

HST – PROCUREMENT AND SUPPLY ISSUES FOR MUNICIPALITIES

By Bruce E. Ratford, CMA, CMM III

The previous HST newsletters looked at various issues relating to the change-over to the Harmonized Sales Tax in Ontario, as of July 1, 2010. These were written to address primarily the concerns and needs of municipal finance and accounting staff. This newsletter is in response to a number of requests that we address the concerns of purchasing officers and agents, and of staff who are running business operations.

The author would like to thank the various purchasing officers who have provided considerable input into this newsletter, particularly in articulating the issues that should be addressed. We have tried to take care of them all, and it is hoped that you will find answers to your questions here, or in the previous newsletters, or at least some guidance as to how to deal with HST-related issues that you may encounter. The ideas and advice presented here are for assistance and guidance only. You should consult legal or accounting experts on HST for advice on specific matters.

The newsletter comprises the following sections:

- Brief overview of what is happening on July 1, 2010
- How HST works compared to Retail Sales Tax
- Public Sector Bodies' Rebates
- Supply side - invoicing and the collection of HST
- Strategic procurement
- Contracts straddling both tax regimes
- The point of supply issue
- Embedded RST and potential double taxation
- Transition rules
- Some special cases
- Other resources
- Frequently asked questions

What is happening July 1, 2010?

A CRA information sheet that was included with the December 31, 2009 GST return (09-114) describes what will be happening on July 1, 2010:

“..... The Government of Canada and the provinces of Ontario and British Columbia have signed Memoranda of Agreement that provide the framework for introducing the Harmonized Sales Tax (HST) in Ontario and B.C. The HST is proposed to come into effect in these provinces on July 1, 2010, at a rate of 13% in Ontario and 12% in B.C. The HST will use the same tax base and structure as the GST, with some exceptions.”

The two provinces have signed tax collection agreements with the Federal Government, which effectively uploads sales tax collection on behalf of the province to the Canada Revenue Agency. Please note that **sales tax collection on behalf of the province will henceforth use the same tax base and structure as the current GST**. There are only a very small number of exceptions.

Except for the specific Ontario provisions (effectively six in total), **the tax treatment for any transaction under HST will be exactly the same as it is now for GST. In spirit and in essence, HST is simply a value-added tax (VAT), the same as GST, for the two separate jurisdictions at a consolidated rate of 13%**. Generally, whatever happens now with GST – is the rate 5% or 0%? – will happen under HST, at a rate of 13% or 0% respectively.

As of June 30, 2010, the Ontario Retail Sales Tax, with all its current terms, provisions and exemptions will no longer be applicable to any sales transactions occurring after that date, save and except for insurance premiums and the private sale of used vehicles. Note that the specific Ontario provisions in the implementation of HST, including provision for point-of-sale rebates on certain purchases, have been legislated as an amendment to the [Ontario Retail Sales Tax Act](#), which at the same time effectively makes large parts of the Act inoperative.

HST (or a value-added tax) versus a Retail Sales Tax

The following chart, provided by the Ontario Ministry of Finance, illustrates well the difference between the current Retail Sales Tax (RST) and a value-added tax (VAT), which is what GST and HST are.

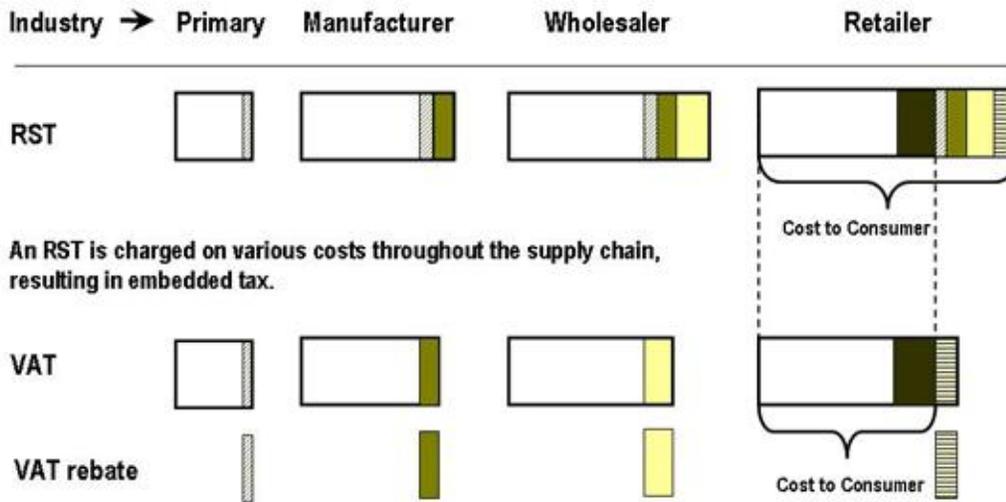
Note the concept of embedded tax that occurs in every step of the supply chain under the Retail Sales Tax. One example of this would be the RST paid on goods and services purchased for consumption by the organization, such as telephone services or office supplies. Another would be those municipal contracts where the contractor is deemed to be the end-user for RST purposes, consuming the supplies in executing the contract for the municipality, and including the RST paid on the supplies in the final cost charged to the municipality. By contrast, only the end consumer pays VAT, on the actual cost of the good or service, because all VAT or GST/HST paid by intermediates is refunded as an Input Tax Credit (ITC). Each party charges VAT on goods and services provided, which in turn is claimed as an ITC by the next party in the supply chain.

