

Association of Registered Graphic Designers - Ontario

Let's Talk About HST

Lang Michener LLP

Lawyers - Patent & Trade Mark Agents

INTERNATIONAL TRADE



Presented by:

Cyndee Todgham Cherniak,
Sales Tax Counsel

Lang Michener LLP

Toronto

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CAVEAT

- This presentation does not constitute legal advice. This presentation is developed to provide guidance. However, many issues relating to the graphic design industry have not been considered by the Canada Revenue Agency at the time of the presentation. The Canada Revenue Agency has not provided guidance on many of the matters raised herein. The contents herein point out issues. Specific questions must be referred to legal counsel or the Canada Revenue Agency at such time all the relevant facts should be discussed and considered.

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Harmonized Sales Tax

- July 1, 2010, Ontario and British Columbia harmonized provincial sales taxes with GST
- Major tax reform
- HST Rates
 - Ontario $5\% + 8\% = 13\%$
 - British Columbia $5\% + 7\% = 12\%$
 - New Brunswick/Newfoundland/Labrador $5\% + 8\% = 13\%$
 - Nova Scotia $5\% + 8\% + 2\% = 15\%$
 - Alberta $5\% + 0\% = 5\%$



The Basics – Ontario HST

Pre-OHST

- GST = 5%
- GST payable on most property and services
- ORST = 8%/5%/10%
- ORST was payable on most goods
- ORST was payable on a limited number of “taxable services”
- ORST was not payable on real property
- ORST was not payable on intangible property
- Complicated rules for graphic designers

Post OHST

- HST = 5% GST + 8% OHST
- HST has same tax base as GST (few point of sale rebates)
- Real property, intangible property, intellectual property and many services are subject to HST
- Businesses engaged in commercial activities entitled to input tax credits - EXCEPT RITCs
- Restricted input tax credits (RITCs) on certain inputs
- Electronic reporting
- Complicated rules for graphic designers (maybe worse)

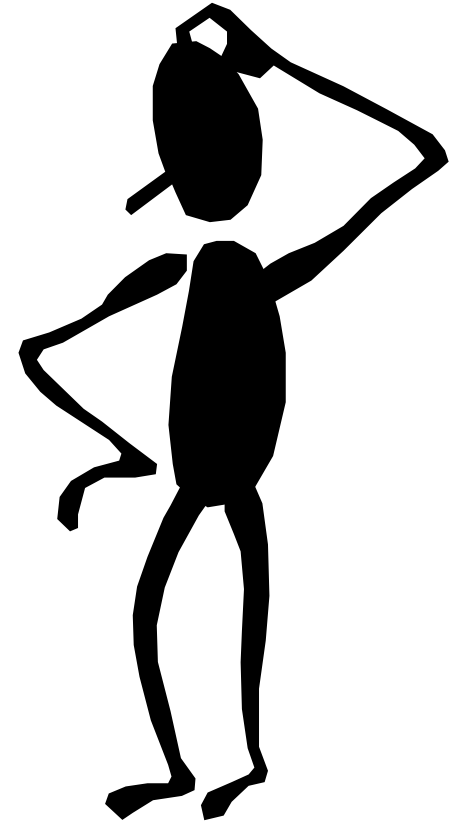
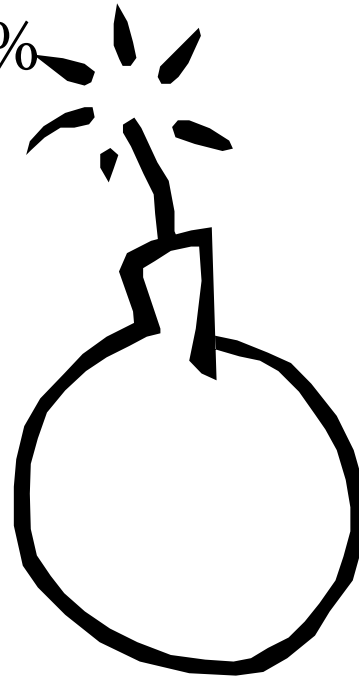


