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# SPECIAL REPORTS

## Nonresidents and Canada's VAT System

by Camille Kam

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Canada is one of many jurisdictions that impose a tax on consumption in the form of a VAT. The goods and services tax/harmonized sales tax is a federal tax in Canada that applies at a fixed rate to the final consumption of property and services (generally referred to as a ''supply''). The legislation governing the application of the GST/HST is the Excise Tax Act (Canada) (ETA).[1] The GST is a federal tax that is imposed in every province and territory in Canada, while the HST is a combined federal/provincial tax that is imposed in provinces that have harmonized their provincial sales taxes with the GST.

While a nonresident that carries on business in Canada may not be subject to Canadian federal income tax because of an income tax treaty entered into between Canada and the nonresident's country of residence, the same relief is not available in respect of the GST/HST. Therefore, a nonresident not captured by the Canadian income tax net may be caught for GST/HST purposes and be required to both collect and pay GST/HST.

The two potential ways in which nonresidents of Canada can come into contact with Canada's GST/HST system are when they do business in Canada or do business with Canada. Specifically, nonresidents can be caught by the GST/HST regime when they undertake any one or more of the following activities:

- selling into Canada;
- purchasing from Canada; or
- leasing into and out of Canada.

This article will provide a brief overview of the GST/HST system in Canada and then discuss the GST/HST consequences of each of these three types of activities commonly undertaken by nonresidents of Canada. Any nonresident doing business in or with Canada will generally be engaged in one or more of these activities and should consider whether any GST/HST compliance obligations may apply.

### I. GST/HST Overview

The GST/HST is a multistage tax: it taxes the value added to goods and services at each stage of the production and distribution chain. To avoid double taxation (in the form of cascading),[2] tax is refunded to qualifying businesses for the GST/HST they pay on inputs[3] through refundable input tax credits (ITCs). Final consumers at the end of the supply chain bear the ultimate burden of the tax in that they pay the full amount of any applicable GST/HST but are not entitled to recover it by claiming ITCs.

#### A. How Does GST/HST Work?

Everyone who purchases property and services to which the GST/HST applies is required to pay the tax, with the exception of some provincial/territorial governments and First Nations entities. Vendors who supply property or services to which the GST/HST applies are required to collect the tax from those who purchase their supplies and to remit the tax to the federal government via the Canada Revenue Agency if

[1]RSC 1985, c. E-15, as amended.

[2]Cascading refers to the application of tax to the same supply several times as it passes through the supply chain.

[3]Inputs are purchases of property and services used in the course of doing business.

**Table 1. Overview of GST/HST Issues for Nonresidents**

| Selling Into Canada | Purchasing From Canada | Leasing Into and Out of Canada |
|---|---|---|
| **Mandatory registration and collection**<br>• Taxable supplies made in Canada<br>– Place of supply rules<br>– Nonresident override rule<br>• Carrying on business in Canada<br>**Voluntary registration**<br>**Security requirements for registrants**<br>**Importing goods, services, and intangibles into Canada**<br>• Importing into Canada<br>• Importing into an HST province | **Payment and recovery of GST/HST**<br>**Exporting goods, services, and intangibles from Canada**<br>• Proof of residence and registration status<br>**Purchasing and reselling in Canada**<br>• Drop shipments to GST/HST registrants<br>• Transfers to a carrier or warehouse<br>• Exports | **Place of supply rules**<br>**Where possession or use obtained**<br>**Periodic lease payments**<br>**Potential registration requirements** |

they are registered for a GST/HST account.[4] Whether a vendor must register for GST/HST depends on, among other things, whether the vendor is providing taxable supplies in Canada. Although the purchaser is legally liable to pay any applicable GST/HST, the vendor is legally obligated to collect and remit the tax. As such, the CRA will generally look to the vendor first for any unremitted GST/HST. When assessed for unremitted GST/HST, a vendor may have recourse against the purchaser on whose purchases the GST/HST was not collected.

*1. Taxable vs. Exempt Supplies*

Taxable supplies are supplies made in the course of a commercial activity that are not exempt supplies.[5] The general rule, subject to specialized exceptions, is that a vendor that provides taxable supplies is entitled to claim ITCs on any GST/HST that it pays on inputs purchased in the course of providing those taxable supplies.[6] As such, vendors who provide exclusively taxable supplies are generally able to fully recover the GST/HST they pay in the course of running their businesses. Taxable supplies include zero rated supplies, which are supplies that qualify as ''taxable'' (so ITCs may be claimed for inputs purchased in the course of providing those supplies), but are ''taxed'' at a rate of 0 percent.[7] Taxable supplies can therefore be taxed in Canada at a rate ranging from 0 (for zero rated supplies) to 15 percent (for taxable supplies provided in Nova Scotia).

