. During the liaison meeting, please provide an overview of the reasons for the changes.

B. *Misdirected Requests* to File Form. Several TEI members — who do not work for companies that qualify as financial institutions under subsection 149(1) of the Excise Tax Act (ETA) — have received letters requesting them to file the Form GST111, apparently based on the inclusion of interest and dividend income on their income tax returns. The reporting of such income from a closely related corporation, however, is not included in the calculation under paragraphs 149(1)(b) and (c), which determines whether a registrant qualifies as a financial institution. Responding to these requests is time consuming; indeed, some members report receiving multiple inquiries or inquiries in subsequent years, even after demonstrating they were not required to file.

   During the liaison meeting, we request an update on this program, including how it can be modified to avoid future requests to file the form. In the interim, CRA should suspend requesting the information.

## ANSWER # 1: Form GST111

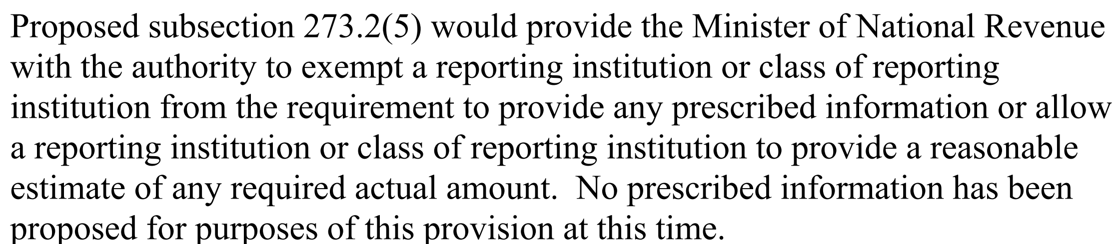
A. On September 23, 2009, the Department of Finance released draft legislation, explanatory notes and a backgrounder with respect to a proposed information return for financial institutions. The information return would be used by financial institutions to meet the same information reporting requirement that is currently met by filing Form GST111, *Financial Institution GST/HST Annual Information Schedule* (FI Schedule).

The most significant aspect of the new draft legislation is that it would provide for specific penalties under new proposed section 284.1 of the ETA for failure to report or misstatements of amounts required to be reported on the information return. An exception is proposed in the draft legislation where a registrant has exercised due diligence in attempting to report the required information. The penalty provisions would be phased in and the Minister of National Revenue would be given certain discretion in the application of penalties.

These penalties were introduced to promote compliance and legislative certainty and would generally apply for fiscal years commencing after 2008. There is an exception proposed which would apply if the proposed legislation is not law at the time when the penalties would otherwise apply.

In order to provide certainty and guidance to financial institutions, proposed section 273.2 of the ETA sets out who would be required to file an information return. Those persons required to file the information return include listed and de minimis financial institutions under subsection 149(1), which is the same as for the FI Schedule, as well as persons who are considered to be financial institutions under either subsection 149(2) or (3) as a result of an amalgamation or the acquisition of a business.

The proposed legislative framework also includes classifying the type of information reported on the return and allowing a financial institution to provide a reasonable estimate of an amount on the return where it is not an "actual amount" and is not reasonably ascertainable at the time on or before which the return is required to be filed. The terms "actual amount" and "tax amount" are defined in proposed subsection 273.2(1).



Proposed subsection 273.2(5) would provide the Minister of National Revenue with the authority to exempt a reporting institution or class of reporting institution from the requirement to provide any prescribed information or allow a reporting institution or class of reporting institution to provide a reasonable estimate of any required actual amount. No prescribed information has been proposed for purposes of this provision at this time.

B. In order to ensure that all registrants who are required to file an FI Schedule are informed of this obligation, each year a letter and an FI Schedule is sent to a broad spectrum of registrants who may be required to file the FI Schedule. We take this approach as the FI Schedule is a relatively new filing requirement, and because the requirement to file can vary for individual registrants from year to year depending on a number of factors, including the registrant's revenue from financial services (e.g., interest income). As a result of this broad-based approach, it is likely that more registrants are sent the letter and FI Schedule than are actually required to file it.

