



HST

Harmonized Sales Tax



Ministry
of Finance

June 3, 2009

Confidential Advice to Minister - Numbers Preliminary

Slide 1

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BC Sales Tax (PST)

What is the PST?

- The PST is a retail sales tax
- Tax applies to purchase price of goods and some (very few) services
- Tax is paid by both consumers and business – tax on business inputs
- Many consumer exemptions (food, fuel, children's clothing, school supplies, bicycles etc.)

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Federal Goods and Services Tax (GST)

What is the GST?

- A broad-based value-added tax
- Tax applies to most goods and services with very few exceptions (basic groceries, prescription drugs and exports)
- Primarily paid by consumers (approximately 87% of tax paid)
- Businesses pay tax on inputs but most can recover the cost of GST (i.e., Business remits to government the difference between tax collected on sales and tax paid on purchases)

Federal Goods and Services Tax (GST)

GST Terminology

1. Taxable

- GST applies (e.g. cars, restaurant meals, shoes)
- Businesses claim ITCs

2. Zero-rated

- No GST charged to consumer (e.g. basic groceries, prescription drugs)
- Business can claim ITC's for tax paid on purchases

3. Exempt

- No GST is charged to consumer (e.g. dental and financial services)
- Businesses cannot recover tax paid on inputs

Comparison of GST and PST

PST

- 7% retail sales tax
- Narrow tax base
- Applies primarily to goods (few services)
- Many exemptions
- Paid by business and individuals (48% each)

GST

- 5% value added tax
- Broad tax base
- Applies to most goods and services
- Few exemptions
- Paid mostly by individuals (87%)
- Most businesses recover tax paid

Who Pays the Tax - PST vs. GST?

Who Pays the Tax

	<u>PST</u>	<u>GST</u>
Consumers	48%	87%
Businesses	48%	11%
Public Sector	4%	2%

Source: Provincial Input-Output 2004

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Harmonized Sales Tax (HST)

What is Harmonization?

- Elimination of PST
- Adding a provincial tax rate to the 5% GST
- Provincial rate applies to the GST base
- Federal legislation
- Federal administration (no provincial cost)

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Harmonized Sales Tax

HST means applying tax on goods currently exempt from PST

- Residential Fuels and heat (i.e., steam heat)
- Basic Cable and Residential Telephone
- Snack food and candy (only basic groceries exempt)
- Restaurant meals (only basic groceries exempt)
- Used clothing (other than children's clothing if a similar point of sale rebate to Ontario's proposed HST is implemented)
- Non-prescription medications
- Vitamins and dietary supplements
- Bicycles
- School supplies (other than books if point of sale rebate is provided on books)
- Magazines and newspapers
- Work-related safety equipment (i.e., safety glasses, gloves/footwear with built-in safety features)
- Safety helmets, life jackets, first aid kits
- Smoke detectors and fire extinguishers
- Motor vehicle towing, battery boosting and road-side tire services
- Christmas trees
- Energy conservation equipment (i.e., insulation, solar power equipment)
- Time limited energy efficient goods (i.e., fuel efficient vehicles, Energy Star products)

HST means imposing tax on services not currently subject to PST

- Personal Services (i.e., hair care)
- Dry-cleaning services
- Repair and maintenance services to household appliances
- Household repair and maintenance (i.e., renovations, painting, housecleaning, landscaping)
- Real estate fees
- Membership fees (i.e., health and fitness clubs)
- Registration fees (i.e., children's sports and activities)
- Admission fees (i.e., movies, live theatre, museums)
- Tourism services (i.e., booking fees, tours)
- Funeral services
- Professional services (i.e., accounting, architectural, photography, graphic design, home care services)
- Airline Fares (within Canada)

History of HST

- GST introduced in 1991
- Quebec partially harmonized its sales tax in 1991 but differences remain
- Three Atlantic provinces harmonized in 1997 (transitional funding provided)
- Federal requirements in 1997 HST offer
 - Provincial rate must be 8%
 - Same base as GST with sole exception of point-of-sale rebate for books
 - Federal administration
- Ontario will harmonize on July 1, 2010

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Timing

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Other Policy Decisions

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Policy Decisions: Other

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Additional HST Slides for Minister Only



Ministry
of Finance

June 15, 2009

Confidential Advice to Minister - Numbers Preliminary

Slide 1

GST / HST Treatment of Goods and Services

Three possibilities:

1. Taxable

- GST / HST charged to consumer
- Businesses can claim an input tax credit for tax paid on purchases
- Examples: cars, production machinery and equipment, restaurant meals, haircuts
- Why taxable? GST / HST meant to tax consumption of most goods and services