Exempt supplies, like zero rated supplies, are not subject to GST/HST. From the point of view of the purchaser, there is no difference between a product that is exempt from GST/HST and a product that is zero rated. However, unlike a vendor who provides zero rated goods and services, a vendor who provides exempt goods and services cannot claim ITCs for the GST/HST that the vendor pays on the inputs it consumes to provide the exempt goods and services.[8] While ''exempt'' might intuitively sound like a good thing, it is, in reality, bad for vendors that provide exempt goods and services: it means they do not get to recover the GST/HST they pay in the course of their operations, thereby increasing their operational costs. Items that are zero rated or exempt from GST/HST generally have that status for public policy reasons. For example, many exports and other supplies to nonresidents, as well as basic groceries, are zero rated, and many healthcare and financial services are exempt from the application of GST/HST.

In this article, we will generally address GST/HST compliance considerations relevant to nonresidents involved in the purchase and receipt of taxable supplies

[4]ETA section 221(1). *See also* CRA, GST/HST Memoranda (New Series) 2.1, ''Required Registration'' (May 1999).

[5]ETA section 123(1), ''taxable supply.'' *See also* ETA section 123(1), ''commercial activity''; CRA, GST/HST Memoranda (New Series) 3.1, ''Liability for Tax'' (Aug. 1999) at paras. 64-66; and CRA, GST Memorandum 300, ''Tax on Supplies'' (Mar. 15, 1991) at para. 4.

[6]ETA sections 169, 199, and 206.

[7]ETA section 165(3). *See also* CRA, GST/HST Memoranda 300-3, ''Zero-Rated Supplies'' (Dec. 30, 1993); GST Memorandum 300, *supra* note 5, at paras. 5-6.

[8]ETA section 123(1), ''exempt supply.'' *See also* ETA section 123(1), ''commercial activity''; CRA, GST/HST Memorandum 300-4, ''Exempt Supplies'' (Nov. 2, 1993); GST Memorandum 300, *supra* note 5, at para. 8.



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only. Different and more complex rules will apply to exempt supplies than are described here.

*2. Registration and Reporting*

A vendor must register for a GST/HST account to collect and remit the GST/HST and claim ITCs. Registration can be done by a telephone call to the CRA or by completing and sending to the CRA Form RC1, "Request for a Business Number." To register, a vendor must provide general information about its business operations, as well as an estimate of the nature and extent of business activity it expects to undertake in Canada throughout its first fiscal year as a registrant. The effective date of registration is generally the date of application for registration. While the CRA may permit a GST/HST registration to be backdated, its administrative practice in this area is subject to change.

During the registration process, a vendor will be assigned a reporting period — either monthly, quarterly, or annually — for filing its GST/HST return, which is the document by which it reports the GST/HST it has collected and claims its ITCs. The reporting period is assigned based on the vendor's annual estimated taxable sales and revenues. The higher a vendor's estimated taxable sales and revenues, the more frequent its reporting period will be. While a vendor with estimated taxable sales and revenues entitling it to a longer reporting period (for example, annually) can elect to file more frequently (for example, quarterly or monthly), a vendor cannot elect to report less frequently than its assigned reporting period.[9]

GST/HST returns may, and in many cases must, be filed electronically. For quarterly or monthly filers, the filing due date will be one month after the end of the reporting period. Annual filers must file their GST/HST returns within three months after the end of the fiscal year. On their returns, vendors will report how much GST/HST they have collected and how much GST/HST they have paid for which they are entitled to claim ITCs. To determine their net tax, the amount of their ITC claim will be netted against the GST/HST they have collected. If the amount of net tax is positive, the vendor will remit that amount to the CRA along with its GST/HST return. Remittances of amounts in excess of $50,000 must be made through financial institutions — generally Canadian banks. If the amount of net tax is negative, the vendor will be entitled to a refund from the CRA.

The GST/HST system of reporting means that vendors can be initially out-of-pocket for the amount of recoverable GST/HST they pay in the course of operating their businesses. This cash flow issue can be especially acute for companies that are just commencing their business operations, as they often incur business costs that exceed their revenue during the start-up phase. Since these companies typically do not have GST/HST remittable against which to offset their ITC claims, they must wait for an ITC refund after filing their returns, which can often take weeks or months. Similarly, purchase or importation of significant capital assets may cause cash flow concerns.

[9]ETA sections 246-248. *See also* CRA, Guide RC4022, "General Information for GST/HST Registrants," at 11-12.

