

Sales Tax Harmonization Benefits BC's Construction Industry

By Carl Beck, CMA, Sales Tax Advisor

On a quiet summer day, July 23, 2009, the BC Government made a very large announcement that has since generated a lot of noise - BC intends to harmonize its Social Service Tax (PST) with the GST to form a single Harmonized Sales Tax (HST).

Value-added taxes similar to BC's proposed HST are used in Quebec and the Maritimes (excluding PEI) and very broadly throughout the industrialized world. In March 2009, Ontario announced its intentions to implement HST. BC will now follow Ontario's lead and combine its 7% PST with the 5% GST for a single 12% HST in BC (Ontario's HST will be 13%), both starting on July 1, 2010. Economists and most business advocates applaud this news which in theory will reduce the costs of doing business in BC (and Ontario) and possibly stimulate new investment to help Canada's economic recovery.

The BC Government's recent PST Consultation on Real Property Improvements produced several PST simplification measures that had previously burdened BC Construction Association members for many years. PST audits had been particularly onerous against construction companies which were perpetually exposed to assessments for errors, mainly because of the excruciating complexity of the PST rules affecting construction contracts.

HST represents the optimal PST simplification measure for contractors and the entire construction industry. Compliance with one tax, essentially a larger GST, will be much easier than trying to administer two inherently different sales tax systems. The business tax savings generated by a refundable HST is an added bonus.

Significant Cost Savings for Contractors – And their Suppliers

Among the beneficiaries are manufacturers, wholesalers, exporters and most commercial enterprises whose costs will decrease by the amount of unrecoverable PST presently paid.

The construction industry will be the single biggest beneficiary of the newly-refundable provincial portion of HST. BC Finance estimates that, of the \$1.9 billion of PST currently paid by businesses, the construction sector will save \$880 million, or 46% of the total expected business savings from conversion to HST!

The transportation sector will save \$210 million; Manufacturing - \$140 million; Forestry - \$140 million; Mining, oil and gas - \$80 million. These sectors are major suppliers to the construction industry. Contractors should expect, perhaps demand, that PST savings realized by these and other suppliers are passed on through lower prices.

The Effect on your Construction Industry Customers May Vary

As with any change of this magnitude, there will be winners and losers. Commercial real estate customers are the big winners as the provincial portion of HST becomes newly refundable throughout the distribution chain (e.g., forestry, manufacturing, construction) as well as on selling, purchasing and/or rental costs.

New residential developments with unit prices of \$400,000 or less will be eligible for a partial HST New Housing Rebate that theoretically will not increase the tax cost of the purchase. Even high-end homes will be eligible for some reduction of the 12% tax, up to \$20,000.

Municipalities get all the GST back, and may benefit with 100% HST rebates on infrastructure and other construction projects. Hospitals get 83% rebates while universities, colleges and schools are eligible for refunds of two-thirds of the GST that they pay. These and other public sector entities may also find that the cost of major construction projects is lower under HST.

Organizations that provide GST exempt supplies will generally experience higher costs due to the increased non-refundable taxation on expenditures such as office rent and services. Some examples are residential rental and seniors' home operators, industries serving resale homes such as home renovators and realtors, the financial services sector, and doctors and dentists.

Others who will be hurt by HST are industries where PST is currently not collectible on revenues, and the customer isn't eligible for HST refunds. Restaurateurs, for example, will see the 5% GST on their services increased to 12% overall.

Consumers worry that they will have to pay more when HST is implemented. However, the implementation of HST during recessionary times will put pressure on businesses which are competing hard for limited consumer dollars. Smart businesses will move quickly to reduce their cost structure and will pass on savings as soon as possible, to preserve their market share. Ultimately, the markets will have a greater effect on prices, including new and resale housing, renovations and commercial construction, than the harmonization of the GST and PST.

What to Do in the Meantime

Very little information has been provided at this point. Transitional rules and other specific details may be released as late as March 2010, leaving little time to prepare for HST. But you can start now. Contractors and other businesses may wish to reconsider the timing of planned expenditures, perhaps delaying a major capital outlay until July 1, 2010 when non-recoverable PST is converted to refundable HST. One-time accounting and reporting system changes are required but, once implemented, should flow seamlessly.

Contracts straddling HST implementation will require careful disclosure regarding PST vs. HST. Transitional tax adjustments, still to be announced, may be expected on construction costs subject to PST prior to July 1, 2010, where the sale closes on or after July 1, 2010.

Please contact the writer if you have any questions or comments. I would appreciate your feedback, both positive and negative, so that we can share experiences throughout the various phases of HST implementation. Let me know if you would like to receive a free email-based update on HST and other relevant tax issues as new information becomes available.

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Carl Beck has extensive experience advising clients during sales tax transitions, having been directly involved in the implementation of GST in 1991, Quebec Sales Tax (QST) in 1995 and HST in the Maritimes in 1997. During the implementation of GST, Carl Beck worked as a Senior Policy Officer in CRA's HQ Real Property Unit where he was able to monitor and resolve many of the transitional complexities as the construction sector moved from an embedded Federal Sales Tax in material costs to a generally-refundable GST on value added components.