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Attention: Jordan Goss
c/o Tax Policy Branch

Via email: Jordan.Goss@gov.bc.ca

Re: PST Reporting and Compliance

Dear Ms. Goss:

The transition back to the Provincial Sales Tax continues to challenge businesses with operations in British Columbia. Many areas of the law still need additional guidance and clarification. This letter comments on various provisions in the *Provincial Sales Tax Act* (PSTA), the Regulations, and the administrative guides issued by the Ministry of Finance (hereinafter the Ministry). Addressing the issues identified by members of Tax Executives Institute (TEI) will improve the administrability of the provincial sales tax (PST) system. We have limited our focus to issues that are administrative in nature, which should have little or no impact on provincial revenue. TEI also welcomes the opportunity to meet with Ministry staff to discuss these matters further.

TEI is the preeminent association of in-house tax professionals worldwide. The Institute's approximately 7,000 professionals manage the tax affairs of over 3,000 of the leading companies across all industry sectors in North America, Europe, and Asia. Canadians constitute approximately fifteen percent of TEI's membership, with our Canadian members belonging to chapters in Vancouver, Calgary, Montreal, and Toronto (which is TEI's largest chapter). These TEI members contend daily with the planning and compliance aspects of Canada's business tax laws. Many of our non-Canadian members work for companies with substantial activities in British Columbia and Canada generally. The comments set forth in this letter reflect the views of the Institute as a whole, but more particularly those of our Canadian constituency.

1. Assessments for Invalid PST Exemption / Exception Requests

The PSTA generally places the responsibility to collect PST on the vendor. In cases where the purchaser provides a PST registration number, declaration form, exemption certificate, or proof of status as a farmer, Indian, agency of the Federal Government, or some other exempt person, the vendor is not required to collect the PST. The PSTA and the Regulations identify the documentation or records that must be kept on file by the vendor to support the non-collection of PST. There is no requirement to verify the PST number or validate the declaration on the exemption certificate or its equivalent.

Under subsection 203(1.1) of the PSTA, an assessment may be imposed on a vendor if the director determines the vendor “*had reason to believe*” the purchaser does not qualify for an exemption or exception. The Ministry has provided no guidance on what duties this provision places on vendors to verify the use of an exemption or exception from the PST. This uncertainty creates significant risk for, and places undue administrative burdens on, vendors, who are often not familiar with the purchaser’s business operations, legal status, or how the purchaser intends to use the property or services. Even the on-line enquiry tool provided by the Ministry to validate PST numbers does not include any assistance for determining whether the vendor is claiming an exemption or exception.

Alternatively, the PSTA allows vendors to charge PST at the time of sale, and later refund the PST if the purchaser provides the correct documentation. This pay and refund process only works when the purchaser voluntarily produces the documentation or PST number at a later date after the tax is paid. The resulting delay between payment and ultimate refund of the PST causes many purchasers to acquire the property or services from a vendor that does not require payment of the PST at the time of purchase. This approach favors those vendors willing to take on more risk related to their PST obligations. The requirement to validate PST numbers and/or exemption certificates unnecessarily burdens vendors already tasked with collecting the PST and creates significant uncertainty about the scope of a vendor’s due diligence obligations.

Vendors would benefit from guidance on what factors the director will use to determine when a vendor has “reason to believe” a purchaser was not eligible for an exemption or exception from PST. Additional certainty can be achieved by amending subsection 203(1.1) of the PSTA to provide that an assessment will only be issued against the vendor if there is no ability to assess the purchaser and there is evidence of bad faith by the vendor.

2. Products and Services that are Nontaxable or Exempt

Vendors often erroneously charge PST on sales of property or services that are not taxable, such as intangible personal property, intellectual property, professional services (other than legal services), real property rentals, etc. When this occurs, the purchaser must often prepare a lengthy technical explanation to persuade the vendor to refund the PST or adjust its invoice. In other words, the purchaser must prove a negative. In contrast, when a vendor charges PST on an

exempt property or service, it is a fairly straightforward task for the purchaser to cite a particular provision in the PSTA or Regulations to prove the tax need not be collected on the sale.