### A. GST/HST and the Provinces/Territories

The federal GST portion of the GST/HST applies at a rate of 5 percent on supplies made in each Canadian province and territory.[10] To determine the appropriate rate of GST/HST that must be charged on supplies made in Canada, suppliers must determine where the supply is made within the country.[11]

*1. Non-Harmonized Provinces*

In Saskatchewan and Manitoba, a provincial sales tax of 5 percent and 7 percent, respectively, is levied in addition to the federal GST on goods and a limited number of services.[12] Although the provincial sales taxes charged in these provinces are also consumption taxes, they are unlike the GST/HST in that they are single-stage taxes: all consumers in the supply chain are treated as the final consumer. There is also no mechanism for recovering tax paid on inputs as there is with a multistage tax like the GST/HST. However, some goods and services are not taxable, for example, goods that are purchased for resale or that meet specific conditions.

Prince Edward Island (PEI) also imposes its own single-stage provincial sales tax at a rate of 10.5 percent, but unlike Saskatchewan and Manitoba, the tax is applied in a way that includes the federal GST in its base. In the 2012-2013 provincial budget for PEI, it was announced that PEI would harmonize its provincial sales tax with the GST. As of April 1, 2013, the HST will apply in PEI at a rate of 14 percent.[13]

Alberta is the only non-harmonized province in Canada that does not levy a provincial sales tax. The only sales tax that applies in that province is the 5 percent federal GST.

*2. Harmonized Provinces*

Ontario, Newfoundland and Labrador, Nova Scotia, and New Brunswick have harmonized their provincial

[10]In Canada's three territories — Yukon, Nunavut, and the Northwest Territories — only the GST applies and no other sales taxes are imposed.

[11]Suppliers should be aware that the rules that apply to determine where a supply is made within Canada are slightly different than the rules that apply to determine whether a supply is made in Canada.

[12]Retail Sales Tax Act, CCSM cR130, section 2(1); Provincial Sales Tax Act, ch. P-34.1, section 5(1).

[13]PEI, The Government of Prince Edward Island, 2012-2013 Provincial Budget (budget address presented at the second session of the 64th General Assembly of Prince Edward Island, Apr. 18, 2012), *available at* http://www.gov.pe.ca/photos/original/fema_bdgtadd12.pdf.

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**Table 2. Sales Tax in the Provinces and Territories**

| Province/Territory | Harmonized? | Rate |
|---|---|---|
| **Alberta** | No | 5% GST |
| **British Columbia** | Yes, but HST will be repealed on April 1, 2013 | 12% HST (5% GST/7% PST as of April 1, 2013) |
| **Manitoba** | No | 5% GST/7% PST |
| **New Brunswick** | Yes | 13% HST |
| **Newfoundland and Labrador** | Yes | 13% HST |
| **Nova Scotia** | Yes | 15% HST (14% HST as of July 1, 2014, 13% HST as of July 1, 2015) |
| **Northwest Territories** | No | 5% GST |
| **Nunavut** | No | 5% GST |
| **Ontario** | Yes | 13% HST |
| **Prince Edward Island** | No, but will harmonize on April 1, 2013 | 5% GST, 10.5% PST applied including GST in base (14% HST as of April 1, 2013) |
| **Quebec** | Partially, will fully harmonize as of January 1, 2013, though QST name and provincial administration will be retained | 5% GST/9.5% QST applied including GST in base (5% GST/9.975% QST not including GST in base as of January 1, 2013) |
| **Saskatchewan** | No | 5% GST/5% PST |
| **Yukon** | No | 5% GST |

sales taxes with the federal GST to create the combined HST. Accordingly, provincial sales taxes are no longer levied in these provinces. The HST is, for all intents and purposes, identical to the GST, and can be thought of as GST charged at a higher rate (that is, 13 percent in Ontario, Newfoundland and Labrador, and New Brunswick, and 15 percent in Nova Scotia[14]). British Columbia harmonized its provincial sales tax with the GST (at the same time as Ontario in 2010) at a rate of 12 percent. However, political backlash in response to the harmonization will result in the repeal of the HST and the reinstatement of a nonharmonized provincial sales tax in British Columbia effective April 1, 2013.

Quebec has partially harmonized its provincial sales tax with the federal GST to create the Quebec sales tax (QST). Like PEI's provincial sales tax, QST includes the federal GST in its base. Unlike the other provinces, Quebec administers not only the QST, which applies at a rate of 9.5 percent, but also the GST within Quebec; it is the only province to administer the federal tax.[15]

[14]Nova Scotia announced in its 2012 budget that it will gradually reduce its HST rate from 15 percent to 13 percent by July 1, 2015. *See* Nova Scotia, Department of Finance, ''Nova Scotia Budget 2012-2013,'' *available at* http://www.novascotia.ca/finance/en/home/budget/default.aspx.

[15]An Act respecting the Quebec Sales Tax, RSQ, ch. T-0.1, section 16.

