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ELI J. DICKER
Executive Director

W. PATRICK EVANS
Chief Tax Counsel

1 September 2015

Please Respond To:

Lynn Moen
Senior Vice President, Tax
Walton Global Investments Ltd.
2300, 605 - 5th Avenue S.W.
Calgary, AB T2P 3H5
CANADA
(403)750-2278
lmoen@walton.com

Paul Flanagan
Executive Director
British Columbia Ministry of Finance
Tax Policy Branch
P.O. Box 9547 Stn Prov Govt
Victoria, British Columbia V8W9C5
CANADA

Via email: paul.flanagan@gov.bc.ca

Re: Comments and Proposed Budget Changes to British Columbia's PSTA and CTA

Dear Mr. Flanagan:

On April 20, 2015, several members of Tax Executives Institute, Inc.'s ("TEI") Canadian Commodity Tax Committee met with representatives from the British Columbia Ministry of Finance ("the Ministry") Tax Programs Branch. In that meeting, Ministry staff informed TEI that "revenue-related" changes to the *Provincial Sales Tax Act* ("PSTA"), *Motor Fuel Tax Act* ("MFTA"), *Carbon Tax Act* ("CTA"), and their regulations are made during the provincial budget process beginning in September of each year. "Administrative" changes to the PSTA, MFTA, CTA, and their regulations are made throughout the year if required.

This letter contains TEI's revenue-related comments and proposed changes to the PSTA, CTA, and their regulations, and is submitted in conjunction with the Ministry's annual budget process. TEI is concurrently submitting a separate letter to the Ministry's Tax Programs Branch outlining its "administrative" comments and proposed changes to the PSTA (copy attached).

The comments and proposed changes in this letter are not listed in order of importance. Many have been included in previous written correspondence from TEI and discussed with Ministry staff. TEI welcomes the opportunity to meet with Ministry staff to discuss these matters further.

About Tax Executives Institute, Inc.

TEI is the preeminent association of in-house tax professionals worldwide. Our approximately 7,000 members represent more than 2,800 of the leading corporations in North and South America, Europe, and Asia. TEI has over 850 members resident in Canada, which belong to chapters in Vancouver, Calgary, Montreal, and Toronto, and constitute approximately 12 percent of TEI's membership. TEI's Canadian members contend daily with the planning and compliance aspects of Canada's business tax laws. In addition, many of TEI's members resident outside of Canada work for companies with substantial activities in British Columbia and Canada. The comments in this letter reflect the views of TEI as a whole but, more particularly, those of our Canadian constituency.

1. Partnership - Person for PST Purposes

Under the PSTA, a partnership can register as a collector for Provincial Sales Tax ("PST") purposes, but is not treated as a separate legal person for purposes of owning partnership property. Instead, each partner is treated as if it owns a fractional interest in all of the partnership's property. This places responsibility on the partners to collect or pay PST on property owned by the partnership when an interest in the partnership is purchased or sold. In contrast, when shares in a corporation are purchased or sold, there is no requirement to account for PST on property owned by the corporation.

Consistent with the treatment under the *Excise Tax Act*, a partnership should be treated as a "person" for PST purposes, including, among other things, the ability to sell/purchase a partnership interest without triggering a PST expenditure and the ability to use exemptions for transactions within a closely-related group.

Other jurisdictions, such as Ontario (prior to adopting the HST), Saskatchewan, Manitoba and states in the United States of America, treat partnerships as separate persons for sales and use tax purposes.

TEI recommends amending the PSTA and its regulations to treat partnerships as separate persons, using provisions similar to the *Excise Tax Act*.

2. Administrative Materials Delivered from Outside British Columbia

PST Bulletin 313 – Administrative Materials requires businesses with operations in British Columbia and other jurisdictions to self-assess PST on the landed cost of administrative materials (e.g., invoices, investment statements, annual reports, prospectuses, and other written correspondence) mailed to British Columbia-based customers from locations outside the province.

This imposition is problematic for several reasons. Significant effort is required to track the costs incurred to produce and deliver administrative materials into British Columbia. Moreover, double taxation often occurs because the jurisdiction from which the administrative materials are produced and mailed may not provide relief from sales tax on the printing, shipping, and handling fees incurred prior to export. Moreover, the majority of the cost for self-assessment purposes often relates to postage, a cost not subject to PST if the materials had been printed and mailed in British Columbia. PST should be imposed on administrative materials such that taxpayers incur the same sales tax expense regardless of where the materials are produced or mailed. The current rules do not achieve that goal.