To assist the general public (both consumers and businesses) with the phase-out of the Harmonized Sales Tax (HST) and re-introduction of the PST, the Ministry prepared a document titled: *What's Taxable under the PST and What's Not*. This document was updated several times, most recently in April 2013. While TEI applauds the Ministry's efforts to assist businesses and consumers in identifying transactions where no tax is due, the guidance lacks an explanation of why items are classified as "No PST." Exempt and excepted items are both classified the same way, and many non-taxable items are not listed. As a result, when disputes arise between vendors and purchasers this document has little value. Further, the process of issuing PST refunds is complicated, which increases the compliance burden for businesses. For example, vendors may not refund PST on issued, but unpaid, invoices through the issuance of a credit note, even if the purchaser demonstrates that a particular property or service is not subject to PST.

Purchasers and vendors would benefit from a comprehensive document that explains why PST is *not* applicable to a particular property or service. TEI urges the Ministry to create an on-line tool, with search capabilities, that lists property and services that are exempt or not taxable. Using an online format would simplify the process of updating the list when new tax-free items are identified, or the tax base is changed.

3. Due Date for Returns Filed Using Fiscal Periods

Under subsection 238(1) of the *Excise Tax Act*, the due date for GST/HST returns filed using fiscal periods is one month after the end of the reporting period. In contrast, under paragraph 72(1)(b) of the Regulation, the due date for PST returns filed using fiscal periods is "*30 days after the last day of the collector's reporting period.*"

Taxpayers who adopt fiscal periods usually do so to simplify their financial reporting and tax compliance. Having different rules in the two sales tax statutes means the same due date for sales tax returns only occurs four times each year when a month has 30-days. This results in scheduling challenges and, on occasion, late remitted PST.

TEI urges the Ministry to amend the Regulations to make the due date for PST returns the same as the due date for GST/HST returns (*i.e.*, one month after the end of the reporting period).

4. Delayed PST Rulings

During the transition back to the PST, there were occasionally significant delays in the issuance of rulings clarifying the application of PST to particular products or services that had not been addressed in a PST Bulletin. As a result, some vendors may not have collected the proper amount of PST. On commercial transactions where the vendor issues an invoice, there is a record of the purchaser, and there is an opportunity for the vendor to bill and collect the PST retroactively. In contrast, given the nature of retail transactions, it is often impossible to recover the PST after the sale has taken place. TEI requests that the Ministry provide administrative

leniency to vendors who are exposed to an assessment for non-collection of PST on retail transactions prior to the date guidance is released on an issue.

5. Optional Service Contracts with No Scheduled Services

Optional service contracts with no scheduled services were not part of the tax base under the former Social Service Tax (SST) because they fell outside the definition of a taxable service. To assist taxpayers, the Ministry's position on these contracts was set out in former Consumer Taxation Branch (CTB) Bulletin 018 and in several references in the Tax Interpretation Manual (TIM).

Regrettably, the definition of a "related service" in section 1 of the PSTA is broad and may capture optional service contracts where there is no scheduled maintenance. To stay within the Ministry's commitment to having the PST apply to property and services in the same manner as the SST, the tax-free status for these services should be confirmed.

Recently, PST Bulletin 105 – *Software*, was significantly revised and re-issued. It includes a paragraph confirming that optional service contracts covering hardware and software are not taxable where services are provided on an "as needed" basis. We understand a similar explanation will be provided in the yet-to-be released PST Bulletin 303 – *Warranties, Service Contracts and Maintenance Agreements*.

Given the complexity of the agreements under which these types of services are provided, TEI anticipates disputes will arise between PST auditors and taxpayers, leading to assessments that will be litigated. To defend a position in the courts, taxpayers are generally required to cite provisions from a tax statute. Rather than using administrative guides to explain the PST treatment of optional service contracts with no scheduled services, the Ministry and taxpayers would be better served by adding to the Regulations a new PST exemption specifically for these services.

6. Administrative Materials¹ Delivered from Outside British Columbia ("BC")

Under the SST, businesses with operations in BC and other jurisdictions were required to self-assess tax on the value of administrative materials (*e.g.*, invoices, investment statements, annual reports, prospectus, and other written correspondence) mailed to BC-based customers from a location outside BC. Based on the comment in PST Bulletin 109, and yet-to-be released PST Bulletin 313, we understand the Ministry intends to apply the PST in the same manner as the SST. This will create significant administrative burdens and double taxation risk for businesses with operations in BC.