   If a financial institution's total annual revenue does not exceed $1 million for a particular fiscal year, the financial institution should phone a GST/HST rulings office at 1-800-959-8287 or send a letter to the Tax Centre identified in the letter to advise us of this fact. If a person is not a financial institution, the person should send a letter to the identified Tax Centre clearly explaining why the person is not a financial institution.

   Until we are confident that those persons that are required to file the FI Schedule are aware of this relatively new reporting requirement, we will continue to use this broad-based approach in sending out FI Schedules. We are working to improve the process through which we identify those registrants that may be required to file the FI Schedule so that in the coming years we hope to minimize the number of registrants that are not financial institutions that receive the FI Schedule.

## QUESTION # 2: Standardized Accounting

The standardized accounting initiative — under which the federal government is harmonizing various accounting, interest, and penalty provisions administered by CRA — has significantly increased the transfer of funds among taxpayer accounts. The result is a substantial administrative burden on both taxpayers and government agents as they try to unravel the trail and rationale behind the transfers.

The burden is borne by taxpayers large and small. Large taxpayers have many accounts, often maintained by different areas within a business. Small taxpayers, while perhaps not dealing with the same number of accounts, still face the burden of identifying the cause of the transfers with limited resources.

Revenue Quebec has also implemented a revenue accounting system that facilitates the offsetting of overpayments of one tax against unpaid liabilities for other taxes, but the agency notifies the taxpayer of any deficiencies in filing and identifies the provision that the taxpayer has failed to comply with. This type of notification permits the taxpayer to rectify the error or explain why the proposed offset is wrong (for example, because the identified returns have in fact been filed but not yet processed).

Implementing a similar process to notify taxpayers of the contemplated transfers and the reasons for them would save considerable time for both taxpayers and the government.

A. Is CRA considering any enhancements to improve the process, including ensuring there is an audit trail to permit the tracing of the movement of funds and the reasons for that movement?

B. TEI recommends that CRA adopt the following policy:

   (i) If a large file case manager is assigned to an account, all transfers should be approved in advance by that manager, permitting the manager and taxpayer to discuss the problem and ensure that the transfer is correct.

   (ii) If a large file case manager is not assigned to a taxpayer's account, a written notification should be sent to the taxpayer, explaining the transfer under consideration. The transfer would not be made until 30 days after notification.

## ANSWER # 2: Standardized Accounting

A. The CRA has implemented changes to improve our communication products to include additional information (account number, period end and amount transferred) pertaining to both accounts affected by the offset. Please see attached copy of a notice to a taxpayer showing an offset has been made from one account to another. The account number information is shown at the 15 digit level so includes the program identifier. The CRA will continue to work with the TEI as well as others to identify other improvements to our communication products.

B. The CRA has developed an automated offset process within the standardized accounting system in order to decrease the cost of manual processing as well as ensuring refunds are issued with all due dispatch, in part to avoid increasing the cost of refund interest. The manual intervention suggested to notify taxpayers would delay the automated offset process, increasing the cost of processing and possibly the cost of refund interest. The CRA is not considering at this time any modifications that would result in the fully automated offset process becoming one that relies on manual intervention.

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DRAFT



| Date of Mailing |
|---|
| April 9, 2009 |
| Business Number |
| |
| Period Covered |
| 2008-12-01 to 2009-02-28 |

## NOTICE OF (RE)ASSESSMENT
## GOODS AND SERVICES TAX/HARMONIZED SALES TAX (GST/HST)

Reproduction

### SUMMARY OF (RE)ASSESSMENT

RE: GST/HST Return

Reporting Period From: 2008/12/01 To: 2009/02/28

**Reference Number:**

| | | | |
|---|---|---|---|
| Line 101 | Sales and Other Revenue | $ | 0.00 |
| Line 105 | Total GST/HST and Adjustments | $ | 0.00 |
| Line 108 | Total ITCs and Adjustments | $ | 215.55 Cr |
| **Line 109** | **Net Tax Assessed** | $ | 215.55 Cr |
| | **Result of (Re)Assessment** | $ | 215.55 Cr |
| Amount Transferred | | $ | 215.55 |
| | **Balance** | $ | 0.00 |

Reproduction

### EXPLANATION

We have processed your GST/HST return for the period ending February 28, 2009.

