TAX EXECUTIVES INSTITUTE, INC.

EXCISE TAX QUESTIONS

Submitted to

CANADA REVENUE AGENCY
and
THE DEPARTMENT OF FINANCE

NOVEMBER 18-19, 2014

Tax Executives Institute, Inc. welcomes the opportunity to present the following questions on Canadian commodity tax issues, which will be discussed with representatives of Canada Revenue Agency and the Department of Finance during TEI's November 18-19, 2014, liaison meetings. If you have any questions about the agenda, please do not hesitate to call Paul T. Magrath, TEI's Vice President for Canadian Affairs, at 905.804.4930 or Paul.Magrath@astrazeneca.com, or Richard Taylor, Chair of TEI's Canadian Commodity Tax Committee, at 416.935.2568 or richard.taylor@rogers.ca.[1]

TECHNICAL QUESTIONS

1. Phasing Out of Recaptured Input Tax Credits

As a temporary measure beginning July 1, 2010, and effective through June 30, 2018, large businesses must recapture input tax credits for the provincial portion of the HST paid or payable on "specified property and services" in Ontario (commonly referred to as "recaptured input tax credits" or "RITCs"). For the first five years, the rate of recapture was 100-percent. Beginning July 1, 2015, the rate of recapture will decrease by 25-percent per year until reaching 0-percent for all supplies made on or after July 1, 2018. (Similar rules came into force in Prince Edward Island on April 1, 2013, where the phase out will begin on April 1, 2018 and end on March 31, 2021.)

Large businesses devoted considerable resources modifying their systems to properly account for these RITCs. For example, several companies engaged specialty

[1] Unless otherwise noted, topics are for discussion at the meetings with both CRA and the Department of Finance. Questions for CRA requesting a written response are noted.

consulting firms or devoted significant internal resources to acquire the information technology support necessary to identify and report supplies of hydro and electrical purchases consumed in manufacturing and research processes. Even with systems improvements the process for identifying, tracking, and reporting RITCs involves intensive analytical work and requires substantial manual intervention.

With the phase out of RITCs in Ontario scheduled to begin July 1, 2015, businesses must start planning for the requisite changes to their IT systems. Please provide an update on the timetable for releasing guidance, including transitional rules, on how the phase out will be reported on GST/HST returns and those issues with the phase out causing concern.

2. Project to Update GST/HST Bulletins, Publications, and Forms
(CRA Only)

Changes in the law and the economy necessitate constant revisions to published guidance. For example, CRA's website notes that several forms and publications related to selected listed financial institutions are currently being developed (http://www.cra-arc.gc.ca/tx/bsnss/tpcs/gst-tps/frmspbs/clntgrp-eng.html). Outdated guidance creates uncertainty for businesses attempting to apply those rules and can result in disputes between business and CRA. We invite a discussion of the process CRA uses for identifying which publications are out of date and how it prioritizes the revision of those documents.

3. Rules for Recovery of GST/HST on Out-of-Pocket Costs
(CRA Only)

Service firms, consultants, and other GST/HST registrants routinely charge their clients for out-of-pocket costs they incur in the course of performing their work. Those expenses commonly include travel and related costs for food and beverages (and occasionally, entertainment).[2] Misapplication of the GST/HST rules to those charges complicates compliance by businesses invoiced for out-of-pocket expenses by their service providers.

Some suppliers mistakenly include GST/HST charged on out-of-pocket expenses in the amounts that are passed through to their clients. Those charges should be invoiced to clients ex-original GST/HST and treated as additional consideration for the underlying service (also taking on the same GST/HST status). Further complications arise when suppliers and/or their clients misapply income tax and GST/HST rules for meals and entertainment costs. When a client is aware its supplier has not correctly handled the GST/HST aspects of the supplier's disbursements charges, the client must spend time bringing the error to the attention of a supplier and explaining why the invoice is incorrect. Because this occurs frequently, it creates an inefficient system often involving cancellation and re-issuance of invoices.

[2] Please note that in the majority of cases there is no agency relationship between the supplier and its client.

Although CRA has published guidance concerning lawyers' disbursements, there is no single publication that explains the GST/HST rules for a non-law firm's recovery of out-of-pocket costs, including those that are non-taxable when initially incurred such as costs incurred outside Canada. Clear direction on this topic, including examples, would help reduce the frequency of GST/HST errors on re-billable disbursements. TEI would be willing to work with CRA on guidance applicable to this issue.