HST: Why does it matter? Some clients/customers are not able to recover GST/HST

- If a client is engaged in commercial activities, they should be entitled to recover GST and HST paid in connection with graphic design services
- Some clients who may not be able to recover GST/HST:
 - individuals
 - charities and not-for-profits
 - banks, financial institutions, insurance companies
 - *de minimis* financial institutions (e.g. certain holding companies)
 - municipalities
 - schools, school authorities, colleges, universities
 - day cares
 - nursing homes, retirement homes
 - hospitals
 - doctors and health care professionals
 - residential builders

HST: Why does it matter?

- Mistakes are costly
- 5% mistakes can now be 13%
- 5% mistakes can now be 15%
- 4 year audit period
- Plus penalties
- Plus interest
- Short time to pay



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First step in any HST analysis: Characterization of supply

- Major issue for Graphic Design Industry – not one size fits all
- HST transition rules and place of supply rules are many & depend upon characterization of supply
 - Is it property or a service?
 - Is it intangible property or a service?
 - Is it tangible personal property (TPP) or a service in respect of TPP?
 - Is it real property or a service in respect of real property?
 - Is it labour of an employee or independent contractor?
 - Is it real property, TPP or intangible property?



Single vs Multiple Supplies

- Significant issue for some graphic design projects & not given much consideration/guidance yet
- **What is the predominant supply?**
- Is there one or more different supplies?
- **Ask:** Am I making a single supply of a graphic design service or multiple supplies of property and services?
- Ask this question on a:
 - Supply by supply basis
 - On a client matter by client matter basis
 - A bill by bill basis

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Single vs Multiple Supplies (Cont'd)

- The single vs multiple supply analysis comes from the GST/HST legislation, case law and administrative policies of the Canada Revenue Agency
- Based on a determination of fact
 1. Should every element be regarded as distinct and independent
 2. A supply that is a single supply from an economic point of view should not be artificially split
 3. There is a single supply where one or more elements constitute the supply and any remaining elements serve only to enhance the supply
- If you make your client aware of the different elements of your work, you may have multiple supplies
- **Key: Can the client purchase different elements separately?**

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Characterization of Supply

- Pre-HST complexities continue
- Pre-concept approval may have one characterization
- Post-concept approval may have another characterization
- Characterization may affect applicable HST rate

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Characterization of supply

Packaging	General services Services re IP Services re TPP	IP if produce design/artwork/file TPP if produce package
Environmental /Architectural GD Exhibit GD	General Services Services re RP	real property elements
Branding, logos, identity Corporate communications GD	General Services Services re TPP Services re IP	IP if produce design/trademark & send electronically TPP if produce tangible goods
Web Design	General Services Services re IP	IP maintenance contracts – services or IPP
Advertising	General Services	Services in respect of IP IP
Editorial GD	General Services	IP TPP if produce magazine/item

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Example #1

- Graphic designer agrees to design and create business cards for a client with offices across Canada.
- Two phases:
 1. Pre-concept approval: strategic planning and design development: May be considered to be a service or a service in respect of tangible personal property
 2. Printing and delivering business cards: Would be considered to be tangible personal property



Example #2

- Graphic designer agrees to design logo for a client with offices across Canada.
- Two phases:
 1. Pre-concept approval: strategic planning and design development: May be considered to be a general service or service in respect of intangible property
 2. Logo: Likely considered to be intangible property



Second step in any HST analysis: Determine tax status of supply

- Four types of supplies
 1. Taxable supplies
 2. Zero Rated supplies
 - Export Transactions (often determination of residency status of recipient is required)
 - Domestic Transactions
 3. Exempt supplies
 4. Non-taxable importations



Third Step: Apply HST Transition Rules

- Remember to charge GST
- HST Transition Rules are **HST TIMING RULES**
- Application of the HST transition rules depends upon the characterization of the supply (TPP, real property, intangible property or service)
- There are HST transition rules for each general characterization
- There are specific HST transition rules for services: memberships, passenger and freight transportation services, commercial parking, subscriptions to newspapers and magazines, prepaid funeral and cemetery services, direct sellers, continuous supplies, imported goods