A major issue thus becomes what happens to that embedded RST, when you have fixed-price agreements extending past June 30, 2010, or are entering into a contract now, that will extend past June 30, 2010. How can you benefit from the savings?

See Chart 2 on the following page.

VAT Lowers Costs

Chart 2



An RST is charged on various costs throughout the supply chain, resulting in embedded tax.

VAT

VAT rebate

A VAT is rebated at each stage of the supply chain, eliminating the embedded tax.

Note: Illustrative example only. Not to scale.

Public Sector Bodies' Rebates

It is easy to see that after June 30, 2010, bidding and pricing will be on the basis of supplier cost plus 13% HST, whether you are purchasing or supplying a good or service.

Commercial enterprises can claim back the full amount of HST paid as an ITC, for both the Federal and Provincial portions. For your golf courses, restaurants, and tourist attractions that charge admissions, HST paid on supplies acquired for providing those services can be claimed back in full, if deemed to be commercial operations or activities for tax purposes.

For municipal activities, and associated activities such as the tax-exempt activities listed in the next section, your municipality can claim the Federal and the Provincial Public Sector Bodies' (PSB) rebate on all transactions. The Federal PSB rebate is now 100% of the Federal GST/HST paid, or 5%. This is effectively the same as an ITC, so that there is no net tax cost. The Provincial PSB rebate for municipalities will be 78% of the Provincial portion of HST, that is, 78% of 8%, or a net of 6.24%. The remaining 1.76% will be an expense to your municipality, just as RST is now. Thus if you are encumbering your purchase order, you should be using an amount that is 101.76% of the supplier price to reflect the actual cost of the transaction to your municipality.

Supply side - invoicing and the collection of HST

Canada Revenue Agency (CRA) will deem HST to be collected on a transaction and the amount involved to be payable to the Receiver-General of Canada in full, whether you invoiced your client and collected the amount or not. **When in doubt, charge HST**, and have the client demonstrate why the transaction should not be taxed. Otherwise, be prepared to expense the HST payable, if CRA deems the supply to be taxable.

As is the case for GST, you must show your municipality's HST registration number on all invoices or billing slips. **Your HST registration number will be exactly the same as your current GST number.** Your RST Vendor Number will lapse, unless you provide insurance services to clients, in which case you will still be collecting 8% RST on the premiums, and remitting the money collected to the Ontario Ministry of Revenue, as you do now.

The following is a quick overview of **when HST is not levied**. Zero-rated goods and services for which the HST rate is 0%, and is not levied, include:

- medical devices
- basic groceries
- agricultural and fish products
- prescription drugs
- exports to outside of Canada

Suppliers of these items can claim ITCs or PSB rebates on supplies bought.

Tax-exempt supplies are exempted from HST, so that there is no sales tax levied on services or supplies such as:

- rentals of residential housing for a term of longer than one calendar month
- most educational services
- most health care services
- day care services
- legal aid services
- financial services, such as insurance, and
- some supplies by charities and public sector bodies

Suppliers of these items **cannot** claim ITCs or PSB rebates on supplies bought.

Note that specified tax-exempt supplies made or provided by municipalities are exempt from HST, such as:

- inter and intra municipal supplies
- library services
- law enforcement and fire protection services
- non-optional services provided to a property owner, e.g. street lighting
- municipal water and sewer systems and services
- garbage collection, including recyclables
- municipal transit, including special needs transit services
- homemaker services
- property registration
- court registration
- licenses and permits
- provision of information or documents under the Privacy Act or Municipal Freedom of Information and Protection of Privacy Act (MFIPPA)
- unbottled water
- ferry, road and bridge tolls
- admission tickets to amateur performances and events
- recreational programs for children under 14, or to under-privileged or disabled individuals
- relief of poverty suffering or distress

- charitable events organized by a municipal agency, board or commission
- work on street lights, signs, barriers, traffic lights or similar property
- removal of snow, ice or water
- managing vegetation
- repairing and maintaining street, sidewalks, or similar or adjacent property
- installing accesses and egresses, such as curb cuts, and
- **variations and permutations of the above, unless specifically taxable.**

Note that for the last two lists, you will not be charging clients HST, but that your municipality can claim the PSB rebates on HST paid on acquisitions to supply these goods and services, as long as the activity is deemed to be a municipal activity or an activity associated with your municipality.