Is CRA willing to create written guidance that provides comprehensive and easy-to-understand guidance on the administration of the GST/HST aspects of re-billable out-of-pocket costs?

4. Filing GST/HST Returns in Functional Currency
(Finance Only)

Corporations resident in Canada may elect to file their Canadian income tax returns using their functional currency (*e.g.*, a Canadian corporation can file its income tax return in U.S. dollars). This election is helpful for corporations transacting primarily with non-resident customers. The *Excise Tax Act* (ETA), however, does not have a similar provision. All businesses must file their GST/HST returns in Canadian dollars.

Is Finance considering any amendments to the ETA to provide an election for Canadian businesses to file their GST/HST returns using functional currency rules similar to those applicable to the corporate income tax? Would Finance consider development of such rules in the event a simplified registration system is established for foreign suppliers of electronically delivered goods and services?

5. Continuing Refinements to My Business Account
(CRA Only)

TEI is appreciative of the continuing refinements that CRA is making to My Business Account. The use of this online tool has streamlined a number of administrative tasks and provided a single location where businesses can access important information about their tax status.

a. *Future improvements.* Can the CRA My Business Account team discuss improvements that will be included in the next release of My Business Account?

b. *Authorized representative status.* Has a date been set for expanding authorized representative status (RepID) to an individual such as a non-resident who does not file a T1 Income Tax Return?

c. *Cooperation with Revenu Québec.* Can the CRA My Business Account team provide an update on their work with their counterparts at Revenu Québec? Specifically, it would be helpful to understand efforts to enable companies whose GST/HST is administered by Revenu Québec to access their GST/HST account

information electronically so these companies can share the same efficiencies in administering their GST/HST accounts as all other companies in Canada.

6. Financial Services

a. *Arranging for Financial Services*. Defined financial services are treated as exempt supplies under the ETA. Paragraph (l) of the definition of financial services in section 123 of the ETA includes arranging for financial services. The legislation provides no additional guidance on what activities constitute "arranging for" financial services. The courts have applied varying interpretations of this language. For example, the Tax Court of Canada found in *Global Cash Access (Canada) Inc. v. The Queen*, 2012 TCC 173, that "[t]he term 'arrange for' in this context has been broadly interpreted as 'plan or provide for; cause to occur.'" On appeal, the Federal Court of Appeal determined that paragraph (l) of the ETA did not apply in the case.

Given the lack of consistency from the courts on this point, we invite a discussion on the following items:

(i) Could CRA discuss the types of common interpretive errors they see taxpayers making when determining whether a service can be treated as "arranging for" a financial service?

(ii) Could CRA discuss the criteria (or weighting of criteria) used to determine when a service will be treated as arranging for a financial service?

(iii) Could CRA and Finance discuss whether any changes are being considered to address the outcome of the *Global Cash Access* decision and other similar cases (*e.g.*, legislative amendments, published guidance, etc.)?

b. *Financial Institution GST/HST Annual Information Returns*.

(i) Could CRA and Finance discuss any changes that are being considered for the Financial Institution GST/HST Annual Information Returns?

(ii) Would CRA/Finance consider setting up a working group with industry participants to discuss possible changes to the return that would both improve the information being provided on the return and help simplify the current reporting requirements?

(iii) Would CRA/Finance consider eliminating the obligation to file the Financial Institution GST/HST Annual Information Returns for persons qualified as financial institutions under the *de minimis* rule of paragraph 149(1)(c), when the principal activities of such persons are to make taxable supplies and the reason they qualify as financial institutions under

the *de minimis* rule of paragraph 149(1)(c) in a given year is due to the receipt of interest on cash flow required for their commercial activities?

c. *Imported Taxable Supply Rules for Financial Services*.

(i). Could CRA and Finance discuss any changes they are considering to the imported supply rules of sections 217 and 218 of the ETA? For example, are any changes being considered in relation to loading, or will any further guidance be released on this concept?