2. Exempt

- No GST is charged to consumer
- Businesses cannot recover tax paid on inputs (they bear tax burden)
- Examples: dental and financial services, long-term residential rental accommodation
- Why exempt? Social policy rationale, difficulty taxing financial services

3. Zero-rated

- Full tax relief
- No GST charged to consumer
- Businesses can claim an input tax credit for tax paid on purchases
- Examples: basic groceries, prescription drugs, exports of all goods and services
- Why zero-rated? Mitigates regressivity of sales tax, no embedded tax

Exempt Supplies

Specified Real Property

- Used residential housing including resale of rental housing
- Residential rental accommodation (1 month or more)
- Parking space in a condominium complex
- Share in cooperative housing

Medical/Dental services including:

- Ambulance service
- Nursing service by a registered or licensed nurse
- Optometric, chiropractic, physiotherapy, osteopathic, audiological, occupational therapy, psychological and midwifery services,
- Dental hygienist services
- Diagnostic, treatment or health care service prescribed by a medical practitioner

Exempt Supplies Cont'd

Child Care Services and Personal Care Services

- Babysitting and Daycare services for children 14 & under
- Care services for children and individuals with disabilities in residential care facilities

Bridge, Road and Ferry Tolls

- Includes BC Ferries charges*

* BC Ferries pays GST on all inputs – including fuel – and does not get input tax credits

Legal Aid Services

Specified Educational Services, including

- Elementary and secondary school
- Extracurricular activities
- School bus service
- Courses in Respect of Recognized Professional or Trade Designations
- Credit course for diploma or degree
- Vocational Courses

Exempt Supplies Cont'd

Music Lessons

Food & Beverages in school cafeterias and student meal plans

Specified Financial Services, including

- Arrangements for a loan or mortgage
- Arrangements for and issuing insurance policies by insurance companies, agents, and brokers

Most goods and services provided by charities, including

- Supplies of used or donated goods
- Short term residential accommodation (less than a month)
- Facilities rentals

Certain goods and services provided by non-profit organizations

- Goods less than \$5 sold for fundraising purposes

Exempt Supplies Cont'd

Certain goods and services supplied by public service bodies, including:

- Supply of children's recreational classes
- Property service registration, court registration fees
- Supplies of municipal services (water, snow removal, road maintenance)
- Municipal transit service

Zero-Rated Supplies

Prescription Drugs and Biologicals, includes

- Any medication purchased on the prescription of a medical practitioner
- Vaccines
- Dispensing fee
- **Does NOT** include agricultural or veterinary drugs

Medical and Assistive Devices, including

- Prescription eyewear,
- Hearing aids,
- Guide dogs for the blind
- Canes and crutches
- Orthotic devices
- Wheelchairs

Zero-Rated Supplies Cont'd

Basic Groceries, includes

- Basic foods (fruits, vegetables, bread, meat, etc.)
- Sweetening agents, seasonings and other ingredients to be mixed with or used in the preparation of such food or beverages
- **Does NOT** include vitamins and dietary supplements

Agriculture and Fishing Products, includes

- Livestock
- Grains and seeds
- Bulk fertilizer
- Tractors and harvesting equipment

Exports

International Freight Transportation and International Passenger Transportation

HST – on goods currently exempt from PST

HST means applying tax on goods currently exempt from PST

- Residential Fuels (i.e., electricity, natural gas) and heat (i.e., steam heat)
- Basic Cable and Residential Telephone
- Snack food and candy (only basic groceries exempt)
- Restaurant meals (only basic groceries exempt)
- Used clothing (other than children's clothing if a similar point-of-sale rebate to Ontario's proposed HST is implemented)
- Non-prescription medications
- Vitamins and dietary supplements
- Bicycles
- School supplies (other than books if point-of-sale rebate is provided on books)
- Magazines and newspapers
- Work-related safety equipment (i.e., safety glasses, gloves/footwear with built-in safety features)
- Safety helmets, life jackets, first aid kits
- Smoke detectors and fire extinguishers
- Motor vehicle towing, battery boosting and road-side tire services
- Christmas trees
- Energy conservation equipment (i.e., insulation, solar power equipment)
- Time limited energy efficient goods (i.e., fuel efficient vehicles, Energy Star products)