Also note that for all invoicing for goods and services provided after June 30, 2010, you will simply delete GST and RST from invoices and replace them with the single HST. In POS systems and cash registers, “tax #1” will be changed to 13% (or 0.13), and “tax #2” will be set to zero, or to minus 8% (or -0.08), if POS rebates are to be provided. These are discussed in the section Special Issues.

More complete documentation of the information presented in this section can be found in CRA publication [RC4049 - GST/HST Information for Municipalities](#).

Strategic procurement

Strategic procurement is planning your acquisitions to take advantage of the potential benefits from the difference in how the two tax regimes work. Some acquisitions such as professional services and fire engines are not currently subject to RST, but will be subject to HST at 13%. RST is not refunded, whereas HST can be claimed back, in full or at least 11.24% of the 13% paid.

For acquisitions not currently subject to RST, endeavour to have as much of the work done before June 30, 2010, and insist that all billable work completed before July 1, 2010, be invoiced in full in July, on an invoice dated June 30, 2010 or earlier. In the case of the fire engine, take possession of it before July 1, 2010, by being invoiced before July 1, 2010, as long as it is substantially completed.

Conversely, for acquisitions currently subject to RST, postpone them until after June 30, 2010, so that they become subject to HST instead. For supplies, buy sufficient to last to June 30 or to July 15th, and restock in July. Later would be better, to be better positioned to take advantage of the elimination of embedded RST in supplier pricing.

Examples of the types of items this would apply to would be:

- Motor vehicles
- Office supplies
- Computer hardware and software
- Utility poles and street lamps
- Building, electrical and plumbing supplies
- Office furniture
- Plants
- Etc.

For major items, the latter may not be a real consideration, as the order would have been priced under the current tax regime, and the item built using current pricing. However, postponing delivery and taking possession until after June 30, 2010 means that your municipality will be taxed under HST and the HST can be claimed back in whole or in part as ITCs

or as PSB rebates, as the case may be. Take delivery on June 30, 2010, and your municipality has a total net cost of supplier cost plus 8% RST.

Contracts straddling both tax regimes

This is probably the purchasing officer's biggest nightmare. Bids, tenders, and contracts are made and agreed to based on the current tax system. However, what is the tax treatment if the contract will not be completed by June 30, 2010? The remainder will be invoiced under the new tax system. The same is true for price agreements that typically run for a calendar year.

At the same time, there is also the issue of the embedded RST in supplier pricing. This should result in lower supplier prices, at least from Ontario and British Columbia sources, but how much of a reduction will you see, and when will you see it? Experience in the Maritimes was that it took up to 18 months for savings to flow through, when the 3 provinces moved to HST. Much depends on how competitive is the marketplace and the nature and term of contracts with your suppliers.

Many of the questions that have been asked relate to this issue:

1. Contracts that I am tendering for now, with work to be carried out after June 30, 2010
2. Contracts that I am tendering now, which will have work carried out before July 1, 2010, and likely have some work carried out afterwards
3. Existing contracts and price agreements that will still be active and not completed before July 1, 2010.

Contracts that I am tendering for now, with work to be carried out after June 30, 2010

With regard to issue 1: what I am tendering for is to be supplied in full after June 30, 2010. Whether this is a construction project or a vehicle or other equipment, all transactions will be subject to HST. Request bidders to supply cost price, plus HST. Since all will charge HST at 13%, the tax is superfluous to the evaluation of vendor price. Do have clear instructions in the bid documents directing bidders to bid based on the transition to HST as of July 1, 2010.

We discuss later the issue of embedded RST in pricing, but the experience of some municipalities and of some Provincial (Ontario) Ministries is that vendors are already factoring this into longer term quotations, and passing along the anticipated tax savings. For those municipalities who would like to guarantee that this happens, it will likely cost you more to do so than you will save, and that assumes that your supplier will be willing to let you go through their books. Remember that other than by doing an audit, you can't ensure this at all. What will do it for you, and this is the experience mentioned earlier, is a competitive market place. If suppliers try to capture the embedded RST for themselves, they risk losing the contract to other suppliers who are prepared to pass the savings through to the client.

Once you have selected a supplier, you have a supplier price. Your payments to the supplier will be 13% higher, but the real cost to your municipality will be 0% or 1.76% higher, depending on whether the supply is for a commercial activity or a municipal operation, which determines how much HST your municipality gets back. Thus for spending approval and for encumbrances, the amount used should be 100% or 101.76% of supplier cost, as the remainder of the payment to the supplier is not an expense, but a (HST) receivable amount, that your municipality expects to recover from CRA.