**Line 101 "Sales and other revenue" is a mandatory line. This amount should be rounded off to the nearest dollar. Line 101 should only be zero if no business activity was recorded during the reporting period.**

The following is a breakdown of the amount transferred.

| | | Amount: | | Effective Date: |
|---|---|---|---|---|
| To: | 2008/11/30 | $ | 215.55 | 2009/03/17 |

**If you need more information please see "General Information."**

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Page 1 of 3

| Date of Mailing | April 9, 2009 |
|---|---|
| Business Number | [redacted] |
| Period Covered | 2008-12-01 to 2009-02-28 |

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**NOTICE OF (RE)ASSESSMENT**
**GOODS AND SERVICES TAX/HARMONIZED SALES TAX (GST/HST)**

**RESULTS**

This notice explains the results of our (re)assessment of the GST/HST return(s) received on March 24, 2009, for the period indicated above.

| | | |
|---|---|---|
| **Result of this (Re)Assessment** | $ | 215.55 Cr |
| **Prior Balance** | $ | 0.00 |
| **Amount Transferred** | $ | 215.55 |
| **Total Balance** | $ | 0.00 |

Please keep this Notice of (Re)Assessment for your records.

Commissioner of Revenue

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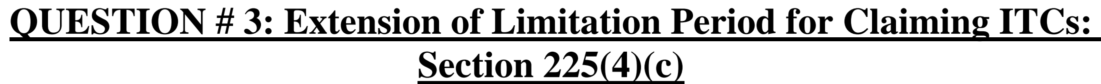

## QUESTION # 3: Extension of Limitation Period for Claiming ITCs: Section 225(4)(c)

ETA section 225(4)(c) requires the supplier to disclose in writing to the registered customer that the Minister has assessed the supplier, and the customer must pay the tax prior to claiming any input tax credit (ITC). This requirement is difficult to comply with when the taxpayer has made a voluntary disclosure because there are frequently delays in issuing assessments after a voluntary disclosure and the taxpayer may not invoice the GST to the party who should have been charged until after the assessment is issued.

A. Where there has been a prolonged delay in issuing the assessment, is CRA granting any leniency concerning when the taxpayer may issue the invoice without negatively affecting the ability of the purchaser to claim their ITCs?

B. Will CRA consider proposing that the Department of Finance make any changes to this section to accommodate the current voluntary disclosure process?

C. Is CRA considering any changes to its voluntary disclosure program?

## ANSWER # 3: Extension of Limitation Period for Claiming ITCs: Section 225(4)(c)

A. This situation is not unique to the VDP. It may occur within an Audit or other program areas where assessments are raised. The timing of the invoicing is beyond the control of the CRA. There is no discretion available to the CRA with respect to the timing of the invoicing for the GST pursuant to ETA section 225(4)(c) or to the claiming of the associated ITC. These are legislative requirements the CRA must follow no matter which program within CRA is dealing with the matter.

B. The VDP process occurs before the assessment. ETA section 225(4)(c) deals with issues after the assessment. Therefore, the VDP is not affected by this provision and therefore we are not considering proposing any amendments. Taxpayers may propose amendments directly to the Department of Finance with respect to any changes in the legislation.

C. There are no substantive changes to the VDP being contemplated at this time. However, there are changes to the GST WASH Transaction Policy being made that will be administered by the VDP officers that will benefit registrants who voluntarily disclose WASH transactions. Details will be released in the near future.

## QUESTION # 4: Harmonization

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 transitional period, however, invoices issued by suppliers will likely not identify the right name of the tax to be charged, although the amount of the taxes charged under these invoices will be correct. For example, many suppliers may incorrectly invoice the five-percent GST and eight-percent Ontario PST on tangible personal property shipped after June 30, 2010, rather than charging the thirteen-percent Ontario HST. A similar issue may occur in respect of services billed before July 1, 2010, but performed after that date, which would subject them to the new harmonized tax.

Since the amount of collected taxes will remain the same, companies' accounts payable departments will likely be unable to identify that the wrong taxes were charged, though these errors may be detectable after a review of the invoices issued and taxes paid.

