

Tax Memo

Harmonization – Retail Trade

After 18 years of maintaining a retail sales tax alongside the federal GST, Ontario is making a bold move to modernize sales taxes in the province. In his budget, Finance Minister Dwight Duncan announced that Ontario will be “harmonizing” its sales tax system with the GST, effective July 1, 2010. Instead of a 5% federal GST and 8% Ontario Retail Sales Tax (RST), there will be a single 13% Harmonized Sales Tax (HST) in Ontario. This system has been in operation in Newfoundland and Labrador, Nova Scotia and New Brunswick since 1997.

This decision will be applauded by most economists as a step toward improving the productivity and competitiveness of Ontario’s economy. With regard to the retail sales sector, on the cost side, harmonization with the GST will be beneficial. Currently, many costs borne by the sector are subject to unrecoverable RST, including building materials, computers, display furniture and delivery vehicles. Under the HST, the industry will be able to recover the HST paid on these purchases by claiming input tax credits on their GST/HST returns.

On the sales side, however, the effect of sales tax harmonization will depend largely on the existing RST status of the goods and services sold. Most goods sold to consumers are currently taxable under the RST and will continue to be so under the HST. However, because the HST will tax a much broader range of services, retail service providers, from plumbers to golf courses, will see an increase in the tax rate applied to their services.

Notwithstanding that the tax base for the Ontario portion of the tax will broadly mirror the GST, Ontario is providing point-of-sale rebates for the provincial portion of the tax for the following selected items:

- Books;
- Children’s clothing and footwear;
- Children’s car seats and car booster seats;
- Diapers; and
- Feminine hygiene products.

What should the retail trade sector do before the new HST system is introduced?

Although business systems currently used for the GST can also be used to comply with the HST, some modifications may be required. In addition, the transition to the HST in Ontario will give rise to many of the same issues that arose with the GST rate reductions on July 1, 2006, and on January 1, 2008.

The HST in Ontario will substantially mirror the GST, but there are certain differences which will require systems modifications. As noted, the above point-of-sale rebates will require retailers to distinguish such sales from other fully taxable items. In addition, during the first 8 years of the tax, large businesses (annual taxable sales in excess of

\$10 million) will face restrictions in claiming input tax credits for certain categories of expenditures, such as energy (other than for producing goods for sale), telecommunications, food, beverages and entertainment, and road vehicles weighing under 3,000 kg (including repairs, parts and fuel). This will require additional modifications to systems to track purchases of these items.

Vendors outside Ontario may also have to modify their systems to apply HST, rather than GST, on sales to Ontario customers.

Apart from systems issues, Ontario retail sales companies and service providers should plan for the removal of the RST from costs and may wish to postpone certain major purchases which are currently subject to RST. Service providers should also carefully review agreements entered into with buyers to ensure that they can contractually add on the provincial HST component to their prices.

Experience suggests that transitional rules will apply to transactions straddling the implementation date – such as long-term leases, equipment rentals and fixed-price contracts.

For more information on the implications of Ontario sales tax harmonization on your business and what you should be doing now to prepare for it, contact the following or your local PricewaterhouseCoopers Indirect Tax representative.

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