(ii). Retroactive Legislation on Reinsurance Premiums from 2010 Federal Budget (CRA only). The 2010 Federal Budget tabled complex retroactive legislation that affected the insurance industry, specifically reinsurance premiums. This legislation affects all Canadian insurance companies and all large corporations that have captive insurance companies. CRA has advised on numerous occasions that clarification on their position with respect to this legislation will be coming soon. At the annual TEI Canadian Tax Conference in May of this year, "soon" was defined to "hopefully, mean less than 3 months."

There is significant uncertainty in the market in respect of the definition of "expense loading" and other issues related to this legislation. Even professional advisory firms have taken slightly different positions. Until CRA clarifies its position the market for reinsurance will continue to be fraught with uncertainty.

When will CRA clarify it position on this legislation?

d. *Pension Plans (Finance Only)*.

(i) Are any changes being considered around master trusts?

(ii) Would Finance consider adding an election to allow a pension plan to be recognized as the recipient of services where the services were contracted for by the employer as administrator for the operation of the pension plan and paid for by the pension plan so long as no input tax credits were taken by the employer?

(iii) Taxpayers have welcomed the introduction of an election to not account for GST/HST on actual supplies to a pension plan. However, the rules and administration for selected listed financial institutions (SLFIs) remain complex and administratively burdensome. Has CRA or Finance analyzed the SLFI regime for ways it can be simplified?

TEI is willing to participate in that process, and could provide examples that would inform the discussion.

e. *Status of Internal Review of Financial Services (Finance Only)*. Could Finance provide an update on the status of the financial services review?

7. Threshold Amounts and Procurement Cards
(Finance Only)

a. *Indexing Threshold Amounts for Inflation.* Since the introduction of the GST in Canada, the Consumers Price Index has increased by approximately 55-percent. Many threshold amounts in the ETA have never been adjusted to reflect the effects of inflation. Those amounts include the *de minimis* financial institution rules in paragraphs 149(1)(b) and 149(1)(c), the small supplier rules in section 148, and the documentation requirements of the Input Tax Credit Information (GST/HST) Regulations. Does Finance have any plans to review these and other threshold amounts in the ETA and its regulations that have never been adjusted to reflect inflation?

b. *Procurement Cards.* TEI's initial request for administrative tolerance regarding documentation requirements of subsection 169(4) of the ETA was answered with CRA's publication of GST/HST Notice 199, *Procurement cards - Documentary Requirements for Claiming Input Tax Credits*, in June 2005. The success of the administrative policy contained in that notice can be measured by the very limited number of GST registrants who have applied for exemption under subsection 169(5).

In 2006, Finance and TEI established a sub-group in an attempt to find a better solution. Much work was completed by Finance and TEI, which culminated in an alternative proposal being presented by TEI on November 7, 2007. Progress on this matter stalled due to a reallocation of resources within Finance, particularly in respect of Ontario and British Columbia harmonization.

Is Finance prepared to reopen this file with a view to improving the solution proposed in GST/HST Notice 199?

8. Ontario Ministry of Finance First Nations Point-of-Sale Exemption Audits
(CRA Only)

Beginning September 1, 2010, Ontario began providing a point-of-sale exemption to the provincial component of the HST for sales of qualifying property or services made to First Nations peoples (referred to as Status Indians, Indian Bands and councils of an Indian Band living off-reserve in Ontario). Vendors provide a credit at the time of sale on these purchases. If a First Nations person makes a qualifying purchase but is charged the Ontario portion of the HST, he or she can apply to the Ontario Ministry of Finance for a refund of that amount. When a vendor makes a qualifying sale, it reports those amounts separately on its GST/HST returns filed with CRA.

The Ontario Ministry of Finance has been conducting its own audits of vendors making qualifying sales under the Ontario First Nations point-of-sale exemption. Those

auditors do not appear to have any information on the exemption amounts included by registrants on their GST/HST returns filed with CRA.

a. Is CRA aware of the Ontario Ministry of Finance audits of the Ontario First Nations point-of-sale exemption?

b. If a business is subjected to an Ontario Ministry of Finance First Nations point-of-sale exemption audit, will CRA exclude this review if CRA audits the same period?

9. Notice of Objection – Procedures

Despite the best efforts of CRA and businesses, some issues remain unsettled at the end of an audit. The inability to agree on an issue is often the result of a misunderstanding about the underlying facts. Finding a way to collaboratively eliminate those misunderstandings would result in fewer cases being appealed to the courts, saving all parties unnecessary time and expense.

a. *Avoiding factual misunderstandings (CRA only)*. We invite a discussion with CRA about its policy on Appeals officers discussing their determinations in advance of issuing decisions to ensure that there are no misunderstandings about the underlying facts that would lead to inappropriate results and unnecessary litigation.