Although the QST is a multistage, value added sales tax like the GST, the QST is only ''partially'' harmonized with the GST because there are some significant differences in the way the two taxes are applied — most notably regarding financial services. On September 30, 2011, however, it was announced that Quebec will fully harmonize the QST with the GST, although the term ''QST'' will be retained and Quebec will continue to administer both taxes.[16] As of January 1, 2013, the QST rate will increase to 9.975 percent, but will no longer include GST in its base.[17] Further, financial services will generally become exempt for QST purposes, instead of zero rated.

### B. Who Is a Nonresident for GST/HST Purposes?

Special provisions in the ETA apply to persons who are ''nonresidents'' regarding their activities in Canada. ''Nonresident'' for GST/HST purposes is defined circularly in the ETA as ''not resident in Canada.''[18] In

[16]*See* Prime Minister of Canada Stephen Harper, ''Quebec Sales Tax Harmonization'' (Ottawa: Office of the Prime Minister, Sept. 30, 2011), *available at* http://pm.gc.ca/eng/media.asp?id=4373.

[17]The current 9.5 percent QST rate applies to amounts that include GST. The new 9.975 percent rate will not change the total amount of tax charged since it will apply on a pre-GST amount.

[18]ETA section 123(1), ''non-resident.''

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general, residency is determined based on common law principles, subject to the application of deeming rules discussed below.

*1. Residency*

*a. Individuals.* For individuals, residency is typically determined according to:

- the length and reason for the individual's stay abroad;
- the individual's residential ties with Canada;
- the individual's residential ties elsewhere; and
- the regularity and length of the individual's visits to Canada.[19]

Factors indicating that an individual is resident in Canada include having a dwelling place, family, personal property, and social and community ties in Canada. Individuals who are deemed to be resident in Canada under certain provisions of the Income Tax Act (Canada)[20] are also deemed to be resident in Canada for GST/HST purposes.

*b. Corporations.* In general, a corporation is resident in Canada if its central management and control activities occur in Canada.[21] Factors that determine where a corporation is centrally managed and controlled include:

- where its directors live and hold their meetings;
- where its managers live and hold their meetings;
- where its shareholders live and hold their meetings; and
- where the corporation performs its principal business and operations, and where it keeps its books and records.

A corporation incorporated or continued in Canada and not continued elsewhere is deemed to be resident in Canada.

*c. Trusts.* The residency of a trust historically has been determined based on where the trustee who has management and control of the trust lives. If there is more than one trustee with management and control of the trust, the trust has been considered resident in the country where the majority of the trustees live.[22] In a recent income tax case, the Supreme Court of Canada held that a trust will be considered to be resident for Canadian income tax purposes where the central management and control of the trust actually take place, regardless of where the trustee lives.[23] Whether this decision will apply to determine the residence of a trust for GST/HST purposes has not yet been tested.

*d. Other entities.* The ETA deems the following entities to be resident in Canada:

- a partnership, unincorporated society, club, association or organization, or branch thereof, when a member (or the majority of the members) having management and control is (or are) resident in Canada; and
- a labor union carrying on activities as such in Canada and that has a local union or branch in Canada.

*2. Deemed Residency*

The presence of a permanent establishment in Canada can change the residency status of a nonresident. Even if a person is determined to be a nonresident of Canada in accordance with the factors described above, that person can still be considered to be resident in Canada regarding activities undertaken by that person if those activities are conducted through a PE in Canada.[24] Conversely, a person who is resident in Canada, but who has a PE outside Canada, will be considered to be a nonresident regarding the activities it carries on through that PE.[25] As such, a determination of residency status under the definition of nonresident in the ETA is not always the end of the residency inquiry. To determine whether the GST/HST rules regarding nonresidents apply, it must also be determined whether a person has a PE inside or outside Canada, and what activities the person carries on through that PE.

The ETA defines a PE as a fixed place of business through which a person provides goods or services, expressly including a place of management, a branch, an office, a factory, a workshop, a mine, an oil or gas well, and a quarry, timberland, or any other place of extraction of natural resources.[26]

*a. Fixed Place of Business.* Outside the express examples provided in the definition of PE, the CRA has indicated in its policy statement on the meaning of ''permanent establishment''[27] that a fixed place of business will be found to exist when all the following elements are present:

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[19]*See* CRA, GST/HST Memoranda (New Series) 3.4, ''Residence'' (Apr. 2000), at paras. 5-30 [NM 3.4]; CRA, Guide RC4027, ''Doing Business in Canada — GST/HST Information for Non-Residents,'' at 7 [Guide RC4027]; CRA, Interpretation Bulletin IT-221R3, ''Determination of an Individual's Residency Status'' (Oct. 4, 2002).

[20]RSC 1985, c. 1 (5th Supp).

[21]N.M. 3.4, *supra* note 19, at paras. 31-34; Guide RC4027, *supra* note 19.