Contracts that I am tendering now, which will have work carried out before July 1, 2010, and likely have some work carried out afterwards

If an RFP/RFQ is issued today, by the time it goes out on the street, allow time to respond, receive and evaluate the bids, prepare a report to Council if required, and get Council approval to go ahead, notify the successful bidder, and allow time for the firm to gear up, the transition issue will virtually become a non-issue. Because of the Input Tax Credit and/or Public Sector Bodies' rebate for HST returns all or nearly all of the sales taxes paid back to your municipality, whereas

RST paid is a straight expense, you may seriously want to postpone these bid processes, or go through the process, but specify the start or delivery is to occur after June 30, 2010.

For things you need immediately, request bidders to quote and price as you currently do, if delivery or work will be completed in full before July 1, 2010. If completion or delivery will be after June 30, 2010, again request supplier cost plus applicable sales taxes, so that the RST paid by the supplier and flowed through to you will be identified, and this approach also covers the switch to HST, if both tax breakdowns are requested, i.e. GST/RST and HST. Evaluate the bids on the basis of supplier cost before applicable taxes, especially if a substantial part of the supply will take place after June 30, 2010. Have clear instructions in the bid documents directing bidders to bid based on the transition to HST as of July 1, 2010.

While you could request your supplier to separate the bid into RST and HST portions, that would be an unfair imposition, as contractors do not have absolute control over when the work actually takes place. For spending approval and encumbrances, use pricing with RST, as this will cover the situation where most or all of the expenditure occurs before June 30, 2010.

Existing contracts and price agreements that will still be active and not completed before July 1, 2010.

Contracts and price agreements already in place and extending beyond June 30, 2010, are a real problem. You entered into agreements in good faith under one set of tax rules, and now those rules are to be changed.

The Canadian Construction Association quotes General Condition 10.1 of CCDC2 2008:

The Contract Price shall include all taxes and customs duties in effect at the time of the bid closing except for Value Added Taxes payable by the owner to the Contractor as stipulated in Article A-4 of the Agreement – Contract Price

10.1.2 Any increase or decrease in costs to the Contractor due to changes in such included taxes and duties after the time of the bid closing shall increase or decrease the Contract Price accordingly.

The industry has recognized this to be a problem from extensive past experience, and this provides a mechanism for addressing the financial impact of the tax change. With all such contracts that you have, it will be a case of renegotiating with the individual contractor to deal with the difference in contract costs due to the tax change.

For fixed price agreements with suppliers, the same is true, though one option would be to cancel them as of July 31, 2010, and enter into new ones, with the expectation that by August 1, 2010, they should have removed most or all of the embedded RST from their prices. This assumes that there are no penalties or other legal issues involved in cancellation.

CRA's GST/HST Technical Information Bulletin B-053 "Construction Supply and Installation Contracts" makes it quite clear that GST, and HST by extension, is to be charged on the full selling price, regardless of the RST content of that selling price. Thus if a supplier buys inputs before July 1, 2010 and pays RST on them, you will pay HST on 108% of the retail price of those supplies. However, you will get nearly all of that HST back as ITCs or PSB rebates. This is a transition problem that should disappear within a few months, as inventories turn over.

Embedded RST and potential double taxation

The previous section looked at specific taxation issues on long-term contracts and pricing agreements – embedded RST and potential double taxation. Embedded RST was discussed in the comparison of RST and VAT. This is the RST paid throughout the supply chain on acquisitions that do not qualify for a vendor exemption certificate, or where your supplier is the deemed end-user, for the purpose of your contract. While an individual supplier can calculate how much that RST would amount to as a percentage of sales, no-one knows for the entire supply chain.

With the move to HST, this embedded taxation should disappear, as each supplier can claim all HST paid to be refunded as Input Tax Credits. In a competitive market-place, most or all of that saving could be passed on to the client. There has been much agonizing amongst municipal finance and purchasing staff as to how to be sure that suppliers pass those savings along.

Unfortunately, you cannot. Some have thought to seek to audit supplier accounts in order to verify this, but the reality is that any such request will result in being politely told to “mind your own business,” and a potential unwarranted invasion of privacy complaint. Firms will likely seek business elsewhere, rather than to have to face such intrusion into their business affairs.

All firms are aware of this issue, and that their competitors can use these tax savings for competitive advantage, so that any particular company that doesn't pass along the savings does so at the risk of being outbid. In short, the same competitive bidding process that you use to award contracts will tease out the savings from the elimination of embedded RST, especially if you request supplier cost, plus applicable taxes itemized separately, and award on the basis of supplier cost, other factors being equal. Again, it is understood that some Ontario Ministries and Ontario municipalities have already experienced this dynamic at work to their financial advantage.