HST – on services not currently subject to PST

HST means imposing tax on services not currently subject to PST

- Personal Services (i.e., hair care)
- Dry-cleaning services
- Repair and maintenance services to household appliances
- Household repair and maintenance (i.e., renovations, painting, housecleaning, landscaping)
- Real estate fees
- Membership fees (i.e., health and fitness clubs)
- Registration fees (i.e., children's sports and activities)
- Admission fees (i.e., movies, live theatre, museums)
- Tourism services (i.e., booking fees, tours)
- Funeral services
- Professional services (i.e., accounting, architectural, photography, graphic design, home care services)
- Airline Fares (within Canada)
- Others

HST may also mean imposing tax on accommodation not currently subject to hotel room tax

- Accommodation in properties with less than 4 rooms (under HST, providers of this accommodation with annual income of \$30,000 or more will be required to collect HST)

HST – What Ontario is doing

Provincial rate choice

- Ontario is harmonizing at 8% - their current sales tax rate

Point-of-sale rebates

- Ontario will provide point of sale rebates on children's sized clothing and footwear, children's car and booster seats, books, diapers and feminine hygiene products

Rebates for MUSH sector

- Ontario will provide partial rebates to MUSH sector (municipalities, universities/colleges, schools, hospitals) and to non-profit organizations and charities
- Rebate levels set to avoid tax increases

New housing

- Ontario will rebate 75% of provincial portion of HST for new homes up to \$400,000

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What else is Ontario Doing?

In addition to harmonization, Ontario announced a full tax reform package during their 2009 Budget:

Personal Tax Measures:

- Personal income tax rate reduction from 6.05% to 5.05% on the first income bracket (up to \$36,848) effective January 1 2010.
- Enhanced sales tax credit and property tax credits effective July 1, 2010. Sales tax credit increased from \$100 to \$260 and phases out at for individuals and families at \$20,000 and \$25,000 respectively.
- Senior Homeowners' property tax grant increased from \$250 to \$500 effective 2010. Grant phased out for individuals and couples at \$35,000 and \$45,000 respectively.

Business Tax Measures:

- General corporate income tax rate reduced from 14% to 12% effective July 1, 2010 and reduced to 11.5% effective July 1, 2011, 11% effective 2012 and 10% effective 2013.
- Small business corporate income tax rate reduced from 5.5% to 4.5% effective July 1, 2010

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- *Other Options*

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HST – Issue Overview



Ministry
of Finance

June 25, 2009

Confidential Advice to Minister - Numbers Preliminary

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Policy Decisions for BC

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Ministry of Finance



Ministry
of Finance

July 13, 2009

Confidential Advice to Minister

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Outline

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Memorandum of Agreement

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Ministry of Finance
BRIEFING DOCUMENT

To: Honourable Colin Hansen
Minister of Finance

Date Requested: March 2, 2009
Date Required:

Initiated by: Glen Armstrong, A/ADM
Strategic and Corporate
Policy Division

Date Prepared: March 12, 2009

Ministry Contact: Glen Armstrong, A/ADM
Strategic and Corporate
Policy Division

Phone Number: 250 387-9011
Email: Glen.Armstrong@gov.bc.ca

184733

TITLE: Sales Tax Harmonization

PURPOSE:

(X) INFORMATION / ISSUE OVERVIEW

COMMENTS:

Ontario Premier Dalton McGuinty has been indicating publicly that Ontario is taking a serious look at sales tax harmonization and may announce something in its budget on March 26.

There is a strong possibility that the British Columbia government will be asked in the next couple of weeks about its position on harmonization.

DATE PREPARED: March 12, 2009

TITLE: Sales Tax Harmonization

ISSUE:

Ontario Premier Dalton McGuinty has indicated that Ontario is seriously looking at harmonization and there is a possibility that Ontario will announce within the next couple of weeks that it will harmonize its sales tax with the federal GST.

Even if this does not occur, it is very likely that the Government of British Columbia will be asked about its position on harmonization.

BACKGROUND:

The federal government is strongly encouraging provinces to harmonize their sales taxes with the federal goods and services tax (GST) and is emphasizing the benefits and importance of harmonization.

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Harmonization means repealing the provincial sales tax (PST) and adding a provincial tax rate to the 5% federal GST. The combined harmonized sales tax (HST) would be a value added sales tax applied to the current GST base (i.e., tax on virtually all goods and services except basic groceries and prescription drugs).

The current HST has four common elements:

- A common HST rate of 13% (5% GST plus a provincial component of 8%);
- A common tax base (the same base as the GST, with a point-of-sale rebate of the 8% provincial portion for books);
- Common legislation (the federal *Excise Tax Act*); and
- Common federal administration (CRA administers the HST at no cost to provinces; payments are made to provinces based on a formula). As the first province to partially harmonize with the GST in 1991, Quebec was allowed to administer both its tax and the federal GST within Quebec. The federal government does not currently offer provincial administration as an option.