[22]N.M. 3.4, *supra* note 19 at para. 34; Guide RC4027, *supra* note 19; CRA, Interpretation Bulletin IT-447, ''Residence of a Trust or Estate'' (May 30, 1980).

[23]*Fundy Settlement v. Canada*, 2012 SCC 14.

[24]ETA section 132(2).

[25]ETA section 132(3).

[26]ETA section 123(1), ''permanent establishment.''

[27]CRA, GST/HST Policy Statement P-208R, ''Meaning of Permanent Establishment in Subsection 123(1) of the Excise Tax Act (the Act)'' (Mar. 23, 2005).

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- *Space.* There must be space at the person's disposal for a fixed place of business to exist. A legal right to use the space is not required and the space may be at the business place of another person. For electronic commerce purposes, space can be found to exist where equipment or machinery (for example, a server) at the person's disposal is located.
- *Continuity and permanency.* The place of business must be fixed in the sense of having a certain degree of continuity and permanency at a particular location. It should last or be intended to last indefinitely and the business should be considered ongoing. A fixed place of business cannot be of a purely temporary nature. Continuity and permanency can be found to exist where a person returns to the same business location for the same business purposes if the place is used with enough frequency and for a long enough duration.
- *Control.* A person must have control for a place to constitute that person's fixed place of business. A person can be found to have control at a place of business where there is someone at that place who has authority to make decisions about the operations of the business, or where operational activities are carried out at that place through automated equipment at the disposal of the business.
- *Constant presence and ordinary routine.* The visibility of personnel at a place of business can demonstrate constant presence for the purposes of determining whether there is a fixed place of business, though it is not required at a location operated through automated equipment. Ordinary routine can be demonstrated through day-to-day business and regular activity, whether it is daily, weekly, monthly, or seasonally. This element is unlikely to be met where there is only isolated activity.

A PE also expressly includes a fixed place of business of *another* person who is acting in Canada on behalf of the nonresident person and through whom the nonresident person provides goods or services in the ordinary course of business. Excluded from this aspect of the PE definition, however, are brokers, general commission agents, or other independent agents acting in the ordinary course of business (that is, entities whose purpose is acting on behalf of others regarding an activity). Under this second element of the definition of PE, a person that has a dependent agent that acts on its behalf in Canada and through whom it makes supplies in the ordinary course of business will be considered to have a PE at the agent's fixed place of business in Canada.

Whether an agent is considered to be dependent or independent depends on the facts. However, in the CRA's view, a dependent agent will typically be subject to control by the person, will not bear the risk of loss, will make supplies in the person's (rather than the agent's) name, and will not act as agent for other parties.[28] When a dependent agent is found to exist, it must be determined whether the agent has a fixed place of business according to the factors and rules described above. Note that a dependent agent does not necessarily need to have authority to conclude contracts on behalf of a particular person in order to be a person through whom that particular person is making supplies.

*b. Place Through Which the Particular Person Makes Supplies.* A fixed place of business is not enough, in and of itself, to qualify as a PE. The place of business must also be a ''place through which the particular person makes supplies.'' The CRA has said that this requires the activity undertaken at the place of business to be ''an essential and significant part of the particular overall business activity of the person'' and ''a large degree of involvement through the fixed place of business in making or facilitating supplies by the person'' must exist.[29]

Primary factors, the presence of any of which is enough to indicate that supplies are being made through a fixed place of business, include the following:

- authority at the fixed place of business to enter into contracts or to accept purchase orders that is regularly exercised;
- the manufacturing or production of goods supplied by the person at the fixed place of business;
- services supplied by a person that are performed at the fixed place of business; or
- performance of the service of maintaining equipment supplied by the person at the fixed place of business.

Secondary factors that may indicate that supplies are being made through a fixed place of business include soliciting or receiving orders; arranging for contracts; providing for storage, packing, shipping, or transportation of goods; providing for general administration of accounts; advertising for a supply; or providing customer follow-up and support. While no one of these factors is solely sufficient to indicate that supplies are being made through a fixed place of business, a combination of these secondary factors may meet that threshold. However, a fixed place of business will not qualify as a PE if it is used exclusively for activities that are of a preparatory or auxiliary nature (that is, activities that serve to make the business ready or that are designed to help or support the main business).

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[28]*Id. See also* CRA, GST/HST Policy Statement P-182R, ''Agency'' (July 2003).

[29]*Id.*

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## II. Selling Into Canada

While the rules regarding who must pay GST/HST and who must collect GST/HST are of general application, nonresidents will have compliance obligations only if their activities in Canada surpass a specific threshold.