TEI recommends that, during a reasonable transition period (say, 6 months), CRA permit recipients who have paid the proper amount of taxes to treat the PST invoiced as the provincial component of the HST and claim an ITC in respect of that amount. The failure to permit an ITC in these circumstances would create a heavy administrative burden for taxpayers, who would first request the supplier to cancel the original invoice, obtain a new invoice with the provincial component of the HST identified, and only then claim an ITC. This process could take months and may be impossible in some cases where a supplier refuses to reissue an invoice or no longer exists. This seems a harsh result, especially since the taxpayer has not received any advantage.

## ANSWER # 4: Harmonization

When a registrant is being audited, in a situation as described above, CRA auditors will make recommendations for assessment based on all of the facts of the situation.

When a supplier's invoice does not properly reflect the HST, it remains in the interest of the registered recipient of a supply to return to the supplier to have the invoice amended to properly reflect the HST for supplies made on or after July 1, 2010 as well as for supplies subject to the transitional rules.

It is imperative for registrants to prepare for harmonization by having their electronic point-of-sale equipment updated in time for the HST and where a registrant's business is such that it is possible that consideration could become due or is paid without having become due on or after May 1, 2010, for supplies to be provided on or after July 1, 2010, the point-of-sale equipment should be ready to properly invoice the amount when that is paid or becomes due before July 1, 2010.

## QUESTION # 5: GST Registration Process: Follow-Up

During its 2008 liaison meeting with CRA, TEI requested information on CRA's business registration services, noting that it is often easier to register a sole proprietorship for GST purposes than it is to obtain a GST number for a corporation or a trust. In response CRA said that it was "examining options for the development of a national inventory system for tracking all correspondence received in [Taxpayer Services Offices] TSOs, which should improve tracking of all correspondence being processed in TSOs."

TEI members continue to experience difficulties in having registrations completed on a timely basis. During our liaison meeting, please provide an update on this initiative.

## ANSWER # 5: GST Registration Process: Follow-Up

The CRA is committed to timely registration. Our service standard is to create a BN or add a new program account within 10 days of the receipt of the request. Our data shows that we meet this standard more than 98% of the time.

For cases that require faster turnaround we offer the following:

- Business Registration Online. A 24/7 on-line service that issues the BN and/or program account immediately.

- Phone registration for new BNs or program account additions. The ability to add a new program account over the telephone (provided incorporation details can be provided) is a new service that has been introduced subsequent to the December 2008 meeting.

To support the tracking of paper registrations, the inventory tracking system discussed at last year's meeting will be piloted in 4 TSOs [Tax Services Offices] and if all goes well with the poof of concept, we intend to roll out this system nationally in April 2010.

## QUESTION # 6: Emission Credits

What is the tax treatment of the buying, selling, and trading of emission credits for GST purposes? Please confirm that payments into Alberta's Climate Change and Emissions Management Fund to purchase Fund Credits are exempt from GST.

## ANSWER # 6: Emission Credits

CRA is unable to provide a specific interpretation as to how the GST/HST would apply to the buying, selling and trading of emission credits. However, we would welcome the opportunity to provide a ruling relating to the GST/HST treatment of the purchase and sale of such credits should any of your members so request. In order to provide such a ruling, we would require all the documentation relating to the specific set of facts, including any legislative authority relating to the emission credits in issue, information relating to the operation of the credit trading markets in question and any contracts or agreements regarding the purchase and sale of such credits.

With respect to your second issue concerning the GST status of payments made into Alberta's Climate Change and Emissions Management Fund (Fund) to purchase fund credits, we have reviewed the *Climate Change and Emissions Management Act* and the *Specified Gas Emitters Regulation* which provide the legislative authority for those payments. Based on a review of that legislation, it is our understanding that for every $15 contributed by a "person responsible" (as defined in the legislation) to the Fund, the Government of Alberta issues a fund credit to the "person responsible". The regulations characterize each fund credit issued as a revocable licence authorizing the "person responsible" to use one tonne of carbon dioxide equivalent in meeting its net emission intensity limit under the regulations. Therefore, based on our review of the authorizing legislation, it would appear that each fund credit, issued by the Government of Alberta for each payment of $15 into the Fund, may be a right that is an exempt supply under paragraph 20(c) of Part VI of Schedule V to the *Excise Tax Act* and as a result, no GST would apply to the issuance of the fund credit.