Double taxation is a potential risk, if a supplier buys supplies in June, pays RST on them, and then charges you for them in July at his net cost (RST included), plus HST on the invoice. As with embedded RST, this will never be a completely clean situation.

One way to address the bulk of this problem will be to require all suppliers with major contracts to provide your municipality with a progress billing that covers everything up to 11:59 pm on June 30, 2010. Thus what is done in June would be invoiced with GST and RST added on. What is done in July would be invoiced with HST added on, but no RST. An acceptable alternative approach would be to set up vendor price schedules to have each applicable tax entered separately and structuring the pricing page to reflect the tax breakdown pre (i.e. GST/RST) and post (i.e. HST) June 30th. The challenge here for the purchasing agent will be to know how much will be completed before July 1st, and how much will be done afterwards. Another challenge will be checking post-June 30th invoices to determine whether the supplier has charged both RST and HST on supplies.

While there is apprehension that a supplier will buy supplies in June (with RST paid) for use in July (with HST charged), the reality is that your supplier is going to practice strategic procurement just as you will. Again, a competitive marketplace will take care of this more effectively than any system one might devise to try to eliminate the risk of double taxation. Realistically, the supplier should issue a vendor exemption certificate for the purchase that is for resale to your municipality. Where you have on-going material supply contracts that span the transition date of June 30th, there should be no change if the price agreement is supplier pricing plus applicable taxes. They will be GST and RST before, and HST afterwards, and double taxation will not normally be an issue. Embedded RST may be, though, after June 30th.

You might wish to audit supplier contract invoices for supplies, where itemized, to determine that the pricing after June 30th does not include RST. If it does, require the supplier to apply for a refund of the RST, or absorb the cost. Bear in mind that both of these issues are really transitional in nature and will quickly disappear as a concern, as was the case when GST was introduced in 1991.

Transition rules

The tax system changes on July 1, 2010. A supplier to your municipality will invoice you for all services rendered up to and including June 30, 2010, and charge 5% GST. For all services rendered from July 1, 2010 onwards, the supplier will invoice you at his price plus HST at 13%.

For example, if I sell your municipality a gross of “whatsits”, and deliver them to you or you take legal possession of them (even though they are sitting in my warehouse) on or before June 30, 2010, I will invoice you at the agreed price, plus 5% GST and 8% RST. If I deliver them to you after June 30, 2010, then you will be invoiced at price plus 13% HST.

The applicable tax treatment depends on when the transfer of goods and services between us actually took place. **This occurs at the earliest of (a) date of delivery, (b) date of invoice, and (c) date of payment.** When the bid was made and when you placed the order have absolutely no bearing on the matter. Without them, the transaction does not get executed satisfactorily, but they are not the taxable sales transaction, or determine what taxation is payable, and when it is due.

You will also encounter transactions that are not so cut and dried, which straddle the changeover date, with benefits being transferred before and after, or the acquisition being made before for delivery after. Both CRA and the Ontario Ministry of Revenue have prepared transition rules for these types of situations.

Examples of such transactions are:

- Leases and rentals
- Memberships
- Professional services, such as standby fees

If the lease requires monthly payments, then the July payment attracts HST, whereas the June one only attracted GST. The transition rules apply to any agreement incurred for a period of time that extends past July 31, 2010, and that is paid for in full up-front. Transaction periods terminating in July 2010 and where more than 90% of the transaction period is before July 1, 2010 are not subject to HST.

Tax treatment for the period:			
Transaction execution date	Oct 14 to April 30, 2010	May 1 to June 30	After June 30, 2010
Oct 14 to April 30, 2010	Charge GST @ 5%	Charge GST @ 5%	Charge GST @ 5% (see Note)
May 1 to June 30	Charge GST @ 5%	Charge GST @ 5%	Charge HST @ 13%
After June 30, 2010	Charge HST @ 13%	Charge HST @ 13%	Charge HST @ 13%

If your municipality is entering into this type of transaction, the supplier is supposed to charge you GST/HST according to the above table. Likewise for taxable services provided by your municipality, this table outlines your obligation to collect GST/HST from your client. If the transaction execution date is after June 30th, note that the entire transaction will be subject to HST.

Note: If your municipality’s client is a GST/HST registrant, i.e. a commercial enterprise or a public sector body, the Provincial portion of HST is to be self-assessed by that client for the period after June 30, 2010, and the amount is to be included on line 405 of the first HST return submitted after June 30, 2010. This would include your municipality, if you are the client. Individual taxpayers are exempt from this requirement.

The point of supply issue

Retail sales tax is a tax on a retail sale at the legislated rate where the sale occurs. If the goods are to be delivered to another province, then the sale is RST-exempt, though the buyer should be self-assessing RST for his/her own province, at the stipulated rate. An example of this is buying a New Flyer bus in Winnipeg for an Ontario municipality. New Flyer does not charge Manitoba RST on the transaction, but Ontario RST must be shown to have been paid, in order to get registration plates for the bus.