When nonresidents sell into Canada, the GST/HST requirements for registration, which determine whether a person is required to charge GST/HST on sales made in Canada, may be different than those that apply to Canadian residents. This section discusses:

- when a nonresident may be required to register for, charge, and collect GST/HST;
- when a nonresident may voluntarily register;
- security requirements that may apply to registered nonresidents; and
- the GST/HST consequences associated with importing goods, services, and intangibles into Canada, which will apply regardless of whether a nonresident is registered.

### A. Nonresident Requirements for GST/HST

A nonresident will be required to register for GST/HST if:

- the nonresident makes taxable supplies in Canada in the course of a commercial activity[30] engaged in by the nonresident in Canada;
- the nonresident carries on business in Canada; and
- the nonresident is not a small supplier.[31]

Even with these requirements, when a nonresident makes taxable supplies through a PE in Canada, the nonresident will be required to register for GST/HST unless the nonresident is a small supplier. Also, as discussed below, the existence of a PE in Canada will be taken into consideration in determining whether a nonresident is carrying on business in Canada.

*1. Taxable Supplies Made in Canada*

The general charging provision for GST/HST requires the payment of GST/HST only for a ''taxable supply made *in* Canada'' (emphasis added).[32] Therefore, to the extent that a supply is considered to be made outside Canada, it falls outside the scope of the general GST/HST charging provision, with the result that the supply will not be subject to GST/HST.

Determining whether a taxable supply is made in Canada involves a two-step inquiry:

- Is the supply considered to be made in Canada under the general ''place of supply'' rules? If no, GST/HST will not apply to the supply. If yes, the second question must be answered.
- Does the ''nonresident override rule'' (described below) apply to deem the supply to be made outside Canada? If yes, GST/HST will not apply to the supply. If no, GST/HST will apply to the supply.

*a. Place of Supply Rules.* The general place of supply rules[33] in the ETA consider the following types of supplies to be made in Canada in the following circumstances:

- goods supplied by way of sale that are delivered or made available in Canada;
- goods supplied other than by way of sale (for example, by lease) under which possession or use is given or made available in Canada;
- intangibles that may be used in whole or in part in Canada or that relate to real property or goods situated in Canada or services performed in Canada;
- real property situated in Canada or services in relation to real property situated in Canada; and
- services performed in whole or in part in Canada.

*b. Nonresident override rule.* An additional deeming rule, known as the ''nonresident override rule,''[34] effectively overrides the general place of supply rules described above when determining whether a supply is considered to be made in or outside Canada.

The nonresident override rule will apply to deem a supply made by a nonresident in Canada to be made *outside* Canada, *unless* one of the following three exceptions to the nonresident override rule applies:

- the supply is made in the course of a business carried on in Canada (discussed further below);
- the nonresident is registered for GST/HST at the time the supply is made; or
- the supply is of an admission regarding a place of amusement, a seminar, an activity, or an event where the nonresident did not acquire the admission from another person.

When the nonresident override rule applies, the nonresident supplier is relieved from the obligation to collect GST/HST on supplies that would otherwise be considered to be made in Canada.

[30]A commercial activity is, generally, a business or an adventure in the nature of trade for which there is a reasonable expectation of profit, or any supply of real property, but that does not include the making of exempt supplies.

[31]A ''small supplier'' is, generally, a person who, together with its associated entities, makes less than C $30,000 per year worldwide in supplies that if made in Canada would be subject to GST/HST. Any member of a corporate group with annual consolidated worldwide revenues in excess of C $30,000 will be unlikely to be considered a small supplier. *See* ETA section 123(1), ''small supplier.'' *See also* CRA, GST Memoranda (New Series) 2.2, ''Small Suppliers'' (May 1999).

[32]ETA section 165(1).

[33]ETA section 142.

[34]ETA section 143(1).

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A nonresident who is registered for GST/HST purposes or who, under the rules discussed above, is required to be registered cannot rely on the nonresident override rule and must collect GST/HST on all taxable supplies made in Canada. Large organizations with multiple divisions should be aware that registration is generally at the legal entity level. Accordingly, if a branch has registered for GST/HST purposes, other branches of the same corporation will not be able to rely on this rule.

If a nonresident is making taxable supplies into Canada in the course of a commercial activity, an analysis of whether the nonresident is carrying on a business in Canada is crucial to determining whether the nonresident override rule applies.

*2. Carrying On Business in Canada*

The effects of carrying on business in Canada for a nonresident are twofold. First, the nonresident override rule, described above, will not apply to deem supplies made by the nonresident in Canada to be made outside Canada. Second, the nonresident will be required to register for GST/HST if it makes a taxable supply in Canada in the course of a commercial activity engaged in by it in Canada.

The concept of ''carrying on business in Canada'' is not defined in the ETA. According to the CRA's policy statement on carrying on business in Canada,[35] whether a nonresident will be considered to be carrying on business in Canada for GST/HST purposes is a question of fact that requires consideration of all the relevant circumstances in accordance with general legal principles. Jurisprudence on income tax, as well as GST/HST, should be considered for this purpose.