(i). Does CRA have a written policy addressing discussions by Appeals officers with taxpayers prior to the issuance of a decision? If so, would CRA be willing to publish it?

(ii). In the absence of a written policy, what considerations do Appeals officers take into account when making these determinations?

b. *Alternative dispute resolution*. Are there any plans to study or advance the use of alternative dispute settlement arrangements such as arbitration or mediation in order to minimize the high costs of litigation?

10. Status of TEI Submissions on Sections 156 and 273 of the ETA

a. *Changes to Section 156 GST/HST Election for Nil Consideration.* On September 19, 2014, TEI submitted a letter to CRA and Finance addressing welcome changes to section 156 of the ETA announced in the Federal Budget. While generally positive, TEI noted a number of concerns about the new election provisions. For example, the proposed requirement to file all section 156 elections with CRA will create a heavy administrative burden that will not improve the administration of the election. We invite a discussion of the issues contained in our letter.

b. *Section 156 Nil Consideration Elections and Amalgamations.* The amendments to section 156 resulting from proposals announced in the 2014 Budget will require 156 elections to be filed with the Minister of National Revenue. The proposed

amendments to paragraph 156(4) provide that existing elections in effect before January 1, 2015 must be filed with the Minister before January 1, 2016. New elections coming into force after January 1, 2014 must be filed by the earliest date on which any of the parties to the election are required to file a return for the period that includes the day on which the election becomes effective.

Section 271 of the ETA provides that a corporation resulting from an amalgamation is deemed to be a continuation of each predecessor corporation under Part IX of the ETA for prescribed purposes. Section 156 of the ETA is one of those prescribed purposes. Consequently, a section 156 election made by a predecessor corporation before an amalgamation remains in effect after an amalgamation so long as the amalgamated corporation continues to satisfy the requirements of section 156.

Assume A Co and B Co are parties to a section 156 election with C Co with an effective date before January 1, 2015. A Co and B Co amalgamate into D Co on January 1, 2015. Assume all corporations are "specified members" of a qualifying group under section 156 subsequent to the amalgamation.

Would the CRA confirm that the section 156 election to which the amalgamated D Co is now a party (by operation of section 271) remains an election entered into before January 1, 2015 with the result that the election would be required to be filed before January 1, 2016?

c. *Application of Sections 156 and 167 to the Sale of a Business.* Consider the following scenario:

- Aco (parent company) and Bco (subsidiary company) are both closely related for purposes of section 156 of the ETA.
- Aco and Bco are partners in a partnership (no other partners) - Pship.
- Xco (parent company) and Yco (subsidiary company) are both closely related for purposes of section 156 of the ETA.
- Neither Xco nor Yco are affiliated with Aco or Bco.
- Aco, Bco, Pship, Xco, and Yco are all exclusively engaged in commercial activity for GST purposes.
- For purposes of the ensuing transaction, Aco forms a new wholly-owned subsidiary Cco (registered for GST).
- All the below transaction steps occur on the same day:

    1. Cco and Xco amalgamate to create Amalco 1.
    2. Amalco 1 and Yco amalgamate to create Amalco 2.
    3. Amalco 2 sells all of its assets to Pship.

It is assumed that steps 1 and 2 are non-taxable events per section 271 of the ETA (which deems certain transfers of property by amalgamating corporations not to be taxable supplies). Please comment on the availability of the section 156 election (election for nil consideration) and/or section 167 election (election for supply of assets

of a business) to relieve the need for Amalco 2 to charge GST to Pship on step 3 considering that Cco and Xco were never closely related, Cco was a new company with no prior business, and the effect (if any) of the Tax Court of Canada's decision in *Aviva Canada Inc. v. R.,* [2006] T.C.C. 57.

d. *Changes to Section 273 GST/HST Joint Venture Election*. On July 18, 2014, TEI submitted a letter to CRA and Finance addressing changes to the joint venture election in section 273 of the ETA proposed as part of the Federal Budget. TEI commended CRA and Finance for their efforts in developing and crafting the expansion of the election to include all joint ventures engaged exclusively in commercial activities where all participants of the joint venture are also engaged exclusively in commercial activities.