## QUESTION # 7: Waiver of Interest and Penalties

ETA section 281.1 grants the Minister authority to waive or cancel penalty and interest payable by a person under section 280. GST Memorandum 16.3.1, *Reduction of Penalty and Interest in Wash Transaction Situations*, provides that, in a wash transaction, CRA will consider waiving or cancelling the portion of the penalty and interest in excess of four percent of the tax not properly collected by the supplier if certain conditions are met.[1] Paragraph 11(b) of that memorandum requires that, among other conditions, the supplier must not have been previously assessed for the same mistake and must have "a satisfactory history of voluntary compliance."

What is CRA's rationale for this restriction? Because there is no revenue loss to the government in these transactions, TEI recommends that CRA apply the four-percent wash to all business-to-business (B2B) transactions. Are updates to GST Memorandum 16.3.1 contemplated in the near future?

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[1] A "wash transaction" occurs when a taxable supply is made and the supplier has not remitted an amount of net tax by virtue of not having correctly charged and collected the tax from the recipient who is a registrant who would have been entitled to claim a full ITC if the tax had been correctly applied.

## ANSWER # 7: Waiver of Interest and Penalties

Where there is a wash transaction, the CRA will consider waiving or cancelling the portion of the penalty and interest, payable at the time of assessment, that is in excess of 4% of the tax not properly collected by the supplier where the conditions identified in paragraph 11 of the GST/HST Memoranda Series 16.3.1, *Reduction of Penalty and Interest in Wash Transaction Situations*.

You have specifically asked what CRA's rationale is for the condition set out in paragraph 11(b) of whereby a supplier must not have been previously assessed for the same mistake and must have a satisfactory history of voluntary compliance.

The principle of voluntary compliance lies at the heart of the administration of the Canadian tax system. Under the GST, registrants have four main obligations:

- to register;
- to collect the taxes due and to calculate net tax;
- to report (file returns) in the prescribed manner and remit net taxes due; and
- to retain appropriate records and make such records available to determine the amount of tax due, or to prove the accuracy of any return.

For the most part, registrants determine their net tax and remit accordingly. Such a self-assessment system of collecting taxes is more efficient and more economical than other methods.

The application of the 4% wash penalty is to maintain the integrity of voluntary compliance in situations that meet all of the conditions set out in GST Memoranda Series 16.3.1. Where a supplier has been previously assessed for the same error or does not demonstrate that they are fulfilling their obligations under the GST by maintaining a satisfactory history of voluntary compliance, a reduction of penalties and interest will not be considered.

GST Memoranda Series 16.3.1 is, as most of our publications are, an evergreen document; that is to say, that where changes are necessary, they will be made in future releases. Should you have any comments or requests for change to this or any other Memoranda Series, please send them to the Director, Technical Publications and Programs Division, Excise & GST/HST Rulings Directorate.

## QUESTION # 8: Drop Shipment Certificate: Sale by Non-Resident

A U.S. company not registered for GST and not resident in Canada, Company (A), sells goods to GST-registered Company (B), who subsequently sells the goods to GST-registered Company (D), and the contract provides for the goods to be shipped to Company (D)'s premises in Canada. Legal delivery of the sale by Company (A) to Company (B) occurs after GST-registered Company (C) supplies a commercial service to Company (A), and the finished goods are shipped directly from Company (C) to Company (D) in Canada. Note that Company (B) never takes physical possession of the goods.

1. Can Company (B) issue a drop shipment certificate to Company (C), to enable Company (C) not to charge GST on the services performed for Company (A). If not, is Company (D) able to issue the referenced certificate, or is Company (A) liable to pay unrecoverable GST to Company (C)?

2. If Company (B) did issue a certificate under Section 179(2) and Company (C) accepted the certificate in good faith and doesn't charge GST on the supply of services to Company (A), does Company (C) possess the required documentation to relieve it from charging GST to Company (A)?