Other provinces with a retail sales tax address this inconsistency. For example, Saskatchewan does not require sales tax to be paid on postage if the value of the postage exceeds the value of the goods sent into the province. Manitoba only applies sales tax to statements printed and sent to customers in Manitoba. Statements printed outside of Manitoba and their associated shipment costs are not subject to sales tax even if the statements are mailed to parties in Manitoba.

TEI recommends amending the PSTA and/or its regulations such that PST is payable on a per unit basis equaling the amount of tax payable had the administrative materials been printed and mailed in British Columbia, with a reduction for tax paid in other jurisdictions.

3. PST Exemption for Safety Equipment

To promote the safety of workers in British Columbia, the *PST Exemption and Refund Regulation* provides a PST exemption for safety equipment listed and described in Sections 32 to 35. These rules are complicated because the exemption is limited to listed safety equipment and the exemption for certain items is only available if acquired by an employer, self-employed worker, or educational institution. Finally, the exemption does not cover all

the equipment and consumables required to prevent or mitigate worker or student injuries.

Safety is a top priority for employers, employees, educational institutions, and students throughout British Columbia. The British Columbia Government can support this priority by simplifying and expanding the PST exemption for safety equipment. This action will help prevent injuries, reduce public healthcare costs, and increase productivity.

It is beyond the scope of this letter to list all of the safety-related equipment and consumables subject to PST. However, we offer the following comparisons to assist the Ministry in better understanding the type of safety equipment currently subject to PST, and to illustrate the complexity of these rules:

- First aid kits are exempt but eye wash stations are subject to PST
- Continuous gas detection monitors are exempt but air monitoring equipment for use outside facilities is subject to PST
- Fire retardant clothing is exempt but fire suppression equipment and blankets are subject to PST
- Hardhats are exempt but lamps for miners' hardhats and winter liners are subject to PST
- Respirators and self-contained breathing apparatus are exempt but portable ventilators used for confined spaces are subject to PST
- Welding helmets are exempt but welding curtains and screens are subject to PST

TEI recommends simplifying and expanding the exemption for safety equipment to include all items required to fulfill an employer's (including self-employed persons and educational institutions) obligations to protect workers and students under the *Workers Compensation Act*, British Columbia electrical and building codes, and all other Federal statutes that include safety provisions.

4. Pollution Prevention and Control

Section 99 of the *PST Exemption and Refund Regulation* provides an exemption for machinery and equipment used substantially and directly in the prevention, measurement, treatment, and reduction of pollution. This exemption is only available if the pollutants are attributable to the manufacturing, extraction, or processing of petroleum, natural gas, or minerals. The exemption is further limited to qualifying persons who are manufacturers, oil and gas producers, or mine operators. There is no PST exemption for similar machinery and equipment acquired by other industries or for marine operations, even though they operate with a similar goal: the reduction of pollutants in the environment.

Given British Columbia's concern for the environment and the need for taxpayers to follow government environmental standards, all taxpayers that acquire machinery and equipment to prevent and control pollution should be eligible for the PST exemption on these items. The exemption also should be expanded to include consumables used to clean up pollutants after a spill.

TEI recommends amending the *PST Exemption and Refund Regulations* to allow all taxpayers to purchase pollution prevention control machinery, equipment, and consumables on a PST-exempt basis.

5. Carbon Tax Exemption – Non-Combustion Use of Defined Fuels

Subsection 17(1) of the *Carbon Tax Regulations* provides an exemption for fuel used but not combusted during specified activities. Although this list of qualifying exempt activities may have been a suitable starting point when the carbon tax was enacted on July 1, 2008, the list excludes, and thus subjects to tax, new and innovative uses of fuel not combusted.

Applying the carbon tax to non-combusted fuel is contrary to the overall intent of the CTA. Moreover, limiting the carbon tax exemption to activities listed in the *Carbon Tax Regulations* stifles research and innovation into new uses of fuel.

TEI recommends amending the CTA to eliminate the list of non-combustion activities qualifying for the exemption, and to exempt all fuel not combusted when used in a manufacturing process.

