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HST - Information for the Auto Sector

On July 23, 2009, the British Columbia government announced that the Provincial Sales Tax (PST) would be harmonized with the federal Goods and Services Tax (GST) resulting in a new Harmonized Sales Tax (HST). Details on the exact mechanics of how the new HST will work have been few and far between. With the July 1, 2010 implementation date rapidly approaching, some details on how the new tax will affect the auto sector in B.C. have been released.

Automobile Leases

A. General Rules

In October 2009, the Canada Revenue Agency released GST/HST Notice No. 247 providing general transitional rules for personal property and services. The B.C. Ministry of Finance issued HST Notice #1 on October 14, 2009 providing further guidance on the general transitional rules for B.C. Under these notices and existing PST legislation:

1. GST and PST (where PST is applicable) apply to lease intervals or the portion thereof for periods prior to July 1, 2010;
2. HST applies to lease intervals or the portion thereof on or after July 1, 2010, subject to prepayment rules; and
3. GST and PST (where PST is applicable) apply for lease intervals that begin prior to July 1, 2010 and end before July 31, 2010.

B. Prepayments

In order to prevent avoidance of the HST through the prepayment of leases prior to July 1, 2010, special rules will apply where a lease interval or portion thereof occurs after July 2010 and consideration is paid or payable:

1. Before October 15, 2009

GST and PST apply (where amounts are PST taxable)

2. From October 15, 2009 to April 30, 2010

GST applies and PST does not apply¹

3. From May 1, 2010 to June 30, 2010

HST applies and PST does not apply.²

Restricted Input Tax Credits

A. General Rules

On February 19, 2010, the B.C. Ministry of Finance issued HST Notice # 4 regarding the temporary recapture of input tax credits. Under these new restricted input tax credit (RITC) rules, large businesses having total HST taxable sales of more than \$ 10 million per year will be unable to claim full input tax credits on certain specified items. The RITC recapture system will be subject to a phase out over a number years, summarized in the table below.

RITC	Period
100%	July 1, 2010 to June 30, 2015
75%	July 1, 2015 to June 30, 2016
50%	July 1, 2016 to June 30, 2017
25%	July 1, 2017 to June 30, 2018
0%	On or after July 1, 2018.

The British Columbia government has indicated that it may accelerate the phase-out of the RITC system as financial circumstances permit.

¹ Persons who are non-consumers, for example businesses and public sector bodies, may be required to self-assess the B.C. component of the HST on consideration for a supply of property by way of lease that becomes due, or is paid without having become due, after October 14, 2009 and before May 1, 2010 to the extent that the consideration is for part of a lease interval that occurs on or after July 1, 2010, unless the lease interval begins before July 1, 2010 and ends before July 31, 2010.

² The lessor is required to account for the B.C. component of the HST in the GST/HST return for the lessor that includes July 1, 2010.

In general, the RITC system will apply to:

- specified road vehicles, including certain vehicle parts and services;
- specified energy;
- specified telecommunication services; and
- specified meals and entertainment expenses currently subject to a 50% restriction.

B. Specified Road Vehicles

Of particular interest to auto dealers are RITC's for specified road vehicles. A specified road vehicle is a motor vehicle that is licensed for use on a public highway and weighs less than 3,000 kg at the time the vehicle is first licensed or required to be licensed in British Columbia.

1. Used Before Resupply

Dealer use vehicles are considered to be specified road vehicles used before supply. Large businesses will be required to recapture the provincial component of the ITC's claimed that is attributable to 2% of the cost of the vehicle.

For example, in April 2011, a car dealership that is a large business acquires for the purpose of resale, a vehicle that costs \$ 20,000 and claims input tax credits in respect of the acquisition and does not recapture the ITC's through the RITC system. The dealership subsequently uses the car as a demo vehicle for two months before selling it. The dealership would recapture \$ 56 of the ITC's claimed in respect of the acquisition of the vehicle.³

2. Parts and Services

The RITC system generally applies to vehicle parts and services that are acquired, or brought into British Columbia, by a large business in respect of a specified road vehicle if those parts and services are acquired, or brought into B.C., within 12 months of acquiring the vehicle or bringing it into B.C. The 12 month test will apply even where the vehicle was acquired or brought into B.C. prior to July 1, 2010. The RITC system will generally not apply to vehicle parts

³ \$ 20,000 cost x 2% x 7% (provincial component of HST) x 2 months = \$ 56.

and services that are acquired or brought to B.C. by a large business for the routine repair or maintenance of a specified road vehicle of that business, rather the RITC system will apply to parts and services such as anti-theft devices or other additions that are not considered routine maintenance.

3. Election to Use Estimation and Installment Approach

In recognition of the short time frame to adjust accounting systems to capture RITC information and to simplify tax compliance, large businesses will be allowed to elect to use an estimation and installment approach to account for RITC's. The election would be filed with the Canada Revenue Agency after the end of the fiscal year and would apply for at least one year. Large businesses will be allowed to elect to use the estimation and installment approach prior to the implementation of the B.C. HST on July 1, 2010.

Under the estimation and installment approach, a large business would:

- Estimate the amount of RITC's for a fiscal year;
- Report equal installments of RITC's in each reporting period in the one year period; and
- At the end of the fiscal year, reconcile differences between the estimated and actual RITC amounts.

Mandatory NETFILE

On January 4, 2010, changes to the GST/HST reporting requirements were announced. Businesses that are required to report RITC's for the provincial part of the HST paid or payable on certain taxable supplies in B.C. will be required to file their GST/HST returns by NETFILE for all reporting periods that end on or after July 1, 2010.

2010 Federal Budget

Draft legislation to enact these rules and other potential rules affecting the auto sector may be released in the March 4, 2010 Federal Budget. Kindly contact us after the budget release date for additional information.