HST Transition Rules: Services

- **General Rule:** HST applies to all supplies made on or after July 1, 2010
- **General Rule:** If a supplier enters into a contract to provide property/services AND is paid after May 1, 2010 AND the property/services are rendered on or after July 1, 2010, then OHST is payable
- **Exception:** To the extent that all or substantially all (90% or more) of the property is provided or services are completed before July 1, 2010, OHST will not be payable on the portion of the property/services provided after July 1, 2010



HST Transition Rules: Services (cont'd)

- **General Rule:** HST applies to provisions of property/ services that commence before July 1, 2010 and end after July 1, 2010: allocation is necessary



Example #3

- A company in Ontario provides services to clients and bills the clients in advance for services to be rendered in the following month. ABC Co. sends out bills in May/June 2010 for services to be rendered on or after July 2010
- ABC Co. **must charge HST** (depending on the HST place of supply rules) with respect to services to be delivered on or after July 1, 2010



Example #4

- A company in Ontario takes on a new client in May 2010 and indicates that the services will be provided after July 1, 2010
- ABC Co. **must charge HST** (depending on the HST place of supply rules) with respect to services to be delivered on or after July 1, 2010



Example #5

- A company in Ontario takes on a new client in May 2010 and indicates that the services will be provided between May 2010 and September 2010
- ABC Co. should issue an invoice on June 30, 2010 with respect to any services rendered before July 1, 2010. HST is not payable on services performed prior to July 1, 2010
- ABC Co. **must charge HST** (depending on the HST place of supply rules) with respect to services delivered on or after July 1, 2010 (unless 90% of the services are delivered pre-July 1, 2010)
- Consider multiple service contracts for MUSH/exempt sector clients



Fourth Step: Apply HST Place of Supply Rules

- 4 types of place of supply rules:
 1. Goods
 2. Services
 3. Intangible Property
 4. Real Property

HST Place of Supply Rules: General Rule

- Easy for large # of graphic designers
- If supply goods or services
- If supply ON real property
- If clients only in Ontario / local
- Charge 13% HST



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HST Place of Supply Rules: General Rule

- If supply intangible property/services re IP
- If clients (of TPP, services, IP) located outside Ontario
- If clients have many locations including Ontario
- More difficult



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HST Place of Supply Rules for Goods

- **Who Must Apply Rules:** Graphic designers who are delivering a good
- **Key Question:** Where is the good delivered/shipped to?
- **HST Place of Supply Rule #1a:** HST applies to a good if it is delivered to an address in an HST province
- If the supplier ships the goods to a destination in an HST province, then HST applies (destination is specified in a contract for carriage or transfers possession to courier that the supplier has retained on behalf of the buyer/client)



HST Place of Supply Rules for Goods (Cont.)

- **HST Place of Supply Rule #1b:** HST applies to a good if it is sent by mail or courier to an address in an HST province
- **HST Place of Supply Rule #2:** HST does not apply to a good if it is delivered to an address outside the HST Zone



HST Place of Supply Rules for Goods – NOTE OF ISSUE

- Undetermined issue: Whether must divide project into two parts (2 different place of supply rules may apply):
 1. Service Component
 2. Goods Component
- Billing Strategy: If one client who provides instructions from location to which goods are shipped, then charge that HST rate on all goods and services
- If ship goods to location different than the location of person who provides instructions, seek guidance

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Example #6

- A client/customer located in Ontario hires a graphic designer to design and produce 100 business cards and send by courier to an address in Ontario
- HST applies at a rate of 13%
- Graphic designer **must charge HST** with respect to goods delivered on or after July 1, 2010
- If services pre-July 1, 2010 and goods delivered after July 1, 2010, may want to bill for pre-July 1, 2010 services – see transition rules

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Example #7

- A client/customer located in Ontario hires a graphic designer to design and produce a booth for a trade show to be shipped to location in Michigan
- GST/HST does not apply if graphic designer arranges for the shipping and maintains proof of export in records