While the test for determining whether a nonresident is carrying on business in Canada for GST/HST purposes is similar to the test used for income tax purposes, the two tests are not identical. The definition of business in the ETA, which includes any activity engaged in on a regular and continuous basis and involves the supply of property by way of lease, license, or similar arrangement,[36] is broader than the definition of business in the ITA.[37] Further, there is no requirement that an activity be carried on with a reasonable expectation of profit in order to qualify as a business under the ETA. Also, unlike the ITA, the ETA does not use an extended definition of carrying on business. As such, a nonresident can be considered to be carrying on business for GST/HST purposes but not for income tax purposes (and vice versa).

The CRA's administrative position is that a nonresident person must have a ''significant presence'' in Canada to be considered to be carrying on business in Canada.[38] Isolated transactions in Canada that are undertaken by a business being carried on outside Canada will typically not be sufficient to show that a nonresident is carrying on business in Canada, particularly when the factors described below do not so indicate. The factors that the CRA will consider to determine whether a nonresident is carrying on business in Canada are:

- where agents or employees of the nonresident are located;
- the place of delivery;
- the place of payment;
- where purchases are made or assets are acquired;
- the place from which transactions are solicited;
- the location of assets or an inventory of goods;
- where the business contracts are made;
- the location of a bank account;
- where the nonresident's name and business are listed in a directory;
- the location of a branch or office;
- where the service is performed; and
- the place of manufacture or production.

According to the CRA's policy statement, the importance or relevance of a given factor will depend on the nature of the activity undertaken by the nonresident, as well as the particular facts and circumstances of each case. Judgment must be exercised to determine the importance of each factor in the context of what the nonresident is doing. For example, factors that would be more relevant when the nonresident leases property in Canada are the place where the property is acquired by the nonresident lessor and the place where the property is delivered to the lessee. Regarding services, the most relevant factors will generally be where the services are performed and where the employees are located when the services are the principal object of the contract (as opposed to services that are ancillary to the provision of property).

Further, with the rise and expansion of electronic commerce, some of the factors that are relevant in the context of more traditional business activities may not apply, or should be modified to account for, supplies made via the Internet.

Ultimately, the determination of whether a nonresident is carrying on business in Canada will depend on the application of the factors listed above to the particular facts and circumstances surrounding a nonresident's activities in Canada. The nature of the supply being made, as well as the way in which the business activity is conducted, will influence the way in which those factors will be applied in each case.

[35] CRA, GST/HST Policy Statement P-051R2, ''Carrying On Business in Canada'' (Apr. 29, 2005).

[36] ETA section 123(1), ''business.''

[37] ITA section 248(1), ''business.''

[38] *Supra* note 35.



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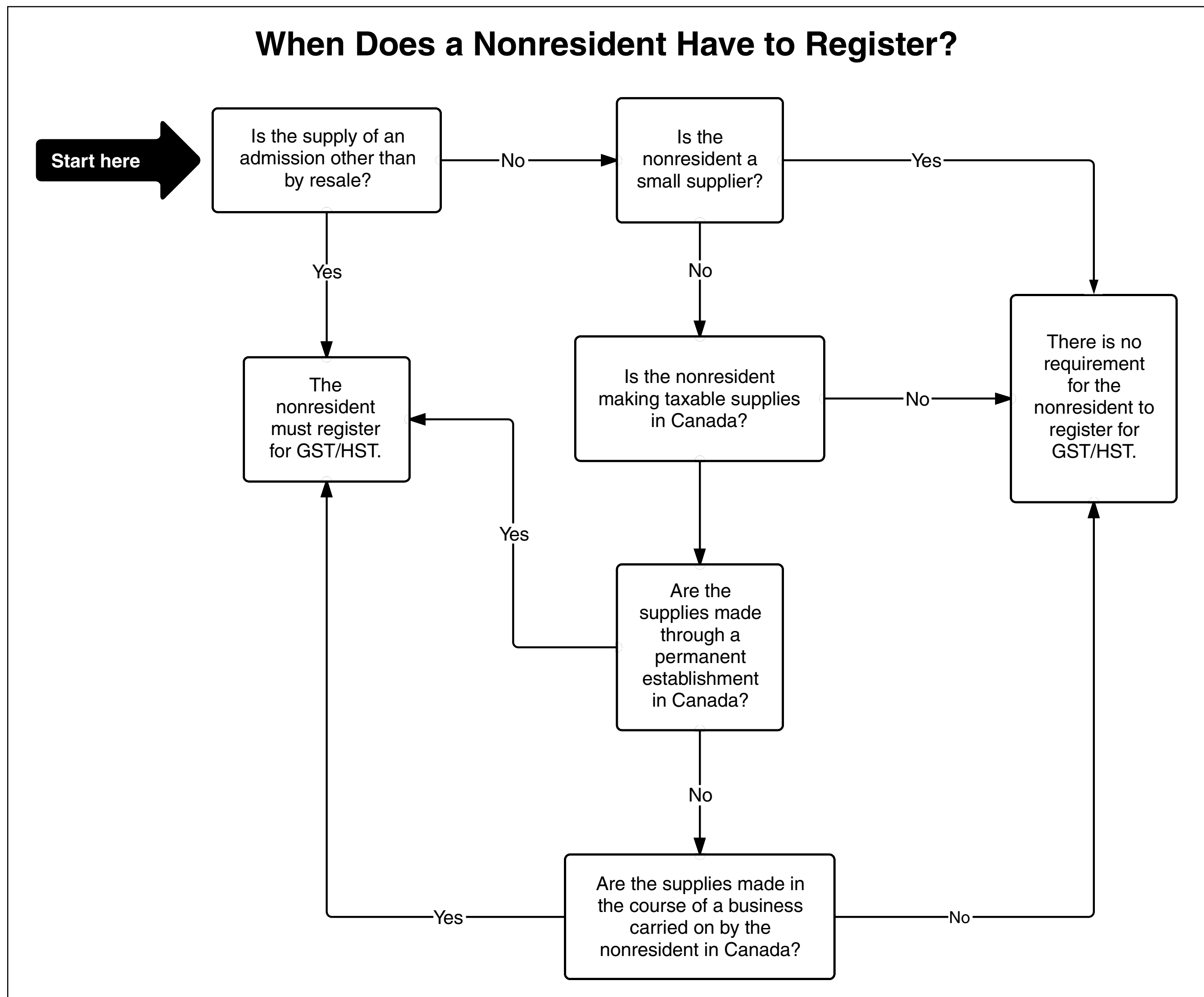