For RST, the point of supply is considered to be the province where the good or service originates, and is taxed at the appropriate provincial rate. If the good or service is to be demonstrably used or consumed in a different province, such as the New Flyer bus, then the item is exempt from RST of the originating province, but is RST-taxable in the destination province. Whether one self-assesses RST for the destination province may be a moot point. To register a vehicle, there is clearly no choice. From a procurement perspective, Ontario RST should be factored into the pricing and cost of the purchase.

Value-added taxes like GST and HST are consumption taxes, levied on the consumer of goods and services. CRA is currently proposing to change the deemed point of supply to be the location of the consumer. Proposed regulations were circulated for comment. The deadline for comment has passed (March 31, 2010). Regulations are anticipated soon.

What will this mean? Since over half the country will be "harmonized" on July 1, 2010, the plan is to require the supplier to charge, collect and remit the full HST payable in the participating province of the receiving customer location, regardless of where the supplier is located in Canada. If this happens, New Flyer will invoice your municipality for cost, plus 13% HST, and you can show the paid invoice to get the plates, as both portions of HST will have been paid. Any PO or other document to New Flyer should request pricing to be expressed in terms of "supplier cost plus applicable sales taxes" (just in case).

If the rules are not changed, the situation will be the same as now, only your municipality will have to self-assess the Provincial portion of HST. New Flyer would bid at cost plus 5% GST, and invoice your municipality for cost plus 5% GST, yet your net cost will be the additional 1.76%, the portion of the Provincial portion of HST that is not rebated. The self-assessment would normally be done as an entry on line 405 of the HST return, and added into the net remittance or subtracted from the refund claimed for the reporting period, as the case may be. Now, when you apply for the plates, how will the staff at the MTO office/agency counter know or be certain that you have paid the full HST on the purchase? It is no longer a simple matter of going in with a cheque payable to the Treasurer of Ontario, which would be the wrong jurisdiction.

One solution would be to request/require New Flyer and all other suppliers to bid and invoice at cost plus 13% HST, if the supply is GST/HST-taxable. This way, your municipality can prove that you have paid HST in full, if required. More important, you will be evaluating bids and encumbering tenders and purchase orders using the actual amount of HST your municipality will be paying.

On the supply side, if you are selling goods or services in Canada, the revised rules will require you to charge HST at the appropriate rate for all participating provinces. For the three Prairie Provinces, Prince Edward Island and the three territories, you will still only be charging the Federal portion, or 5% GST.

Some special issues

Are any items left that will not have HST added to them? The zero-rated and tax-exempt items that will have no HST charged on them were listed in an earlier section of this newsletter. There are some special cases or circumstances that may have little or no impact on your municipality's procurement function, but which may be of professional or personal interest.

There are a number of classes of supply that will be subject to the Federal portion of HST at 5%, but which will receive a 100% point-of sale rebate of the Provincial portion of HST. Thus the purchaser will still be taxed at 13%, but receive a rebate of 8/13ths of the HST for a net HST rate of 5%. The POS rebate applies whether you are purchasing these supplies from an outside supplier, or your municipality is the supplier.

This provision applies to:

- books;
- children's clothing, footwear and diapers;
- children's car seats and car booster seats;
- feminine hygiene products;
- newspapers; and
- prepared food and beverages purchased in prescribed circumstances for not more than \$4.00.

These are the only exceptions to the general rule: **if GST is payable on a transaction now at 5%, HST will be payable on that transaction at 13%, effective July 1, 2010.** Whatever favourable sales tax treatments may have been conferred on your municipality under the Ontario Retail Sales Tax Act, such as exempting fire engines, they no longer apply. We will all be playing on a much more level field.

What about things like personal travel and expenses? If they get rolled into P-card purchases, will P-card purchases still be subject to the rebates? There are two issues here: P-cards and personal expenses. P-cards are a payment mechanism for settling taxable sales transactions. Tax collected and credited or rebated for a transaction is governed by the nature of the good or service, and of your business status under the Excise Tax Act. How you pay for something is irrelevant to this. Incidentally, fees and other charges imposed by the financial institution will not be subject to HST, because the institution is a tax-exempt activity.

Personal travel is fully claimable for ITCs or rebates, but note the treatment of meals. As discussed in an earlier newsletter, under the Income Tax Act, meals and entertainment are only allowable as a business expense at 50%, because there is a deemed personal benefit to the employee. The Excise Tax Act follows the same principle for allowing ITCs and rebates on meals and entertainment, by only allowing 50% of the GST or HST to be claimed for refund. There are some cases where the full amount can be claimed, and truck drivers can claim a different percentage, which is documented in CRA publications. You should be aware of the 50% allowance principle.