¹ For the purposes of this letter, administrative materials *do not* include promotional materials as defined in the PSTA.

In addition to the effort required to track the delivery of administrative materials into BC, there is often double taxation on administrative materials because there is no relief of the sales tax paid on the printing, shipping, and handling fees in the jurisdiction where the materials are produced and from which they are mailed. Moreover, the majority of the landed cost for self-assessment purposes relates to postage, which would otherwise not attract PST if the materials were printed and mailed in BC.

The PSTA already includes the following provisions that appear to eliminate the requirement to self-assess PST on the majority of administrative materials imported into BC:

Bundling Rules - Administrative materials that qualify as a “*taxable component*” and are mailed to a BC-based customer as part of a property or service that is a “*non-taxable component*” should qualify for an exemption under the bundling rules in sections 26 and 137 of the PSTA.

Purchase for Resale - Administrative materials that relate to taxable property are essentially imported for resale rendering them exempt from PST as material included in the amount paid for the taxable property.

More broadly, to eliminate double taxation on these transactions and to achieve consistency with their treatment under the former SST, TEI urges the Ministry to reconsider its position on the requirement to self-assess PST on administrative materials that are delivered from outside BC where the importer has already paid tax on the printing and handling fees in another jurisdiction. The above provisions that already exist in the PSTA support this position.

7. Ongoing Vendor Training

In advance of the transition back to the PST, the Ministry conducted a number of training sessions to familiarize businesses with the PST. Those “PST Road Shows” provided valuable assistance that made the transition process easier for many stakeholders. Still, TEI members and their staffs must often explain to their customers why a particular product or service is, or is not, subject to PST. This responsibility places an additional burden on large businesses and results in potential risk where the vendor misapplies the explanation (*e.g.*, by incorrectly granting a PST exemption). To better understand what training will be available to vendors in the future, we invite a discussion of the Ministry’s overall strategy for small business vendors.

8. Delays in Issuing PST Bulletins

The Ministry has not yet issued PST Bulletins for certain products and services. In the absence of these Bulletins, businesses may be required to rely on CTB Bulletins issued under the SST and/or information set out in the TIM. In the unlikely event that a newly issued PST Bulletin provides a different tax treatment from a former CTB Bulletin, TEI recommends that the Ministry permit vendors to revise the tax treatment on a prospective basis only.

9. MFT / PST on Natural Gas

The application of either the motor fuel tax (MFT) or PST to natural gas depends on how the natural gas is used. MFT is payable on natural gas used in a stationary internal combustion engine, while PST is payable on other uses (unless an exemption is available). MFT on natural gas must be remitted on a return that is due by the 15th of each month. The settlements for natural gas, however, are not issued until the 20th of each month. This disparity often results in under-remitted MFT because the seller/importer of natural gas does not know the actual amount of natural gas used in an internal combustion engine when the MFT return is filed. There is no problem with the timing of the PST remittance for natural gas used for other purposes because the PST return is not due until 10 days after the settlements are issued.

The Ministry could simplify compliance with the MFT by changing the filing/remittance date for MFT returns for natural gas to the end of the month so the due dates for MFT and PST returns are aligned.

10. PST Refunds by Vendors

TEI appreciates the improvements the Ministry made to the PST refund provisions over those used under the SST. For example, sections 146 and 147 of the PSTA permit vendors to refund tax paid on certain transactions when the purchaser subsequently informs the vendor it did not have a legal obligation to pay the tax or produces documentation showing it was entitled to an exemption from the tax. Both provisions require the purchaser to make the claim for refund from the seller “*within 180 days of the date the amount was paid.*” Uncertainties remain, however, as to when the tax “was paid” for purposes of starting this 180-day period.

In many retail transactions, the tax is billed and paid at the time of sale using a cash register. Conversely, in non-retail transactions, PST is charged on an invoice that is sent to the purchaser, and the invoice is paid on an undetermined date in the future. While the vendor is required to add the tax to its PST return for the period in which the invoice was issued, the purchaser generally does not pay the tax until it pays the invoice. In cases where a purchaser subsequently provides the vendor with an exemption certificate/declaration or PST number after the invoice is issued, the purchaser typically demands the 180-day rule be applied beginning with the date it paid the tax rather than the invoice date.

