Legislation matters

STANDARD LIFE

July 2010

Harmonized Sales Tax (HST) – Coming July 1, 2010

As was announced in the April 2010 issue of "Legislation matters", the governments of Ontario and British Columbia have agreed to implement the Harmonized Sales Tax (HST), which will replace the provincial sales taxes and GST. Therefore one single HST, administered by the Federal Government, will take effect in Ontario and British Columbia starting **July 1, 2010**.

Moreover, the Federal Department of Finance took this opportunity to review its rules on the application of GST to segregated funds, mutual funds and registered pension plans. These revised rules, published recently by Finance Canada, will have an impact on the application of the HST in Ontario and B.C., as well as in provinces where HST is already in effect, namely New Brunswick, Nova Scotia, and Newfoundland and Labrador.

How HST will be applied

Going forward, the HST will be applied to the investment management fees (IMF) charged by investment managers to administer the funds offered under your group retirement program. It will also be applied to annual "Member fees" (e.g.: $2/month/member) that are sometimes charged directly to the clients via an invoice, or deducted from the unit values held by the member (like management fees).

HST will therefore be applied as follows:

- For IMFs, Standard Life will deduct HST from the unit values on members' accounts, as is currently done with GST.
- The amount of HST to be deducted will be determined according to the province where the policyholder (the employer in most cases) is based.
  - E.g.: If policyholder is based in Ontario, but the member is located in Quebec, the Ontario HST will be charged.
- HST on the Member fee will be charged in the same way, unless it is the client who pays these fees. In such cases, the HST on annual fees will be charged to the client on their next invoice.

With these new regulations in effect, taxes in the various provinces apply as follows:

- Ontario, New Brunswick, and Newfoundland and Labrador – The HST rate will be 13% (5% federal component and 8% provincial component).
- British Columbia – The HST rate will be 12% (5% federal component and 7% provincial component).
- Nova Scotia – The HST rate will be 13% from May 1 to June 30, 2010, and 15% as of July 1, 2010 (5% federal component and 10% provincial component).
- Quebec – The tax rates are 5% GST and 7.5% QST.
- Alberta, Saskatchewan, Manitoba, Prince Edward Island, Northwest Territories, Nunavut and Yukon Territory – only GST (5%) applies.

It must be noted that in New Brunswick, Nova Scotia and Newfoundland and Labrador, these rules came into effect on **May 1, 2010**.

Context: Draft legislation on place of supply rules

Under draft legislation, tabled on April 30, 2010, concerning place of supply rules, a supply of service is made in a province where, in the ordinary course of business, the supplier obtains the business or home address of the recipient of the supply in the province.

If the supplier obtains addresses in more than one province, the supply is made in the province to which the address is "most closely related to the supply".

"Recipient" is defined as the person who is required to pay the consideration for the supply under an agreement with the supplier.

In order to determine the sales tax rate Standard Life must apply to management fees (and other fees) to be charged for fund management services supplied to the client, it was necessary to determine the address "that is most closely related to the supply".

The facts

- The client (i.e. the employer, Quebec pension fund or trustee) must sign an application wherein it accepts the submission from Standard Life. This submission is an integral part of the insurance policy issued in the name of the client who will become the policyholder.

- The submission basically provides investment options, pricing (including related services) and optional services.
- Ultimately, Standard Life issues an insurance policy, which is actually an annuity contract including the submission to the client for establishing an employee pension plan.
- According to the policy, the main services that Standard Life is committed to providing are: to allocate member and employer contributions to the investment options selected by each member, provide segregated fund asset management services and pay benefits on termination of employment, death, etc.
- Each client is charged segregated fund asset management fees by Standard Life in one of the following ways:
  - Management fees are deducted from the funds by reducing their unit values
  - Management fees are billed to the client.
- Standard Life also charges certain clients Member fees (e.g.: $2/month/member). These fees are sometimes charged directly to the clients via an invoice or deducted from the unit values held by the member (like management fees).

Standard Life's position

For place of supply rule purposes, the correct address is the **client's address** (the address of the policyholder) and **not** the member's address).

Here are the main reasons for our position:

- Contracts (insurance policies) are entered with the clients, not the members.
- We understand that the client is the one required to pay the fund management fees (and any applicable taxes) under the contract with Standard Life.
- The fact that the member ultimately incurs the management fees through a decrease in fund unit values represents, in our opinion, a form of payment chosen by the client.
- Standard Life sometimes bills the client directly. For example, PIF clients. In this case, we charge the GST, HST or QST according to the client's address on the invoice.
- The member fees (e.g.: $2/month/member) sometimes billed directly to the client via a paper invoice will receive the same tax treatment as management fees (i.e. according to the client's address on the invoice).
- The SAM (Special Attribution Method) applicable to pension plans, which was proposed on May 19, 2010 by the Federal Department of Finance, requires the pension plan administrator to calculate a net tax based on the provincial distribution of its plan members. The net effect of this method is to ensure members pay the same tax rate and the plan administrator, in the plan's name, recoups (or pays) any overpaid (or owed) provincial portion of the HST.
- In fall 2009, the Federal Department of Finance tabled draft legislation which aims to improve the application of GST to financial services. As a result, current rules on input tax credits and rebates would be replaced by a single rebate process (i.e. the plan management entity, the pension fund, would be entitled to a rebate equal to 33% of the GST/HST that was paid or deemed to be paid) to ensure that reducing the GST/HST applicable to pension plans benefits the pension fund. The rebate would be available regardless of the plan provisions and whether or not the employer or fund is registered for the GST/HST.
- Under this new 33% rule, we believe the pension fund could claim a rebate equal to 33% of the GST/HST paid or deemed to be paid. If the recipient is the member, the rebate may not apply. However, this remains to be confirmed by the Federal Department of Finance.
- Quebec Sales Tax (QST) – According to the new rules, we believe the pension fund could claim a QST rebate. If the recipient is the member, the rebate may not apply.

These new regulations and other GST regulations announced during the year will have an impact on pension plans. We recommend therefore that you review your pension plan and consult your tax advisor.

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GE12338-06-2010 GS