If you use a corporate travel agent, the tax change will have no impact on the agreement or the relationship that your municipality has with that agent. There will be a change at the individual transaction level as Ontario hotels will be charging 13% HST on rooms, rather than the current 5% GST and 5% RST, and air, rail and inter-city bus fares will be taxed at 13% HST, rather than at 5% GST. The good news is that your municipality can claim most or all of the HST back as ITCs or PSB rebates, so that the impact of the tax change will be minimal.

Other resources

There is now a wealth of resource material available on-line. MFOA has posted this series of newsletters addressed specifically to the needs of Ontario municipalities.

Other useful reference sites include the Ontario Ministry of Revenue, Canada Revenue Agency, the Canadian Construction Association, and the major accounting firms. All provide detailed information and try to provide helpful advice.

Frequently asked questions

1. Currently, Consulting, Legal, Mediation and Waste Services have been exempt from RST. Will this remain the same under HST or will it change? If it will change how will we implement that change against contracts that will overlap the July 1st HST start date? How should we be addressing this issue in our Procurement documents? How should we be considering the tax change in our evaluation of bid submissions?

If the services are currently subject to GST, they will be subject to HST, and not exempt. Your contracts probably include the term "plus applicable taxes", which would cover HST. If your contract only refers to GST, the legislation trumps your contract, and HST will be payable, regardless of what the contract says. You should consider revising your contract. The answer to the last two questions was given earlier. You evaluate bids on the basis of price, so request bidders to provide the invoiced cost, plus applicable taxes, evaluating on the basis of supplier price. If everyone will be charging you 13%, including taxes muddies the waters, as the true cost to your municipality will not be supplier cost plus 13%, but supplier cost and perhaps 1.76%, if for a municipal activity. This will also apply is there is a pre-July 1st component to the bid, subject to GST/RST

2. What changes should be made to the standard bid and contract forms?

You want to know the price the supplier will charge you, plus applicable sales taxes. As stated above, you evaluate on the basis of price. The sales taxes will really not be an issue, since you will be refunded nearly the entire amount paid anyway.

3. Is it appropriate to revise POs whether or not the vendors have been told up front? Or, whether or not my municipality has signed an agreement with them? Legal issue? How should they be revised? Divide line items into 2 each, one for each tax code?

Your municipality has entered into an agreement with a supplier, either by contract, or by PO, which is a contract. They either stand as is, or are terminated or renegotiated. Whatever terms you have about sales taxes, the legislation overwrites them, so that they automatically will conform to the new tax regime. If your concern is to recover the embedded RST, then you should renegotiate or issue a new set of RFQs, to be priced on the basis of no embedded RST, though this would present a workload problem.

4. Should revised POs be sent to vendors with a letter? If yes, would this be all vendors including contractors with whom my municipality has executed an agreement?

This is covered in the answer to the previous question.

5. How should price schedules be prepared for use in tenders? Should there be two? One for pre-July deliveries and one for post? In this case, my municipality would have to estimate quantities under both conditions.

If you use two price schedules, how will you compare and evaluate bids? You would have to estimate quantities under both conditions. Use the approach of supplier cost plus applicable taxes, which will cover both situations

6. Should staff request RST out pricing on construction? And, should they ask for RST amounts to be shown as part of the line item information? Should labour and materials for 'supply and install contracts' be separated?

At this point in time, yes, yes and yes. Then your pricing will work fine for evaluating bids and for being invoiced under both tax regimes.

The issue of asking for RST tax information to be broken out and submitted by contractors on contractor invoices for work done pre-July 1st is problematic. The CCDC2 and OPSS construction contracts both lay out a progress payment process based on payment certificates, which are typically completed by the owner's staff/consultant. As such, a typical invoice is not provided by the contractor during the contract period. Again, requiring bidding and reporting on a cost plus applicable taxes basis will provide a mechanism for holding the contractor accountable for submitting proper tax information in this case, and will also work well with HST after June 30, 2010.

7. If using one price schedule, should bidders be told to blend their pricing if selling items bought pre & post July 1?

No – tell them to make their best offer. Your concern is to get the best price for your municipality, I believe.

8. How can my municipality ensure fairness in calling for bids? Bidders need to understand all the implications to be able to bid equally.

The tax regime is changing, not the bidding process or the integrity of the process. This is an issue for them as much as for you, and suppliers need to inform themselves about the change as much as municipalities.

9. Should existing orders all be cancelled and reissued?

For where you have price agreements, this might not be a bad idea. The question is when, if you want to try to get the embedded RST as savings. The reality is that it may be more practical to do this for the end of 2010, to give suppliers the chance to turn over their inventories, and to have truly eliminated the embedded RST from the supply chain. Again, the flow-through took 18 months in the Maritime Provinces, so don't expect savings to show up July 2nd.