The use of joint ventures has become ubiquitous. Historically, businesses in the oil and gas sector have entered into joint ventures for innumerable projects that exist for long periods and often change considerably over time. Many other industries also regularly make use of joint ventures in various contexts. If businesses were required to file joint venture elections for each joint venture with CRA, it would create a substantial administrative burden on both businesses and CRA with no compliance or tax administration benefit to anyone. Indeed, a requirement to file a joint venture election would run contrary to the Government's commitments under the "Red Tape Reduction Policy of Economic Action Plan 2014." Recent amendments to the section 156 election for nil consideration requiring the filing of those elections with CRA have made businesses concerned that a similar requirement could be mandated for the section 273 joint venture election.

We invite a discussion of the issues addressed in our July 18, 2014 letter, and specifically our comments on the ill effects of requiring joint venture elections to be filed with CRA.

11. Modification and Termination Payments Under Section 182 of the ETA

Under section 182 of the ETA, certain damage payments or other amounts paid relating to the modification or termination of an agreement are deemed to include GST/HST. For example, if a person (the "Customer") makes a modification or termination payment to a registrant (the "Vendor") relating to an agreement for the making of a taxable supply, the modification or termination payment is deemed to include GST/HST (assuming all requirements under section 182 are met). In many cases, the Customer and Vendor document their modification or termination in a written agreement (a "Termination Agreement"). The ETA contains no requirement for a Termination Agreement to include a clause addressing the applicability of section 182 to the modification or termination payment.

Assuming the Customer is registered for GST/HST and engaged exclusively in a commercial activity, will the Termination Agreement (along with other documentation evidencing the Vendor's GST/HST registration number) satisfy the recordkeeping

requirements necessary to claim an input tax credit for the GST/HST deemed to be included in the termination or modification payment under section 182?

12. GST Flow-Through – Potential Double Recovery Under Section 180 of the ETA
(CRA only)

Registrants generally request a copy of the B3, *Canada Customs Coding Form*, issued by Canada Border Services Agency ("CBSA") as back-up documentation for claiming an input tax credit to recover the GST by a non-resident non-registrant ("NR²") vendor on the import of tangible personal property into Canada, and then reimburse the NR². In cases where physical possession of the tangible personal property remains with the registrant there is very little risk that a NR² vendor will be able to recover the GST from any other source. In the event the tangible personal property is returned, there is potential that the NR² vendor will seek a GST refund from CBSA when the property is exported from Canada. If this occurs, the NR² vendor would essentially recover the GST twice (*i.e.*, once from the registrant purchaser and once from CBSA). On February 17, 2014, section 180.01 was added to the ETA to prohibit the NR² vendor from recovering the GST that was paid on import more than once. However, this new section focuses on the NR² vendor not the registrant who is located in Canada and subject to GST/HST audit. Questions remain about the obligations of Canadian registrants in these situations.

What are the registrant's responsibilities if it has (i) paid an amount to an NR² vendor as a recovery for GST paid at the border for the import of tangible personal property, (ii) claimed an input tax credit, and (iii) later returns the tangible personal property to the NR² vendor exporting it from Canada?

13. Place of Supply
(CRA Only)

In the event where the general place of supply rule for services is being applied for a particular standard-rated supply made in Canada, can CRA provide guidance on the proper place of supply where the registrant supplier of the services is directed by the recipient to prepare the invoice for the supply with the recipient listed as the bill to party and to place the address of the recipient's third party broker on the invoice rather than the recipient's head office address (where the broker's address is in a different province than the recipient's head office address)? More specifically, is the place of supply of the services based on the recipient's head office address or the broker's address that was placed on the invoice?

In a similar context, would the guidance with respect to the place of supply of the services change where the supplier is being directed by the recipient to prepare the invoice with the recipient's third party broker listed as the bill to party and to place the broker's address on the invoice rather than the recipient's head office address (where the broker's address is in a different province than the recipient's head office address)?

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CONCLUSION

Tax Executives Institute appreciates this opportunity to present its comments and questions for discussion. We look forward to meeting and discussing our views with you on November 18-19, 2014.

Respectfully submitted,

Tax Executives Institute, Inc.

By: 

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