Application of GST to Pension Plans and the Financial Services Sector

Canadian - 11/10/2009

November 10, 2009

On September 23, 2009, the Department of Finance released draft legislation, explanatory notes, and a backgrounder concerning several measures aimed at improving and streamlining the application of the goods and services tax (GST) to pension plans and the financial services sector. The proposal includes changes in the following areas:

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

Tax Executives Institute is pleased to submit the following comments on these proposals.

I. Background

Tax Executives Institute is the preeminent association of business tax executives worldwide. The Institute's 7,000 members manage the tax affairs of 3,200 of the leading companies in Canada, the United States, Asia, and Europe and must contend daily with the planning and compliance aspects of Canada's business tax laws. Canadians make up 10 percent of TEI's membership, with our Canadian members belonging to chapters in Calgary, Montreal, Toronto, and Vancouver, which together constitute one of our nine geographic regions. Many of our non-Canadian members (including those in Europe and Asia) work for companies with substantial activities in Canada. TEI's membership encompasses most major industries including manufacturing, distributing, wholesaling, and retailing; real estate; transportation; financial services; telecommunications; and natural resources (including timber and integrated oil companies). TEI concerns itself with issues of tax policy and administration and is dedicated to working with government agencies to reduce the costs and burdens of tax compliance and administration to our common benefit.

II. Pension Expenses

Pension plan entities are generally not entitled to claim ITCs because they are considered to be involved in exempt activities. Certain employer pension plan entities are eligible, however, for a 33-percent rebate of the GST paid on plan-related expenses as a proxy for the percentage of pension-related expenses that would be eligible for ITCs.

The proposed legislation would deem all GST on pension-related expenses incurred by employers to have been paid by the pension plan entity, entitling them to claim a rebate of 33 percent of the GST it has paid or is deemed to have paid. The rebate would be available irrespective of the nature of the plan arrangements or whether the pension plan entity is registered for the GST. Certain restrictions would apply to pension plan entities where 10 percent or more of pension contributions are made by financial institutions (FIs). According to Finance, the 33-percent rate was chosen because it reflects the proportion of pension trust expenses generally eligible for ITCs.

The proposed legislation is intended to limit the effect of a February 22, 2008, decision of the Tax Court of Canada in *General Motors of Canada Ltd. v. The Queen*, which was upheld by the Federal Court of Appeal earlier this year. The court held that General Motors, as employer/sponsor of its employee pension plans, was entitled to claim ITCs on investment management expenses.1 The court rejected Canada Revenue Agency's (CRA) argument that GM was not acting in the course of its commercial activities when acting as administrator of the plans.

Given the judicial determination that the taxpayer's entire ITC amounts are eligible for recovery, the 33-percent rebate in the proposed legislation seems extremely low. When third-party expenses are incurred in administering other employee benefit plans, those expenses are considered reasonable expenses incurred to produce income, and thus deductible for income tax purposes and the ITC is not restricted. The same treatment is warranted here.

III. Deadline for Filing Annual GST Return

The proposed legislation provides welcome relief to FIs that currently file their GST returns on an annual basis. The provision applies to fiscal periods beginning after 2009, and provides a three-month extension to the current filing date. To ensure that the benefits of this change can be realized as quickly as possible, the effective date should be changed to take effect for fiscal years ending after the Announcement Date (September 23, 2009). This would be particularly helpful in the short term because FIs are currently implementing changes necessary to deal with the transition to the HST in Ontario and British Columbia.

Back to top

IV. Form GST111

A. In General. Most large registrants have seen an increase in GST-related compliance burdens. This is in direct contrast to other jurisdictions (notably, in Europe) that recognize that administrative burdens relating to value-added tax (VAT) hinder competitiveness; those countries are taking concrete actions to reduce, rather than increase, VAT compliance burdens.

An example of the increased compliance burden is Form GST111, *Financial Institution GST/HST Annual Information Schedule*. The form often requests information that has been provided to, or is otherwise readily available from, either CRA or another government body (*e.g.*, the Canada Border Services Agency or Office of the Superintendent of Financial Institutions). TEI recommends that companies be asked to supply only information that has not already been reported to the government.

In addition, TEI understands that the General Index of Financial Information (GIFI) is under review to ensure that there is an "owner" for each piece of information requested on the GIFI, as well as a documented need for the requested data. TEI suggests that a similar review be undertaken for Form GST111. We believe the ultimate recommendation will be to eliminate the form.