Under the HST provinces are able to provide certain public sector bodies with rebates of varying percentages (municipalities, universities, schools, hospitals, charities and non-profits). There are also partial rebates for new housing. There is considerable variation in the rebates provided by current HST provinces.

The attached appendices provide a technical overview of sales tax harmonization (appendix 1)

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Ontario recently indicated that it is taking a “long, hard look” at harmonization.

- Previously (as recently as November 2008), Ontario Premier Dalton McGuinty stated that the province had no desire to harmonize and would only entertain the idea if substantial federal funding were provided.
- In January 2009, McGuinty indicated that Ontario was looking at harmonization and that Ottawa could help seal the deal if it provided financial support, similar to that provided to other provinces in the past. McGuinty also said that he had raised the issue with Prime Minister Stephen Harper and hopes talks continue.
- In February 2009, McGuinty indicated that Ontario is looking at harmonization so seriously that a change may come in Ontario’s Budget on March 26. McGuinty said that there seems to be an emerging consensus around harmonization and he reiterated that financial support from Ottawa would be required (likely \$ billions).

DISCUSSION:

In light of Ontario’s recent public statements regarding harmonization (with the possibility of a more substantive announcement within the next few weeks), the British Columbia government will likely be asked about its position on harmonization. Government may wish to consider how to respond to these questions.

Economic Impacts of Harmonization

There is a considerable amount of economic literature which suggests that, in the medium and long term, there are positive economic benefits to harmonization. Potential advantages of harmonization include:

- Improved economic competitiveness and productivity of British Columbia business due to the removal of taxes on most business inputs (i.e., those used to provide taxable sales);
- Improved international and interprovincial competitiveness (no sales tax embedded in exports);
- Reduced economic distortion (an HST would tax most goods and services equally);
- Increased investment and job creation; and
- Simplified compliance and reduced compliance costs for business.

Studies have shown a significant increase in investment in the harmonized provinces following sales tax reform. Studies have also shown that the savings from reducing tax on business inputs were passed along to consumers.

However, while there are many studies showing the positive long-term economic benefits of harmonization, there are also studies showing potential short-term economic costs. Given current economic conditions, this could be a concern.

For example, a recent study by the C.D. Howe Institute suggests that, while the long-term economic gain from harmonization is relatively clear, harmonization will cause a short-term loss in GDP and unemployment. Part of the reason is that the negative effect of higher consumption taxes occurs faster than the positive effect of lower taxes on investment goods and exports. The study suggests that it may take five or more years before the impact on GDP is positive and even longer for real wages and job numbers to recover.

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The C.D. Howe study also suggests that harmonization has a positive impact on federal government revenues, creating an opportunity for compensation from the federal to provincial governments.

Distributional Impact

Harmonization would result in a real shift of the tax burden from businesses to individuals, and an even larger perceived shift.

- Businesses currently pay PST on business inputs but under the HST businesses making taxable sales would receive input tax credits (ITCs) to recover tax paid on their business purchases. Businesses making exempt sales (e.g., residential rents and financial services) would pay tax on their purchases but would be unable to claim ITCs because businesses can only claim ITCs to the extent that the inputs are used in making taxable supplies (i.e., sales which are subject to HST).
- Consumers would pay tax on virtually all goods and services, including most that are currently exempt from PST or not taxable (e.g., residential fuel, magazines and newspapers, children's clothing and footwear, restaurant meals, etc.).
- Individuals are already indirectly paying some of the sales tax that they would pay directly under an HST (i.e., a portion of PST paid by business is imbedded in product costs and passed on to consumers). However, the imbedded sales tax is not visible and the HST is very visible, so individuals would perceive that there has been a larger tax shift than has actually occurred.

- About 48% of the total PST paid in British Columbia is paid by business, 48% by consumers and 4% by the public sector. For comparison, 87% of GST paid in British Columbia is paid by consumers, 11% by business and 2% by the public sector.

The issue of harmonization is often raised and supported by many businesses and business associations, including Chambers of Commerce. However, some business sectors, such as the restaurant industry which currently enjoys PST exemptions that would be lost under an HST, strongly oppose it.

Fiscal Impact

The fiscal implications of harmonization are dependent on multiple provincial policy decisions that would have to be made such as the level of low-income tax credit to help offset the impact of the broader tax base and the level of rebates, if any, for municipalities, universities, schools, hospitals, and new housing.