6. Custom Software and Custom Modified Software

Part 4 of the PSTA subjects software to PST unless the software source code has been significantly modified to meet the requirements of a specific person (referred to as "custom modified software") or the software is developed solely to meet the requirements of a specific person (referred to as "custom software"). These rules do not reflect the current state of how software is developed, modified, and licensed. Software solutions are commonly based on one or more existing core applications that are essentially software source code. These core applications are configured, changed, and enhanced to meet a specific customer's requirements. These services do not alter the software source code in the core application(s). The fair market value of the services are typically well in excess of the value of the original core applications.

TEI recommends amending the PSTA and its regulations to update the definition of "custom modified software" to include software comprised of one or more core applications

configured, changed, or enhanced to meet a specific customer's software requirements without altering the original core application.

7. Software Maintenance Agreements

Software maintenance agreements typically encompass service and minor fixes to existing software. Services to software are excluded from the definition of related service and are not subject to PST. In contrast, minor fixes to existing software are treated as a sale of software and are subject to tax under Part 4 of the PSTA.

The bundling rules in Section 26 of the PSTA are intended to ensure that PST will not be imposed on non-taxable software maintenance services. However, it is often difficult to determine which portion of the contract price is attributable to software updates and maintenance services, and the proportions can change from year to year. In addition, software vendors providing maintenance services may be precluded from using the bundling rules if they only provide software maintenance services together with software updates. These issues prevent the bundling rules from producing the desired outcome, which is that PST should not apply to services to software.

TEI recommends amending the PSTA to add a "substantially-all" test to the bundling rules that would exempt software maintenance agreements from PST if less than 10% of the services performed under the agreement relate to minor fixes to software that will be incorporated into a future software update covered by an annual license fee. TEI also recommends amending the PSTA such that the "not ordinarily available for sale" and "not ordinarily provided separate" rules contained in paragraph 26(4)(b) of the PSTA will not apply to software, thus eliminating the competitive advantage for software service providers that do not sell or license software.

8. Reusable Containers – Used in Multiple Jurisdictions

Returnable recyclable packaging containers ("RRPs"), including but not limited to, pallets, reels, barrels, drums, cylinders, skids, and boxes, are used by many businesses for internal shipments and/or shipments to customers. The use of RRP makes excellent commercial and environmental sense: packaging is minimized, costs are reduced, and the product is protected from shipping damage.

RRPs are often filled, loaded, and shipped to other jurisdictions. The location and movement of a particular RRP is typically not tracked due to the substantial administrative cost. Instead, ownership of the RRP is identified using a company logo and/or company name in large print on the RPP so it can be returned to a filling point.

Section 101 of the PSTA imposes PST on the purchase or import of an RRP into British Columbia. There are no provisions in the PSTA that contemplate the use of RRPs in multiple jurisdictions. In contrast, Division 7 of the PSTA includes a series of provisions for multi-jurisdictional vehicles to ensure the PST is only payable based on their use in British Columbia. In order for British Columbia-based businesses with operations and customers in multiple jurisdictions to remain competitive, PST on RRPs should be calculated based on the portion of use in British Columbia, similar to how PST is calculated on multi-jurisdictional vehicles.

TEI recommends amending the PSTA to impose PST upon the proportional use of RRPs in British Columbia. TEI would be pleased to provide access to industry professionals with knowledge and experience to develop a formula to accurately estimate the use of RRPs in British Columbia for this purpose.

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TEI welcomes the opportunity to meet with Ministry staff to discuss these comments and other issues relating to the PSTA, MFTA, and CTA to ensure that the system operates in a practical, effective, and efficient manner for the benefit of the Ministry and the business community.

TEI's comments were prepared under the aegis of TEI's Canadian Commodity Tax Committee, whose chair is Richard Taylor and whose legal staff liaison is Pilar Mata. Should you have questions about our recommendations, please call Mr. Taylor at (416) 935-2568 (or richard.taylor@rci.rogers.com) or Lynn Moen, TEI's Vice President for Canadian Affairs, at (403) 750-2278 (or lmoen@walton.com).

Respectfully submitted,

Tax Executives Institute, Inc.



C.N. Sandy Macfarlane
International President

cc: Lynn Moen, TEI Vice President for Canadian Affairs