As explained above, this refund issue is further complicated by the requirement that the vendor is prohibited from refunding the PST if it has not yet been paid. This prevents a vendor from issuing a credit note and then issuing a revised invoice if the purchaser provides documentation before it pays the invoice on which PST was charged.

To clarify this issue, TEI recommends that the Ministry confirm the date the purchaser pays the invoice (including the PST) is the date that begins the 180-day limit on vendor refunds in sections 146 and 147 of the PSTA. Further, we urge the Ministry to add a provision to the PSTA allowing vendors to amend their invoices or issue credit notes to essentially refund PST when an invoice is issued by the vendor but not yet paid by the purchaser and the purchaser

provides documentation to support an exemption or otherwise demonstrates the transaction should not be subject to the tax.

11. PST Self-Assessed When No Legal Obligation to Pay

Under the PSTA, businesses must self-assess PST on imported items on the date the item is imported into BC. Most businesses, however, wait for an invoice from the seller confirming that no PST was paid to the vendor before self-assessing and remitting tax. This process also allows the invoice and the self-assessment to be set up in the general ledger, creating an audit trail between the import and the PST return. Also, in certain cases a business will determine that an exemption is available after a self-assessment has been remitted.

While the self-assessment process generally works well, a person may self-assess PST in one reporting period and, in a subsequent reporting period, determine that the self-assessment was not required.

When that occurs, the PSTA does not appear to provide a mechanism for obtaining a refund of the erroneously self-assessed and paid tax. Section 146 of the PSTA allows a refund of PST by a vendor where there was no legal obligation to pay the tax. However, this section does not appear to contemplate a refund in the case of a self-assessment (*i.e.*, where the person who paid the tax and the collector are the same person). Section 152 of the PSTA also allows for a refund of PST to be paid by the director, but only in two very specific cases neither of which directly apply to self-assessments.

While section 146 and 152 could be interpreted as applying to refunds of self-assessed PST, TEI urges the Ministry to confirm that treatment to eliminate confusion and potential instances of double taxation. Businesses would also welcome confirmation that the interest offset provisions of section 206 apply in situations of self-assessed PST and that the ten percent penalty provision of subsection 205(c) does not apply.

12. Inspection Services

Subsection 77(1)(h) of the PST Exemption and Refund Regulation provides what appears to be a fairly broad exemption for “diagnostic services, testing or safety inspections,” relating to tangible personal property. Limiting this exemption solely to “*safety*” inspections seems overly restrictive, especially since diagnostic services require no safety component to qualify.

Diagnostic services typically refer to services performed to identify a problem. For example, if a machine were vibrating unexpectedly, a diagnostic service would identify whether a shaft is out-of-balance or a worn bearing is causing the vibration. In contrast, an inspection service means a service performed to ensure that a certain level of service, fitness to purpose, or quality is met. For example, a company is hired to inspect the assembly of machinery or an apparatus before it is installed. Often a different service provider is used for inspections and diagnostic services with the latter brought in only when a problem has already been identified.

There appears to be no policy rationale for limiting the PST exemption to safety inspections. TEI recommends that the Ministry amend subsection 77(1)(h) of the PST Exemption and Refund Regulation to include all inspection services relating to tangible personal property.

13. Estimated Assessment Amounts

Under subsection 203(1.1) of the PSTA, the director is authorized to calculate an assessment for the non-collection of tax “*in a manner and by a procedure the director considers adequate and expedient*” and then to impose a penalty equal to the amount calculated. The penalty is essentially an estimate of the PST not collected and remitted. Subsection 203(3) of the PSTA prohibits the director from imposing the penalty for periods that begin four years before the assessment date. Subsection 203(2) of the PSTA states that when the penalty is paid it “*satisfies to the extent of the payment the original liability of the person who is required to pay the tax.*” There are similar provisions for estimating assessments related to tax collected but not remitted and for failing to self-assess PST.

