

New Rules for BC PST

Contributed by Ken Ghag and Andy Vogel of Ernst & Young

As announced in the British Columbia budget earlier this year, there are changes to the application of provincial sales tax (PST) to all real property contracts entered into on or after October 1, 2008. Real property contractors and their customers should be aware of these new rules, which may change the way they account for PST.

A real property contractor provides services to real property or supplies and installs materials and equipment that become improvements to real property. This definition includes contractors and trade subcontractors in the construction industry, as well as in other businesses that make improvements to real property.

What were the rules prior to October 1, 2008?

In an attempt to simplify the determination of who pays PST on materials and equipment, British Columbia has introduced new legislation for real property contracts. (See Division 11 of the *Social Service Tax Act*). For contracts entered into before October 1, 2008, the determination of the party responsible for paying the PST on the materials and equipment supplied and installed as part of the contract was determined by the type of contract. For example, for a lump-sum or fixed-price contract, the contractor paid the PST. For a time-and-materials contract, the PST was paid by the customer.

In general, under a lump-sum or fixed-price contract, the contractor delivers a completed improvement to real property to the customer. The contract is set up so the customer pays a single, fixed price for both the materials and the equipment and labour. In contrast, a time-and-materials contract generally provides for a charge for the materials and equipment and

another, separate charge for the labour.

Although the distinction between these two types of contracts may appear to be obvious, many contracts contain elements of both types. This has led to different views by contractors, customers, and B.C. auditors on what type of contract is in place, which has resulted in assessments, adjustments and refunds of PST.

What are the rules now?

For contracts entered into on or after October 1, 2008, there is no longer a need to determine whether the contract is a lump-sum/fixed-price contract or a time-and-materials contract. The default rule is that contractors will be considered the purchaser and thus responsible for the PST on materials and equipment that they install. Contractors and their customers will be able to opt out of the default rule and have the customer directly pay the PST, but only if the contract specifically states that the customer is responsible for paying the PST, and indicates the value of the materials and equipment on which the PST is payable.

It is important to note that these new rules only apply to contracts entered into on or after October 1, 2008. Contracts entered into prior to this date fall under the old rules — even when the work is performed on or after October 1, 2008.


What issues do you need to think about?

To comply with the new legislation, contractors need to be aware of several issues, including the following:

Inside this Issue:

- New Rules for For BC PST

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Contractors and their customers must distinguish between real property and tangible personal property in order to determine how PST applies on a given contract. This determination can be difficult since one has to refer to the common law definition of real property, as well as review the requirements of the B.C. *Social Service Tax Act*. The risk to the contractor is in failing to collect PST on what turns out to be a sale of tangible personal property (TPP). Tangible personal property is property that can be seen, weighed, measured or touched, or in any other way perceptible to the senses. It includes natural or manufactured gas, software, heat and electricity. This could result in a net assessment to the contractor based on the markup that was charged on that TPP. It could also result in an assessment to the purchaser on the price paid for the TPP. When contracts involve the supply of both real property improvements and TPP, the charges for each portion must be shown separately and the PST must be applied according to the type of supply.

Multiple contracts for a single job

Generally, if two contracts govern the same facts and, provided that one is dominant over the other, then the terms of the dominant contract will prevail. If two contracts govern a project but only one comments on the application of PST, then PST would apply based on the wording of the contract that comments on the PST. Contractors and customers should ensure that, if they have more than one contract governing a project, the PST wording is not contradictory.

Contract requirements

In order for an October 1, 2008-or-later contract to be considered a time-and-materials contract, the wording must specifically state that the customer is responsible for paying the PST and must also set out the value of the materials.

It is our understanding that setting out the value of the materi-

als in the invoice is not sufficient unless the invoice forms part of the contract. In order to comply with these requirements, the contractor and customer need to determine the value of the materials at the time of entering into the contract. As this is difficult to do precisely, we hope that the tax branch will allow some leeway and not apply this requirement too strictly. It may be possible to structure the contract so that the default rule does not apply, yet the PST cost is the same as if the default rule did apply.

Exempt customers

Some customers may be eligible for PST exemption, such as First Nations peoples with status, farmers, manufacturers, diplomats and federal government departments. Contractors are able to claim a PST exemption on materials and equipment that they will install on behalf of exempt customers. Contractors should be aware of the documentation required to support such exempt purchases and the requirement to use the new form FIN 453/C (not FIN 453/M) to claim the exemption.

What should you remember?

Real property contractors and their customers should consider the new PST legislation when entering into contracts. Compliance with the documentary requirements of the new legislation will ensure that there are no unpleasant surprises come audit time. Contractors should also keep in mind that, when they are required to pay the PST and their material supplier has not charged the tax, such as on out-of-province purchases, they are responsible for self-assessing the PST.

If contractors are uncertain of their PST obligations, they should consult with the B.C. Ministry of Small Business and Revenue or a professional advisor.

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