3. If Company (C) cannot accept a drop shipment certificate in good faith and GST applies, what option(s) does Company (A) have to recover the GST paid?

**TEI Comment:**

CRA has provided feedback and reference to CRA Memorandum 3.3.1; specifically paragraphs 25 and 71, and examples 6 and 11. TEI agrees:

1. that a drop shipment cannot be issued by any registrant in the question above

2. that a drop shipment certificate (if issued and accepted by Co. C) would not absolve Co. C of liability for tax under the Excise Tax Act

3. that the supply of a commercial service by Co. C is a deemed 'supply' as per Section 179(1); ie., GST applies on the full value of the goods being sold by Co. A to Co. B (refer to 3.3.1, example 6).

**Supplemental Questions:**

The essence of the original question is that a commercial service was performed by Co. C. to Co. A, no drop shipment certificate could be used in the referenced four party transaction and GST applies.

CRA has provided the rationale for recovery of GST paid by Co. A by using the Section 180 provision. This results in practical business issues and we are requesting confirmation that the following statements apply based on the fact pattern given above:

1. Co. C is required to charge GST to Co. A on the full value of the goods that are deemed to have been supplied, ie., GST on the selling price of the goods sold by Co. A to Co. B, inclusive of the commercial service performed by Co. C to Co. A.

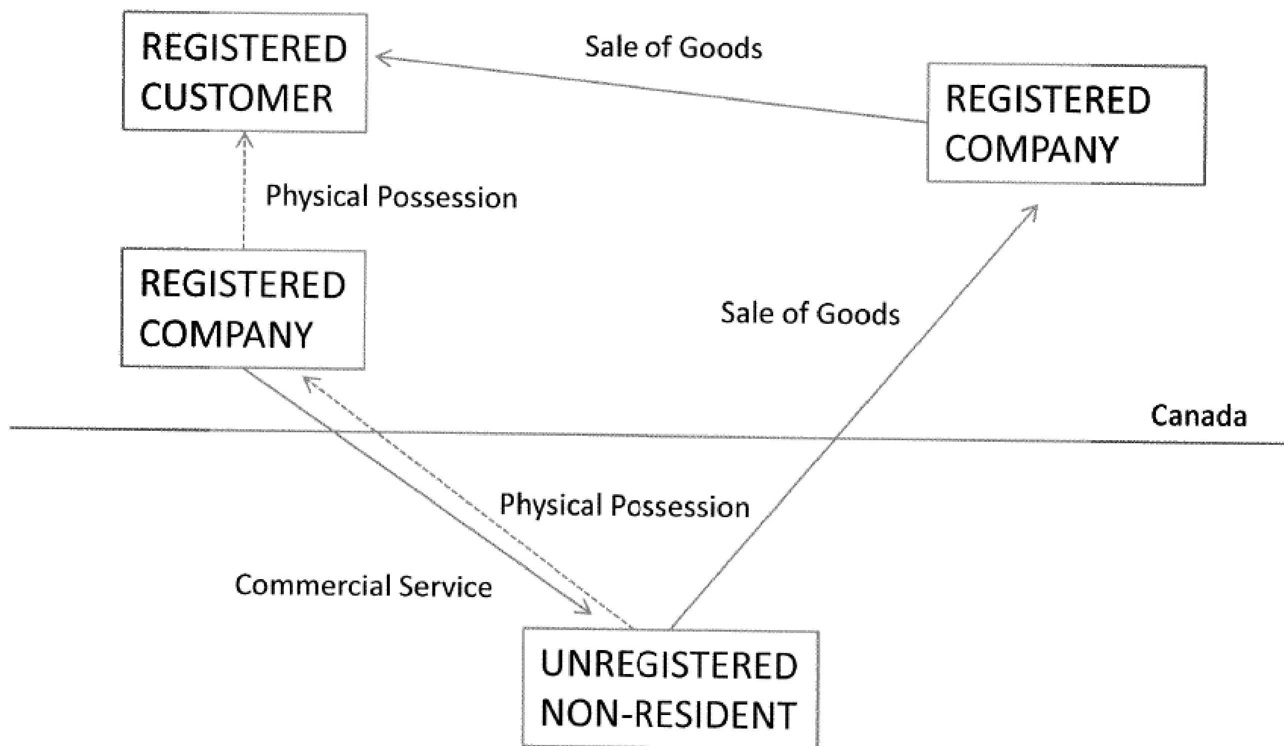
2. Co. A can seek reimbursement of the full GST it paid to Co. C, by invoicing Co. B. and referencing Section 180 [Section 180(b) containing the critical point that Co. A 'has paid tax in respect of a supply of the property deemed under Section 179(1) to have been made by a registrant'].