10. Under what conditions can staff negotiate with vendors to verify or secure the right prices? Does my municipality have any leverage here?

Your best leverage comes from a competitive bidding and tendering process. It is unlikely that all of your bidders will enter into a pact to hang on to the embedded RST that they were paying, when they bid for work with your municipality. If any negotiating is being contemplated, (which is extremely limited in a tender process), it must be disclosed, and the process by which it will occur explained, in the competitive bid document that is released to vendors – otherwise it is not legal to do so.

11. Post implementation, should my municipality request separate line items on invoices, separate invoices or blended?

Post-implementation presumably means after June 30, 2010. In which case, what is the point? You want to see supplier pricing plus HST. What you do want to request is invoicing for goods and services rendered up to and including June 30, 2010, which will have GST and RST (if applicable). This way, you will not have to deal with billings split between the two regimes, or end up paying HST on services rendered before July 1, 2010.

12. What should staff be asking vendors to do post implementation? i.e. Should my municipality ask for RST rebates or HST rebates or tax credits or lower prices? Which is it?

Lower prices. You should be expecting to see some of the savings from the embedded RST being reflected in modest price reductions. Do not expect large savings from this. In most cases, the difference may be a few percent, at most.

13. What counts as documentation (from vendors) to support their claims for old RST? Who should be reviewing said documentation?

Presumably this refers to a vendor wanting to recover RST charges paid on supplies being provided to and invoiced to your municipality after June 30th. And the sale is now subject to HST in your hands. Unless you required the supplier to buy the item for you before July 1st, why would you even entertain such a claim? Lack of planning and foresight on the supplier's part does not constitute a liability for your municipality. Your supplier has had 8 months to figure out how to deal with this tax change, and to plan accordingly. Your vendor could have issued a Vendor Exemption Certificate for buying the goods RST-free before July 1st. Then this would be a non-issue.

14. Should staff do anything about existing contracts? For example, should they wait for July 1st before doing anything? Then, after implementation, and to avoid paying HST on top of established prices which have embedded RST, should they ask vendors for new price schedules to replace the old ones in their contracts?

Why wait till July 1st? If you have price schedules with RST included, so that you are not charged RST separately at time of sale, they should be renegotiated to be net of all sales taxes. With respect to embedded RST, you can try to negotiate a lowering of prices, which may or may not work. This may be more effective after July 1st, when this will become much more relevant, and suppliers will start to see changes in pricing from their own suppliers in turn.

15. Should staff ask for invoices to be changed? Basically, how can we avoid paying HST on top of RST inflated prices as per existing contract price schedules?

The invoice is the final phase of a transaction, and you cannot expect to have them changed. An invoice is based on what was done, and there is the saying, "What's done is done." That is why you shouldn't wait until July 1, 2010, to revise contract price schedules, especially where the supplier is paying RST on your behalf, and then billing you for that cost.

16. What is the best approach for construction bidding? That is, what is the appropriate form the pricing schedule should take in order to reduce/eliminate challenges with projects that are bid post July 1, 2010.

Supplier cost, plus applicable taxes. Select the lowest bidder (other things being equal), and the market place should ensure that you get the best possible pricing. The transition to HST really doesn't change anything from a procurement perspective. If anything, it simplifies matters, as every supplier will now be charging 13% on all goods and services, and your municipality will receive all or nearly all back as ITCs and/or PSB rebates. So for soliciting bids and evaluating them, go to the heart of the matter, which is the actual supplier cost.

17. What specific HST parameters do we need to be aware of to ensure they are covered in any clause we put into our bidding documents?

"Plus applicable sales taxes" should cover any future eventuality. HST is a tax on a sales transaction. It is not part of the transaction itself. The legislation and associated regulations determine much of the legal requirements for handling HST. The concern would be that supplier bids reflect them.

18. How will purchasing staff handle budget shortfalls as a result of the implementation of HST?

Budgeting issues were dealt with in HST Newsletter #6. This is really a management problem, not a purchasing one. In most cases, there should not be one.

-----00000-----

For more information and resources regarding Harmonized Sales Tax, please go to [MFOA's HST webpages](#), or contact:

Dan Cowin
Executive Director
MFOA
dan@mfoa.on.ca
416-362-9001 x 223

NOTE: This Newsletter is published to assist you in preparing for the changeover to HST in Ontario as of July 1, 2010, based on information believed to be current up to a week before posting on the web. While every endeavour has been made to be as complete and accurate as possible, MFOA and the author accept no responsibility for any differences of opinion that the Canada Revenue Agency and the Ontario Ministry of Revenue may adopt with respect to the ideas and concepts presented, nor for any outcomes of those differences. The ultimate authority in these matters is the respective Federal and Provincial legislation.