HST Place of Supply Rules for Services

- 2 types of HST place of supply rules for services
 1. General
 2. Specific
 - services in relation to real property (e.g., design way finding)
 - services in relation to intangible property (e.g., designing a trade mark)
 - computer-related services and Internet access
 - telecommunication services
 - premium rate telephone services
 - services in relation to tangible personal property
 - services in relation to a location specific event (e.g., participation in a conference)
 - postage and delivery services
 - repairs, maintenance, cleaning, alterations and other services relating to goods



Specific: HST Place of Supply Rules: Services In Respect of Real Property

- **Who Must Apply Rules:** Architectural graphic designers & exhibit graphic designers
- **Key Question:** Where is the real property located?
- **HST Place of Supply Rule #1a:** HST applies to a service in respect of real property if the real property is located in an HST province
- **HST Place of Supply Rule #1b:** HST does not apply to a service in respect of real property if the real property is located in outside HST Zone (e.g. in Alberta)
- **HST Place of Supply Rule #2** (more than one property): HST applies to a service in respect of real property if the real property is situated in Canada & primarily (50%) in the HST province

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Specific: HST Place of Supply Rules: Services In Respect of Real Property (Cont'd)

- **HST Place of Supply Rule #3 (more than one province):** HST applies to a service in respect of real property if the real property is situated in Canada & in more than one HST province at the rate where the greatest proportion of the property is located
- **HST Place of Supply Rule #4 (more than one property):** If Rule #3 does not apply, HST applies to a service in respect of real property if the real property is in HST provinces at the highest rate of the provinces in which the real property is located

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Specific: HST Place of Supply Rules: Services In Respect of Tangible Personal Property

- **Who Must Apply Rules:** If deliverables are the goods: Brand graphic designer, packaging graphic designers
- **Key Question:** Where is the TPP located
- **HST Place of Supply Rule #1a:** HST applies to a service in respect of TPP if the TPP is located in an HST province at the time the service is being performed

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General HST Place of Supply Rule for Services

- **General Services Place of Supply Rules**

Rule #1(a): A supply of a service is made in an HST province if, **in the normal course of business**, the supplier obtains **a single address of the recipient in the HST province** that is a home or business address in Canada of the recipient

A supply of a service is not made in an HST province if, **in the normal course of business**, the supplier obtains **a single address of the recipient outside the HST Zone** that is a home or business address in Canada of the recipient



General HST Place of Supply Rule for Services (cont'd)

- **General Services Place of Supply Rules**

Rule #1(b): If a supply of a service is made in an HST province and if, in the normal course of business, the supplier obtains **more than one business and/or home address of the recipient**, the address for the HST purposes is the address **most closely connected with the supply of the service**

- If the address **most closely connected** to the supply of the service is in the HST Zone, then HST applies
- If the address **most closely connected** to the supply of the service is outside the HST Zone, then HST does not apply



General HST Place of Supply Rule for Services (cont'd)

- **General Services Place of Supply Rules**
- Rule #1(c): If a supply of a service is made in an HST province and if, in the normal course of business, **the supplier does not obtain a business or home address of the recipient in Canada**, the address for the HST purposes is the address **most closely connected with the supply of the service**
 - If the address **most closely connected** to the supply of the service is in the HST Zone, then HST applies
 - If the address **most closely connected** to the supply of the service is outside the HST Zone, then HST does not apply



General HST Place of Supply Rule for Services (cont'd)

- Canada Revenue Agency is concerned about avoidance
- Canada Revenue Agency is talking about interpretation of the phrase **most closely connected with the supply**
- Will look at the following **in order**:
 - The business address of the recipient/client where the supplier has the most contact with during the course of the provision of services
 - The business address of the recipient/client from where the supplier was hired
 - The business address of the recipient/client to which the invoice is sent (“billing address”)



General HST Place of Supply Rule for Services (cont'd)

