GST and PST

C. Dick Yu, MBA, CA, CFP 余政昌會計師

GST

The Goods and Services Tax (GST) was introduced in Canada on January 1, 1991. Very similar to a Value Added Tax GST (VAT), is a broad based, multi-stage transactional tax system. Effectively, a GST registrant collects GST taxes on sales but obtains Input Tax Credits (ITC) for GST paid on purchases. The registrant remits to the government the difference between what has been collected and what has been paid. When the amount paid is more than the amount collected, the registrant is entitled to a GST refund. Unlike most other VAT systems that recognize credits over the life of capital assets, full ITC for capital purchases can be claimed at once under the GST system.

There are three GST taxation categories: tax-exempt supplies, taxable supplies at 7%, and zero-rated taxable supplies. No GST is collected on sales under the tax-exempt or zero-rated category. However, registrants of zero-rated taxable supplies get the benefit of being able to claim ITC. Exporters, in particular, enjoy GST refunds to enable them to compete more effectively in international trade. Other zero-rated supplies include basic groceries, prescription drugs, medical devices, most agricultural and fishing products, and foreign travel and transportation services. These supplies are considered either life necessities or essential to exporting competitiveness. Examples of tax-exempt supplies are residential rents, financial services and educational services.

Any self-employed person or business whose annual taxable revenue exceeds $30,000 is required to register for a GST account. The $30,000 threshold is created as a concession for small businesses. However, these businesses or individuals can still voluntarily register for GST accounts even if their revenue does not meet the threshold. Trade exporters, for example, may want to register in anticipation of GST refunds. Other incentives provided to small business include simplified ITC calculations and the quick method of accounting. Under the simplified calculations, total taxable inputs are multiplied by 7/107 to arrive at the input tax credit. Eligible businesses, whose annual GST-included taxable sales are $200,000 or less, can elect to use the Quick Method to determine the net GST remittance. Businesses simply apply specific, reduced rates to their total sales for remitting net GST due to the government, saving the effort to track sales and input taxes individually. The GST tax due to the government is calculated at 5% of total sales charged by service providers and manufacturers. In the cases of retailers and wholesalers, a lower 2.5% is applied. In addition, small businesses can deduct 1% of their sales on the first $30,000 of sales each year. These breaks for small business are a reward for joining the system and collecting taxes for the government.

HST (Harmonized Sales Tax) is similar to the GST but adds PST (Provincial Sales Tax) to the 7% GST. The HST is only currently adopted by three provinces, namely Nova Scotia, New Brunswick, and Newfoundland and Labrador. Supplies under the HST system are applied at a 15% rate. The hesitation of non-participating provinces to adopt the HST comes from their fear of shifting more sales taxes from businesses to consumers, and from the potential loss of total sales taxes for the provinces due to ITC claims. Overall, GST has the benefits of simplicity and fairness. It is simple to understand and calculate. For businesses, payment of GST only increases as their business increases.

PST

The Provincial Sales Tax (PST), also called Retail Sales Tax, is a consumption tax. While GST is applicable to most goods and services, PST is most often applicable to goods. Only five services are taxable in Ontario: commercial parking, telecommunications services, hotel accommodation, and repair labour and maintenance contracts for tangible personal property. Goods necessary for basic living are exempt from PST. Examples include food products, children's clothing, books and prescription drugs. Also, real property is not taxable under PST.

Unlike GST, PST does not have any Input Tax Credits as such. Instead, a Purchase Exemption Certificate is used to claim PST exemption for taxable goods purchased for resale purpose. The general PST rate is 8% in Ontario. Different rates apply to other goods and services. Some examples are: 3% for auto insurance, 5% for hotel accommodation and 12% for alcoholic beverages. It is generally more burdensome and complicated to figure out if PST is applicable to certain goods or services, or applicable under certain situations or circumstances. The $30,000 relief threshold for small businesses in the GST system cannot be found in the PST system.

Tax Reform Wishes

I have two wishes for sales tax reform. First, I wish HST (Harmonized Sales Tax) could be adopted throughout Canada. It would save confusion and the headache of understanding the complexity and peculiarity of the PST system in the various provinces. Second, I wish the overall sales tax rate could be reduced. High sales taxes inherently deter consumption, an important driver in economic growth. Many merchants advertise sales campaigns of "no GST and PST" to attract retail customers. These promotions stimulate consumption as consumers seize bargains at a 15% reduction in price. Merchants still need to pay GST and PST to the governments; they absorb the tax burden. When I lived in the U.S. in the early nineties, I enjoyed low sales tax rates of 4% in Michigan and 6% in Minnesota. I had also experienced a 5% VAT in Taiwan and no sales tax at all in Hong Kong. Sales taxes were not a factor in my purchasing considerations. But when combined sales taxes reach as high as 15% in Ontario, I certainly feel the pain of taxes and think twice about all major purchasing decisions I make.