

Getting Ready for Sales Tax Harmonization in Ontario and British Columbia

REALTORS® need to get ready for Ontario's and British Columbia's (BC) new harmonized sales tax (HST). Although the changes will take effect on July 1, 2010, the time to start preparing is now. In fact, the HST will impact certain current agreements, such as purchase and sale agreements for new homes that close on or after July 1, 2010. In addition, REALTORS® will need to take into account the application of HST to their services to be performed on or after July 1, 2010.

Background

The Ontario Government announced in its 2009 budget that it intends to harmonize its 8 percent provincial sales tax (PST) with the 5 percent federal Goods and Services Tax (GST) to create a 13 percent HST on most GST-taxable goods and services provided in Ontario. The BC government announced on July 23, 2009 that BC would harmonize its 7 percent PST with the GST to create a 12 percent HST on most GST-taxable goods and services provided in BC.

The HSTs will generally apply to the same tax base as the GST, with some exceptions. The HST will be federally administered by the Canada Revenue Agency (CRA). GST/HST registered businesses will only be required to file one GST/HST return and there will be one audit.

How will Sales Tax Harmonization Affect REALTORS®?

The sales tax treatment of GST registered REALTORS® services will change. GST registered REALTORS® will be automatically registered for the HST. Rather than REALTORS® commissions being subject to GST at the rate of 5 percent, REALTORS® commissions for services in Ontario and British Columbia will generally be subject to HST at the rates of 13 and 12 percent respectively.

In addition, REALTORS® will pay the Ontario and British Columbia HST on most of their costs, such as office leases, office supplies, and equipment such as computers and software. Some of these costs, such as the lease of office space, were previously only subject to GST.

Although REALTORS® will pay more sales tax as a result of a broader taxable base of goods and services, REALTORS® will generally be able to recover the HST they pay by claiming input tax credits (ITCs). REALTORS® will no longer have to pay unrecoverable PST on purchases consumed in providing their services. In terms of the overall impact of harmonization on a REALTORS'® costs, there should be a net benefit.

When will the HST Apply to REALTORS® Services?

As mentioned, HST will generally apply to the same tax base as the current HST. Also, GST registered REALTORS® will be automatically registered for the HST. As a result, REALTORS® will apply HST to the fees for their services that are currently subject to GST.

Still, GST/HST registered REALTORS® will need to take into account the province in which their services are performed and the timing of their services during the transitional period for purposes of determining whether GST or HST applies.

Place of Supply

At the date of writing this article, Ontario and BC have not published the technical rules explaining how a GST/HST registrant is to determine if a good or service is supplied in or outside Ontario or BC. However, based on the rules that were implemented for sales tax harmonization in Quebec and BC, we can make some reasonable assumptions about how the place of supply of REALTORS® services will be determined for Ontario and BC HST purposes.

The HST will likely apply to REALTORS® services based on the location of the real property to which the REALTORS® services relate. For example, Ontario HST will apply to a REALTORS® commission for services in respect of a house sale in Ottawa, Ontario.

Transitional Rules

Ontario and BC recently released general transitional rules for the HST. These rules explain how HST will apply to transactions that straddle the start-up date. For purposes of the following discussion, it is assumed that a REALTORS® commission becomes due or is paid when the property is sold or leased.

The HST would generally apply to REALTORS® services to the extent, expressed as a percentage, that the services are performed on or after July 1, 2010. However, if 90 percent or more of the services are performed before July 1, 2010, the HST will not apply.

For example, a REALTORS® services are performed from June 1, 2010 to July 2, 2010 with the sale of the property closing on July 2, 2010. The REALTORS® commission becomes due at that time of closing. More than 90 percent of the REALTORS® services were performed before July 1, 2010. In these circumstances, the GST at the rate of 5 percent will apply to the REALTORS® services.

In another example, a REALTORS® services are performed from May 1, 2010 to July 31, 2010 with the sale of the property closing on July 31, 2010. The REALTORS® commission becomes due at that time. In this case, two thirds of the services were

performed from May 1, 2010 to June 30, 2010 and one third of the services were performed from July 1, 2010 to July 31, 2010. The REALTORS® will charge GST on two thirds of the amount charged for the services and HST on the remaining third.

Will REALTORS® Recover the HST they Pay on their Costs?

REALTORS® will generally be able to claim ITCs for the HST on their purchases on the same basis as the current GST system.

However, large businesses (with annual taxable sales exceeding \$10 million) will be unable to claim ITCs for the provincial portion of the HST related to:

- energy (except where used to produce goods for sale);
- telecommunication services, except internet access and toll-free numbers;
- road vehicles weighing less than 3,000 kilograms, including fuel and certain parts; and
- meals, beverages, and entertainment.

After the first five years of HST implementation, full ITCs on taxable purchases made by large businesses will be phased in over three years.

Certain REALTORS®, with total annual revenues (including GST/HST) of \$200,000 or less, may be using a simplified method to calculate their net tax payable; the Quick Method. There are special rules that may require REALTORS® using the Quick Method to self-assess the provincial component of the HST when prepaying for property or services after October 14, 2009 and before May 2010. REALTORS® using the Quick Method should be aware of these rules and seek guidance if any prepayments are made during this time period.

REALTORS® in non-HST provinces, such as Alberta, Saskatchewan, Manitoba, and Prince Edward Island, will also be entitled to claim ITCs for HST incurred on purchases in an HST province. However, the ITCs would remain subject to the restrictions for large businesses.

What is the Impact of HST on Real Estate Transactions?

The HST treatment of real estate transactions will generally follow the current GST treatment of real estate transactions. Sales of used residential housing and long-term rentals of residential housing will be exempt for HST purposes. Sales of new residential housing will be subject to HST and will qualify for GST, HST, and transitional rebates (subject to certain thresholds and maximum amounts). Sales and rentals of commercial real property will be subject to HST.

What do REALTORS® Need to Begin Thinking About in Order to be Ready?

REALTORS® should begin to prepare now in order to be ready. For example, the following items may be affected by harmonization:

- the tax clauses of real estate listing agreements, co-operating broker/agent agreements and other sales and/or purchase agreements;
- sales and receivable systems;
- purchasing and payable systems;
- expense reports;
- Quick Method GST/HST calculations.

REALTORS® should also consider a strategy for communicating with clients and future clients on the impact of harmonization. Finally, REALTORS® should plan for significant purchases during transition to reduce unrecoverable sales tax (e.g., deferring PST taxable purchases).

The information in this article is based on notices released by the tax authorities to October 21, 2009. The legislation relating to sales tax harmonization has not been released and the rules discussed above are not complete. As such, the rules are subject to change.

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