- Rule #2: A supply of a service is made in an HST province if (a) the Canadian element of the service is performed by the supplier primarily (50% or more) in the HST Zone
 - The applicable HST rate is the rate of the HST province in which the greatest proportion of the services are performed



General HST Place of Supply Rule for Services (cont'd)

- Rule #3: If (a) Rule #2 applies (i.e., do not obtain address in Canada of the recipient AND the service performed in Canada is performed primarily in HST provinces), AND (b) **a single HST province cannot be determined** as being the HST province in which the greatest proportion of the service is performed because the service is performed equally in two or more HST provinces, then the supply will be regarded as made **in the HST province for which the rate of the provincial component of HST is highest**
 - Example: 50% of services in BC and 50% in Ontario, then Ontario's 13% HST rate applies



General HST Place of Supply Rule for Services (cont'd)

- Tie Breaker Rule
- Rule #4(a): If Rule 3 applies, **but a single participating province still cannot be determined** to be the place of supply because the particular rate of the provincial component of the HST in two or more of the particular participating provinces is the same (e.g., Ontario and Newfoundland), the supply is made in the HST province where the business address of the supplier is most closely connected is located (e.g., Lang Michener Toronto address – OHST applies)
- Rule #4(b): If the supplier's business address is not located in one of the two HST provinces, the default is the province in closest proximity to the supplier (determined in a reasonable manner) that is most closely connected to the supply



General HST Place of Supply Rule for Services (cont'd)

- Rule #5: A supply of a service is made outside the HST Zone if (a) the Canadian element of the service is performed by the supplier primarily (50% or more) outside the HST Zone
 - Example 1: 50% or more of the services are performed in Saskatchewan
 - Example 2: 35% of the services are performed in Saskatchewan and 40% in Manitoba and 25% in Ontario
 - HST does not apply



Tips: HST Place of Supply Rules for Service Providers: Non-residents of Canada

- Ask if client is a resident or a non-resident
 - If non-resident, possibly zero-rated
 - If resident, apply HST place of supply rules
- If did not previously charge GST probably (but, not always the case) do not charge HST
- Need to satisfy self that client/customer is a non-resident



HST Place of Supply Rules for Intangible Personal Property

- **Who Must Apply Rules:** Web-designers
- **Key Question:** Where is the intangible property to be used?
- **HST Place of Supply Rule #1a:** HST applies to a supply of IPP in respect of which the Canadian rights can be used primarily (50% or more) in HST Zone
 - If contract restricts to one HST province, HST rate = rate for that province (e.g. Ontario = 13%)
 - If contract restricts to one non-HST province, GST, but no HST (Alberta = 5% GST)

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HST Place of Supply Rules for Intangible Personal Property

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HST Place of Supply Rules for Intangible Personal Property (Cont'd)

- **If contract relates to all of Canada, then determination of place of supply is more complicated**
 - If contract value is \$300 or less, HST is applied based on the location of the supplier if the supply is made in the presence of an individual acting on behalf of buyer (e.g. web-design)
 - If contract relates 50% or more to HST Zone provinces, the supply is proposed to be made in the HST province in which where the greatest proportion of rights may be used
 - If a specified number of users, determine HST status based on location of users

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HST Place of Supply Rules for Intangible Personal Property (Cont'd)

- If contract value exceeds \$300 & IPP can be used in HST Zone, the supply is made in a HST province if in the normal course of business of the supplier, the supplier obtains a home or business address of the recipient that is in an HST province
- If contract value exceeds \$300 & IPP can be used in HST Zone, the supply is made in a HST province if the supplier obtains more than one home or business address of the recipient in HST provinces – must select the **address most closely connected with** the supply (e.g., the location of the individuals who provide instructions (see general services place of supply rules))

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HST Place of Supply Rules for Intangible Personal Property (Cont'd)

- If the IPP can be used primarily in HST provinces, but an exact location of the recipient is not provided, then the highest HST rate would apply
 - At the present time, the highest HST rate is re Nova Scotia = 15%
 - Note: Nova Scotia's rate would not apply if cannot use IP in Nova Scotia
 - A CRA auditor may take the position that a web-site that may be accessed in Nova Scotia can be used in Nova Scotia