Depending on the various policy decisions taken, harmonization would require roughly a 7% provincial tax rate on top of the GST to be revenue neutral for the province.

However, while harmonization would probably be revenue neutral at 7%, entering into an HST at a higher rate (e.g., 8%) could provide opportunities to further enhance the competitiveness of the provincial tax system by generating additional revenue that could be used to reduce other taxes.

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OPTIONS:

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Appendix 1: Sales Tax Harmonization – Technical Note

- Harmonization means repealing the PST and adding a provincial tax rate to the five percent federal GST. To be revenue neutral for the province this would require, depending on various policy decisions taken, roughly a seven percent provincial tax rate on top of the GST. The combined tax rate would be applied to the current GST base (i.e. tax on virtually all goods and services except basic groceries and prescription drugs).
- Harmonized sales taxes are now in place in Newfoundland and Labrador, Nova Scotia and New Brunswick. Those provinces impose eight percent provincial tax rates for combined HST rates of 13 percent. Quebec also has a modified version of HST, where a Quebec sales tax (QST) of 7.5 percent is applied on top of the GST for a combined effective rate of 12.875 percent. With the exception of Alberta which has no provincial sales tax, all other Canadian provinces have retail sales taxes.
- The Harmonized Sales Tax (HST) is a multi-stage value-added sales tax levied and collected at all stages of the production and distribution chain as goods move from primary producers to wholesalers, to retailers, and finally to consumers. All businesses and final consumers are required to pay the HST but businesses claim a credit, called an input tax credit (ITC), for any tax paid on their business inputs, provided those inputs are used in making taxable sales. Thus, most businesses effectively recover all tax paid on purchases for business use.

Businesses can claim ITCs to the extent that the inputs are used in making taxable supplies (i.e. sales which are subject to HST). Inputs used for making exempt supplies (e.g. financial services) are ineligible for ITCs.

- Retail sales taxes like the British Columbia social service tax are single stage taxes imposed primarily on sales of goods to final consumers at the time of purchase. Businesses may purchase goods for resale or lease exempt of tax but must pay tax on all items purchased for their own business use as they are the final consumers. Thus, under a retail sales tax, businesses pay tax on business inputs. In British Columbia, even with the exemption for production machinery and equipment, businesses pay about 48 percent of the total provincial sales tax paid in the province (i.e. about \$2.5 billion in 2008/09).
- Harmonizing the PST in British Columbia with the GST would have the following implications:
 - The elimination of most PST exemptions. For example, the following items would no longer be exempt from tax: residential fuel, magazines and newspapers, children's clothing and footwear, restaurant meals, candies, snack foods, school supplies, basic cable TV and residential telephone, prescribed safety equipment, and patent medicines.

- Imposition of the PST on most services that are not currently taxed. All services which are currently subject to GST would be subject to the combined HST rate. A few examples of these services are: accounting services, architectural services, services of a general contractor, consulting services, tourism services (ski lift tickets, golf fees etc.) and personal care services (e.g. beauticians and hairdressers).
- British Columbia's ability to make unilateral changes to the provincial tax base in support of specific provincial social or economic policy objectives would be reduced if the tax were administered by the federal government. Relieving measures would still be possible although at potentially high administrative cost (e.g. NB provides a refund of the eight percent provincial portion of the HST on energy purchased for residential use). Provincial administration would provide more flexibility but would also increase complexity and significantly increase costs for both business and government. Also, the federal government is unlikely to agree to provincial administration of the GST.
- There would be a shift in the tax burden from businesses to individuals because businesses would receive input tax credits to recover tax paid on their business purchases while consumers would pay tax on virtually all goods and services, including most that are currently exempt from PST or not taxable. This shift would likely be perceived as being larger than it actually is because individuals are already indirectly paying some of the sales tax that they would pay directly under an HST (i.e. a portion of sales tax paid by business is imbedded in product costs and passed on to consumers). However, the imbedded sales tax is not visible and the HST is very visible, so individuals will perceive that there has been a larger tax shift than has actually occurred.
- The fiscal implications of harmonizing are dependent on multiple policy decisions that would have to be made such as; the level of rebates, if any, for municipalities, universities, schools and hospitals, and new housing and the level of low-income tax credit to help offset the impact of the broader tax base. However, it has been estimated that, depending on rebate decisions taken, a shift to a harmonized sales tax would be roughly revenue neutral for the province at seven percent.
- The potential advantages of harmonization include:
 - Improved competitiveness and productivity of British Columbia business by removing tax on business inputs.
 - Simplified compliance and reduced compliance costs for business.

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