

Harmonized Sales Tax

Residential Builders

The Ontario government announced in its March 26, 2009 budget, that it will adopt a single sales tax system effective July 1, 2010. This new system will combine the 5% Federal Goods and Services Tax (GST) and the 8% Ontario Retail Sales Tax (PST) to create a 13% Harmonized Sales Tax (HST). The HST will be administered by the Canada Revenue Agency and will substantially follow the GST regime, with a few key differences.

The HST uses a value-added tax structure that will allow most businesses to claim input tax credits (ITC) on the 13% HST paid. This is unlike the PST which applies to many purchases made by a business and is not refunded, leaving the PST embedded in the price of the finished goods and services as a sunk cost to the business. One of the purposes of the HST is to take away the hidden tax as well as lower administrative costs incurred by businesses.

Builders and contractors will now be able to claim the full 13% HST they have paid as an ITC.

Real property builders will see significant changes with the implementation of the HST. Currently, when builders and contractors purchase goods, they pay the 5% GST and 8% PST (the 8% being non recoverable) for most items. Builders and contractors will now be able to claim the full 13% HST they have paid as an ITC. This means a savings for builders and contractors.

Because of the nature of the business, which sees contracts being signed well in advance of construction beginning, builders are faced with many questions about the transitional rules. The residential housing industry faces industry specific rules that will be reviewed below.

When Will HST Apply?

The general rules indicate that for goods, HST will apply when goods are delivered and ownership transferred after June 30, 2010. As for taxable services, HST will apply for services performed after June 30, 2010. For transactions that straddle the July 1, 2010 implementation date, there are also transitional rules that need to be considered.

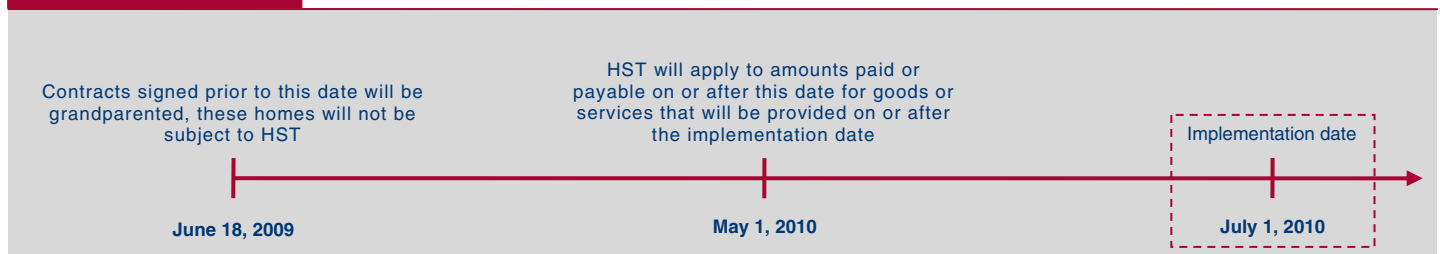
For residential builders, the sale of a newly constructed or substantially renovated home or rental home, will be subject to HST where both ownership and possession of the home are transferred after June 2010, unless it is a grandparented home.

Transitional Rules

The basic transitional rules are as follows for most goods and services:

- If consideration is due or paid on or after May 1, 2010 and before July 2010 then HST would apply to the extent that the consideration is for goods or services that are delivered, performed, or for which ownership is transferred after June 2010.

Key Transitional Dates



PST Transitional Rebate

Residential builders have specific transitional rules that apply when construction straddles the implementation date, since the cost of the home will have some PST embedded in it. Therefore, where HST is payable on the new home and the construction straddles the implementation date, a PST Transitional Housing Rebate will be available. To qualify for this rebate, construction must be at least 10% complete on July 1, 2010. The credit is claimed by the purchaser and can either be obtained through the builder or directly from the Canada Revenue Agency. The eligible applicant will have two methods available to calculate the estimated embedded PST. Once the estimated PST content is established, a percentage ranging between 25% and 100% (varies based on percentage of completion) would be applied to the estimated PST content amount.

Grandparented Rules

Because builders of grandparented homes will be eligible for ITC's for inputs after July 1, they will be required to pay a transitional tax adjustment. This is to account for the PST that would have otherwise been embedded in the new home under the current regime. This adjustment applies to homes that are less than 90% complete on the implementation date. Special rules also apply to resellers who do not occupy the home.

Ontario New Housing Rebate

If the conditions for claiming the GST new housing rebate are met, the home will also qualify for the Ontario new housing rebate. Purchasers will be entitled to a rebate of 75% of the provincial part of the HST up to a maximum of \$24,000. This credit is available regardless of the purchase price for the home. This credit can be claimed by the purchaser or assigned back to the builder. There is also an Ontario new rental housing rebate.

Builder Disclosure Requirements

If a written agreement is entered into for a newly constructed residential complex, the builder will be required to disclose in the agreement whether the provincial portion of the HST applies to the sale. If it does, the builder also needs to disclose whether it is included in the stated price, and whether the new housing rebate will be assigned to the builder.

If the transaction is subject to HST and the disclosure above is not made, under the transitional rules, the stated price is deemed to include the provincial portion of the HST. The purchaser will not be required to pay the provincial portion of the HST.