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Example #9

- Graphic designer in Ontario designs a web-site for a company located in Ontario. The web-design/software is downloaded electronically and the license provides that the web-design may only be used on Ontario
- The only business address obtained by the graphic designer is the Ontario address of the recipient
- HST at the rate of 13% would apply



Example #10 (From CRA Slides)

- A supplier in Ontario makes supplies of subscriptions to its Web site & provides subscribers with the right to access & use digitized content & to download a copy of the digitized content. There are no restrictions with respect to where the subscribers may use the IPP
- Where the home address of the subscriber is outside Canada – CRA recommends that the supplier charge 15% HST unless the supply qualifies for zero-rating (because the IPP can be used across Canada and N.S. has 15% rate)

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Example #11 (From CRA slide)

- A supplier in Ontario supplies software by way of a license to a company in Ontario for use by employees at its offices throughout Canada. The software is downloaded electronically over the Internet. There are no restrictions with respect to where the software may be used. The only business address of the recipient obtained by the supplier with respect to the supply of the software is in Ontario
- The supply of the IPP is made in Ontario and is subject to HST at the rate of 13%

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Temporary Restrictions in Claiming ITCs (RITCs) for Large Businesses

- Large businesses & financial institutions are **NOT ALLOWED** to claim ITCs (on HST portion) between July 1, 2010 – June 30, 2015 on purchases of:
 - Energy (except where purchased by farms or used to produce goods for sale)
 - Telecommunications services (other than internet access fees or charges for toll-free numbers)
 - Automobiles and certain other road vehicles and fuel to power
 - Food, beverages and entertainment expenses



Temporary Restrictions in Claiming ITCs (RITCs) for Large Businesses (cont'd)

- Phase-out (January 1, 2010- June 30, 2015 = 100% restricted)
 - July 1, 2015 – June 30, 2016 = 75% restricted
 - July 1, 2016 – June 30, 2017 = 50% restricted
 - July 1, 2017 – June 30, 2018 = 25% restricted
 - July 1, 2018 = ITCs on HST component fully available (unless gov't changes)
- Large businesses = those businesses with greater than \$10 Million in taxable supplies made in Canada
 - Public service bodies are not to be considered large businesses
- Applies even if business does not have a PE in the particular province
- Threshold is applied on an associated group basis



Tips for CRA Audit Risk Management

- Consider appropriate method to maintain **EVIDENCE**:
 - Dockets / time sheets / recording of time spent
 - Employee punch cards / electronic records
 - Outlook calendar printouts
 - Employee work schedules
 - Purchase receipts
 - Sales receipts
 - Sales invoices
 - Shipping documents – matched to invoices
 - Airline tickets & boarding cards
 - Photocopies of cheques / proofs of date of payment

Slide 52

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Basic Sample File Opening Form

- Name of Client/Customer:
- Name of Contact Person:
- Telephone Number of Contact Person:
- Location of Contact Person:
- Address of Client/Customer:
- Location to which goods will be shipped:
- Type of graphic design services to be rendered:
- Will approvals be required (Circle One): Yes No
- Date (s) of approval(s):
- Deliverables discussed at time of file opening:

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Additional Issues

1. Refunds of ORST paid on computer programs and leased equipment pre-HST where lease period extends into post-HST
2. Billing disbursements to clients/customers
3. Filing of final ORST returns
4. Expect ORST audits before March 2012
5. Making sure systems record GST/HST
6. Filing GST/HST returns electronically

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Contact Details:

Cyndee Todgham Cherniak

Lang Michener LLP

Brookfield Place

181 Bay Street, Suite 2500

P.O. Box 747

Toronto, Ontario M5J 2T7 CANADA

Phone: 416-607-7089

Fax: 416-607-7085

Email: cyndee@langmichener.ca

Web-sites: www.langmichener.ca

www.thehstblog.com

Follow of Twitter: [@CyndeeLaw](https://twitter.com/CyndeeLaw)