3. Co. B is entitled to claim a full ITC for the GST amount invoiced.

## ANSWER # 8: Drop Shipment Certificate: Sale by Non-Resident

The CRA agrees that the three statements made by TEI in the Supplemental Question section apply based on the fact pattern given.

## Drop Shipment Example



## QUESTION # 9: Insurance Premium Tax

TEI has been working with CRA on updating the administrative policy with respect to Insurance Premium Tax. The next return is due on April 30 and the industry will require time to implement any changes. Please provide a summary of the proposed changes, including when they will be issued.

## ANSWER # 9: Insurance Premium Tax

Over the past year, concerns have been raised with respect to the requirement for declination letters from insurers to qualify for the exemption from the 10% insurance premium tax. We have met with a number of industry representatives over the past several months to explore alternatives and possible amendments to current policy. These discussions are ongoing but no changes are anticipated by the next filing deadline of April 30, 2010.

## QUESTION # 10: Joint Venture Election

Under the GST system, a joint venture (JV) is different from a partnership because the JV is not included in the definition of a "person" and thus cannot register and account for the GST in its own right.

ETA section 273 provides for a simplified remittance and compliance process for JVs. Under this provision, a joint election can be made by the JV participants to elect one party as the JV "operator," who accounts for the GST collected by the JV and claims the ITCs in relation to the expenses incurred by the JV.

Under the Joint Venture (GST/HST) Regulations, the JV election may generally be made for certain prescribed activities, including activities relating to the construction of real property (including feasibility studies, design work, development activities and the tendering of bids where undertaken in the furtherance of a JV for the construction of real property). In addition, CRA has administratively accepted numerous activities for the JV election, including the maintenance of roads.

One commentator provides —

> In practice, virtually any legitimate joint venture activity would be permitted by CRA, as long as there is no tax loss involved (*i.e.*, the joint venture election is not used to reduce the total GST that would be remitted to the government). Given that the alternative to the election is to have numerous individual participants account for their respective share of the GST and input tax credits separately, the CRA's tolerance in this area is almost a necessity.[2]

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[2] David Sherman, *Analysis: What Is a Joint Venture?,* TAXNETPRO (Carswell, 2002-11-15).

TEI agrees that CRA's flexibility in this area is vitally important.

A. Businesses often perform feasibility studies before major construction projects are launched. For example, some governments may require consortiums to provide such studies before moving forward with major road, bridge, and infrastructure projects. Please confirm that these studies qualify for the JV election.

B. Issues have arisen in respect of JVs that rehabilitate, repair, and maintain bridges. Under CRA's administrative guidelines, the maintenance of roads is a qualifying activity. Please confirm that the rehabilitation, repair, and maintenance of bridges also qualify.

C. ETA section 273(1)(c) provides that, where supplies are made by the JV operator to the JV, they are deemed not to be taxable supplies, provided that certain conditions are met, and thus no GST applies. On the other hand, where supplies are made to the JV by the other JV participants, GST must be collected. Please confirm that this interpretation is correct.