B. Compliance Burden. Form GST111 requests a significant amount of information that companies do not track for any other purpose, such as the amount of zero-rated financial services (line 61) and supplies other than financial services (lines 70 and 75). Setting up processes to capture this information requires a significant time commitment and related IT costs that may not be warranted by the value of the information. The form requests other data of questionable utility, such as for line 71, which asks for exempt supplies other than financial services. Equally important, even large companies with tax departments will have difficulty obtaining the requested data, and the task is likely even more onerous for small- to medium-sized businesses.

Moreover, companies completing Form GST111 have difficulty understanding whether they should tie the amounts reported back to their financial statements, the annual GST return, or to figures provided to Finance via other government entities. There are many differences among the accounting, income tax, and GST treatments of certain supplies, making it difficult to perform reconciliations between the form and other reporting requirements. Clarification of this issue is needed.

C. Penalties. The proposed legislation would add a new section to the ETA, imposing penalties for failure to report or misstatements of amounts required to be reported on Form GST111:

> 284.1 (1) In addition to any other penalty under this Part, every reporting institution that fails to report an actual amount (other than an actual amount for which the reporting institution is allowed to provide a reasonable estimate pursuant to subsection 273.2(5)) when and as required . . ., or that misstates such an actual amount in the information return, and that does not exercise due diligence in attempting to report the actual amount is liable to a penalty, for each such failure or misstatement, equal to the lesser of $1,000 and 1% of the absolute value of the difference between the actual amount and

(a) if the reporting institution failed to report the actual amount when and as required, zero; or

(b) if the reporting institution misstated the actual amount, the amount reported by the reporting institution in the information return.

The penalty provisions would be phased-in and the Minister of National Revenue would be given discretion in their application.

The penalty imposed under this section is excessive, especially when compared with penalties imposed for failure to answer a demand ($250 for each occurrence) or failure to provide information when required ($100 for each failure).2 TEI recommends that the penalty be lowered to $100 per return. In addition, the proposed legislation seems contrary to previous assurances that the use of estimates is unavoidable and filers using their best efforts to complete the return would not be penalized. Finally, Finance should clarify that the penalty applies on a per-return rather than a per-line item basis.

V. Imported Taxable Supplies

Because the GST applies to imports of goods and services, the ETA requires certain recipients of imported services and intangible property to self-assess the tax. The draft legislation permits FIs resident in Canada conducting business through foreign branches to elect to use a simpler approach to self-assess. The election would permit those FIs to self-assess on the charges of their foreign branches if that charge is generally an amount treated, for income tax purposes, both as income or profit in a particular country other than Canada and as a deduction from income in Canada. Eligible FIs (*i.e.*, FIs resident in Canada) may elect to use this method retroactively for periods back to the proposed 2005 effective date.

Back to top ↑

Please confirm that taxpayers electing to use their intercompany reporting schedules developed for income tax purposes (T106 and T1134) will be allowed to make this election for both branches and other related legal entities.

The definition of "permitted deduction" in proposed section 217 does not include all items defined as a financial service in ETA section 123(1). The definition should be expanded to include all items covered in that section to ensure that tax is not required to be self-assessed on financial services under the imported supply rules.

VI. Conclusion

Tax Executives Institute appreciates the opportunity to comment on this matter. TEI would be pleased to meet with you or members of your Ministry to discuss the issues more fully. If you should have any questions about TEI's letter, please contact TEI's Vice President for Canadian Affairs, Sherrie Ann Pollock, at 416.955.7373 (sherrieann.pollock@rbcdexia.com). Alternatively, questions may be directed to Diana M. Spagnuolo, Chair of TEI's Canadian Commodity Tax Committee, at 403.237.2948 (diana.m.spagnuolo@esso.ca).

TAX EXECUTIVES INSTITUTE, INC.

Neil D. Traubenberg
International President

* * *

1 2008 TCC 117 (2008), *gov't appeal dismissed*, April 16, 2009. *See also Canadian Medical Protective Ass'n v. The Queen*, 2008 TTC 33 (2008), *aff'd*, 2009 F.C.A. 115 (April 16, 2009) (investment management services are GST-exempt services).

2 ETA §§ 283 & 284.

- Less Taxing Matters
- TEI Canada

Privacy Statement

Back to top ↑