Transitional Credit for Small Businesses

To help businesses with this change, a one-time transitional credit for small businesses was introduced to assist with the additional costs that will be incurred to implement the changes. This credit is based on the level of taxable sales in the first full quarter commencing after June 30, 2010. The credits will range between \$300 for businesses with sales under \$15,000 in the quarter to a maximum of \$1,000 for businesses with sales over \$50,000 but less than \$500,000 in the quarter. If sales exceed the \$500,000 threshold in the quarter, there will be no credit available.

Temporary Restrictions for Large Businesses

Large businesses, with annual taxable sales in excess of \$10 million (for associated group), will face a temporary restriction on the provincial portion of the ITC for the first 8 years for certain expenditures such as:

- Energy, except where purchased by farms or used to produce goods for sale
- Telecommunication services other than internet access or toll-free numbers
- Road vehicles weighing less than 3,000 kilograms and fuel to power those vehicles
- Food, beverages and entertainment

The ITC's available will be nil for the first five years and will then be phased in at 25% per year starting in year 6. Full ITC's will be available to large businesses beginning in Year 9 after implementation.

Five P's Residential Property Builders Should Consider in Transitioning Towards the HST

| | |
|--------------------|---|
| Prepare | <ul style="list-style-type: none"> ▪ Assign someone or a committee to learn about HST, the place of supply rules, the transitional rules and the new mandatory electronic filing requirements ▪ Prepare an estimate of decreased costs to assist in proper budgeting and determination of cash flow; consider inputs which currently have PST such as goods used in the building process ▪ Determine if you are a large business, subject to the restrictions <ul style="list-style-type: none"> ➤ If so, accounting systems need to be able to track restricted ITCs (i.e. Fuel on fleet vehicles) ▪ Identify grandparented homes ▪ Establish percentage of completion for PST Transitional Rebate on June 30, 2010 |
| Paper | <ul style="list-style-type: none"> ▪ Review contracts, invoices, receipts, expense reports, etc. that will need to be updated to show HST ▪ Review employee taxable allowance and benefits, ensure proper HST charged and ITCs claimed ▪ Review current contracts to ensure they consider HST and make revisions accordingly ▪ Final PST return due July 23, 2010 |
| Procedure | <ul style="list-style-type: none"> ▪ Review accounting system, ensure updated to be compliant with HST ▪ Cash registers, computer software and possibly websites will need to be updated to include HST <ul style="list-style-type: none"> ➤ Plan on doing a test run of your system prior to May 1, 2010 ▪ Determine the level of training required for management and staff ▪ Consider changing the HST reporting period to assist with cash flow, where eligible |
| Pricing | <ul style="list-style-type: none"> ▪ Consider the effect HST will have on pricing of goods in order to remain competitive ▪ Consider effect on timing of sales in the current year |
| Procurement Policy | <ul style="list-style-type: none"> ▪ Consider leasing vs buying for large purchases prior to July 1, 2010 or delay large purchases until after July 1, 2010 ▪ Understand the effect of HST on major suppliers |

About Collins Barrow

Collins Barrow is committed to the highest level of integrity, quality and professionalism and provides clients with solutions in the area of Audit, Tax and Transaction Services.

Collins Barrow is Canada's largest association of Chartered Accounting firms and the eighth largest group of chartered accountants in Canada. Known as Canada's mid-market alternative for audit, tax and advisory solutions, we have developed a reputation for being a real choice for quality and value added financial advice due to the depth and breadth of in-house skills, customized offerings, commitment to excellence in customer service and our global reach. Our unmatched service and deep financial offerings make Collins Barrow the right choice for maximizing shareholder value.

We serve companies at all stages of their development from large publicly traded companies to emerging and owner managed businesses. Our clients come from a cross section of industries including: Private Equity, Manufacturing, Industrial, Wholesale, Retail and Distribution, Professional Services, Financial Services, Real Estate and Land Development, Hospitality and Entertainment, Technology and Communications, Energy and Mining, Biotech and Not for Profit. Our understanding and firsthand experience in the trends that are impacting these industries continues to prove that our professionals are well positioned to offer valued and effective solutions.

Our global reach extends beyond the more than 40 offices in Canada into 110 countries worldwide through Baker Tilly International, the eighth largest accountancy and business advisory network in the world. Together, we offer clients an established platform and access to the highest quality resources for audit, tax and transaction support in the global market place.

Independent, responsive and trusted. We are the true national alternative. Collins Barrow, Clarity Defined.

For more detailed information on the implications of the Harmonization of the PST with the GST for your business, contact a partner at your local Collins Barrow office or visit us at www.collinsbarrow.com.

Clarity Defined.

Ottawa (Moodie)

301 Moodie Drive
Suite 400
Ottawa, Ontario K2H 9C4
T: 613.820.8010 / F: 613.820.0465
E: ottawa@collinsbarrow.com

Ottawa (Queensview)

2725 Queensview Drive
Suite 500
Ottawa, Ontario K2B 0A1
T: 613.226.5661 / F: 613.226.3141
E: queensview@collinsbarrow.com

Manotick

1136 Clapp Lane
Box 291
Manotick, Ontario K4M 1A3
T: 613.692.2553 / F: 613.692.2995
E: manotick@collinsbarrow.com