The ability to issue an assessment based on an estimate may be administratively expedient, but it also leaves the assessed person at a significant disadvantage. In particular, for retail transactions the assessed person cannot recover the PST from the customer because these are often low-dollar transactions or transactions for which customer information is not collected (*e.g.*, cash transactions). While it may be possible to recover the PST on commercial/wholesale transactions, the PSTA provides very little support to recover the PST other than the right to sue a customer for non-payment when an invoice is issued after-the-fact.

To prevent abuses when estimates are used for assessments, the following features should be included in the guidelines provided to PST auditors:

1. For retail transactions, if a vendor has access to actual sales data for a particular product or service, this sales data must be used to estimate the assessment.
2. If a particular property or service has been available for a period that is less than three years, the estimate should be reduced accordingly.
3. If it is determined that a particular customer who acquired the property or service is not required to pay PST for any reason, the estimate should be reduced accordingly.
4. A reasonable sample of the population of transactions must be taken to calculate the estimate.
5. Gross revenues should not be used to estimate the non-payment of PST on imported property.

TEI would be pleased to work with the Ministry in reviewing and commenting on the rules and formulas to be used by PST auditors for estimating an amount for PST assessment purposes.

14. Exports – Customer Ships Property Using Own Conveyance

Many BC-based businesses sell property to non-resident customers who use their own conveyances to pick up products in Canada for export. Typically, these non-resident customers are not registered for the PST because they do not operate within the province. BC vendors are required to charge PST on these sales even though they are essentially an export. The non-resident customer may claim a refund of this PST directly with the Ministry. For GST purposes, the sale of goods in Canada to a non-resident customer for export is eligible for zero-rating, provided the vendor retains suitable documentation to verify the entire shipment can be traced from its origin in Canada to a destination outside of Canada.

Allowing zero-rating for export sales where the customer uses its own conveyance eliminates the GST refund claim process and thereby reduces the administrative burden on foreign customers as well as the Canada Revenue Agency. The retention of export and shipping documentation by the Canadian-based vendor to verify that the goods were exported is not a significant burden when compared with the benefit of maintaining a competitive position with non-resident vendors.

TEI urges the Ministry to amend the Regulations in a manner consistent with the GST treatment of commercial sales of tangible personal property to a non-resident customer for export using the customer's own conveyance.

15. Recording of a Customer's PST Number

Many businesses use either commercial software, large enterprise resource planning systems or custom software to process customer billings. BC is one of only a few jurisdictions still requiring vendors to record the customer's PST number on a bill, invoice, and receipt to support non-collection of PST. This unique requirement forces businesses to make costly modifications to these complex systems, and this customized functionality is often missed on software updates or new installations. At the same time, businesses are required to maintain other documentation supporting claims that sales are exempt (*e.g.*, exemption certificates).

We urge the Ministry to join the majority of jurisdictions and eliminate the requirement for vendors to record a customer's PST number on a bill, invoice, and receipt and to rely instead on the documentation/information vendors are required to maintain on file, such as exemption certificates, declarations, or PST numbers on purchase orders.

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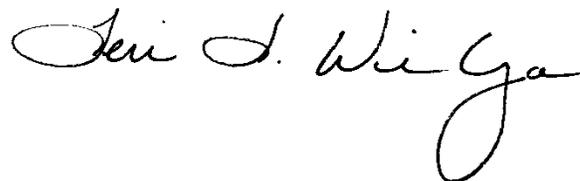
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TEI welcomes the opportunity to meet with Ministry representatives to discuss these comments and other issues relating to the administration of the PST to ensure that the system operates in the most practical, effective, and efficient manner to the benefit of both the Ministry and the business community.

TEI's comments were prepared under the aegis of the Institute's Canadian Commodity Tax Committee, whose chair is Robert Smith. Should you have any questions about our recommendations, please do not hesitate to call Mr. Smith at 514.832.8198 (or Robert.Smith@mckesson.ca) or Shiraz Nazerali, TEI's Vice President for Canadian Affairs, at 403.213.8125 (or shiraz.nazerali@dvn.com).

Respectfully submitted,



Tax Executives Institute

Terilea J. Wielenga
International President

cc: Shiraz Nazerali, TEI Vice President for Canadian Affairs
Robert Smith, Chair of TEI's Canadian Commodity Tax Committee