## ANSWER # 10: Joint Venture Election

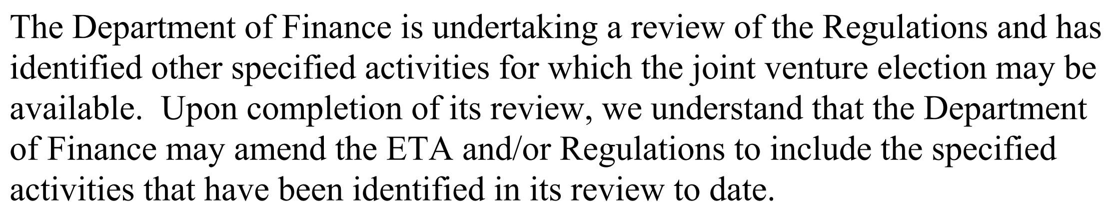
A. Paragraph 3(1)(a) of the *Joint Venture (GST/HST) Regulations* (the Regulations), prescribes the following activity for purpose of the joint venture election in section 273 of the *Excise Tax* Act (ETA):

> "the construction of real property, including feasibility studies, design work, development activities and the tendering of bids, where undertaken in furtherance of a joint venture for the construction of real property".

Thus, a feasibility study is an activity eligible for purposes of the joint venture election, provided it is "undertaken in furtherance of a joint venture for the construction of real property".

B. The CRA cannot confirm the eligibility of an activity for the joint venture election where that activity is not included in section 273 of the ETA or prescribed in the Regulations for purposes of the election.

The responsibility for prescribing activities in the Regulations for purposes of the joint venture election rests with the Department of Finance. Currently, only two activities have been prescribed in the Regulations for purposes of the election.



The Department of Finance is undertaking a review of the Regulations and has identified other specified activities for which the joint venture election may be available. Upon completion of its review, we understand that the Department of Finance may amend the ETA and/or Regulations to include the specified activities that have been identified in its review to date.

One of the specified activities identified by the Department of Finance is the maintenance of roads, except to the extent that the supply of the road maintenance service is an exempt supply and the operator of the joint venture is a public sector body. Consequently, this may be an eligible activity for purposes of the joint venture election once the necessary legislative or regulatory amendment is made. However, the rehabilitation, repair or maintenance of bridges is not one the specified activities identified by the Department of Finance and hence, this activity may not be an eligible activity for purposes of the joint venture election.

As we understand it, the Department of Finance is still reviewing the existing legislative/regulatory approach to determining eligibility of activities for the joint venture election, based on the representations it has received.

C. Where a supply is made by the operator to a co-venturer, the supply is deemed not to be a supply for GST/HST purposes to the extent that the supply is acquired by the co-venturer for consumption, use or supply in the course of commercial activities of the joint venture. As a result, the supply is not subject to tax.

There is no such rule for a supply made by a co-venturer who is not the operator to another co-venturer. Consequently, such a supply is subject to the normal GST/HST rules and would, as a result, be taxable when made by a registrant in the course of the registrant's commercial activities.

## SUPPLEMENTAL QUESTION: Drop Shipments

Goods are sold (title is transferred) by Co. A (registered party in Canada engaged in 100% commercial activity) to Co. B (non-GST registered, non-resident) with terms of delivery FCA Toronto. The intent is for Co. B to export the goods without them being used in Canada prior to export. Co. B requests that the goods be shipped directly to a Canadian public warehouse and stored there for up to one year before export from Canada.

It appears that the answer to the question is stated in CRA Memorandum 3.3.1, in examples 31 and 32, dependent upon whether a drop shipment certificate is issued by the registrant (bailee).

The term 'bailee' is undefined under the Excise Tax Act. Can the term 'bailee' refer to any public warehouse in Canada in the context of its use in Section 179(5) and 179(6)?

Merriam Webster's dictionary (10th Edition) defines **bail** as 'to deliver (personal property) in trust to another for a special purpose and for a limited period'. **Bailee** is defined as 'the person to whom the property is bailed'.

Please confirm that the subject fact pattern results in a supply not subject to the GST when the goods sold by Co. A above, are delivered to a bailee in Canada, for storage purposes prior to being directly exported from Canada.

Please confirm that it does not matter whether Co. A, the bailee, or Co. B arranges for the shipment of the goods from the warehouse in Canada to a location outside Canada.

# ANSWER: Drop Shipments

The CRA confirms that the term « bailee » can refer to any public warehouse in Canada in the context of its use in subsections 179(5) and 179(6) of the ETA.

The CRA agrees that statement 1 and statement 2 apply based on the fact pattern given.