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## B. Voluntary Registration

As discussed above, if a nonresident makes taxable supplies in Canada in the course of a commercial activity and carries on business in Canada, the nonresident is generally required to register for GST/HST. Nonresidents who are not required to register for GST/HST may wish to register voluntarily.[39] Voluntary registration permits nonresidents who incur GST/HST costs in the course of making supplies into Canada to recover any GST/HST they pay in the course of making those supplies by claiming ITCs.

Voluntary registration is available when the nonresident:

- is engaged in a commercial activity in Canada; or
- in the ordinary course of carrying on business outside Canada:
  - — regularly solicits orders for goods for export to, or delivery into, Canada; or
  - — has entered into an agreement to supply services to be performed in Canada or to provide intangibles to be used in Canada or that relate to real property or goods situated in Canada, or services to be performed in Canada.

As discussed above, a nonresident who has voluntarily registered for GST/HST cannot rely on the nonresident override rule and must charge, collect, and remit GST/HST on any taxable supplies it makes in Canada. This exception to the nonresident override rule is reasonable: If a nonresident voluntarily registers to obtain the ability to recover any GST/HST it pays in Canada, it should be required to charge GST/HST on the supplies for which it has recovered GST/HST.

[39]ETA section 240(3).

For nonresident corporations with multiple divisions, voluntary registration by one division may affect the entire corporation. The CRA has asserted in at least one case that once one division of a nonresident corporation is registered for GST/HST, the entire nonresident corporation is considered to be registered.[40] Nonresident corporations therefore should be aware that registering one division may bring the entire corporation into the GST/HST compliance regime.

### C. Security Requirements

A nonresident who registers for GST/HST (whether compulsorily or voluntarily) must provide the CRA with a security deposit if:

- the nonresident does not have a PE in Canada; or
- the nonresident makes supplies in Canada only through another person's fixed place of business.[41]

The purpose of this security deposit requirement is to protect the CRA's ability to recover GST/HST collected by a nonresident from its customers in Canada.[42]

According to the CRA's administrative policy, the amount of security required to be posted is normally equal to 50 percent of the net tax (whether refundable or payable) that is expected for the 12-month period following registration, subject to a minimum of C $5,000 and a maximum of C $1 million.[43] Following the initial 12-month period, the amount of security required will be equal to 50 percent of the net tax for the nonresident's previous 12-month period. An exception to the requirement to post the minimum security amount of C $5,000 is made for nonresidents who make taxable supplies (including zero rated supplies) in Canada of less than C $100,000 annually and whose annual net tax or refund is C $3,000 or less. The CRA will review annually the amount of security required by a nonresident. If the security deposit is considered inadequate, the CRA may require it to be topped up.

While no specific penalties apply to a nonresident that has failed to comply with the security requirements described above, when a nonresident fails to post or maintain the required security, the CRA is authorized to retain any GST/HST refund or rebate to which the nonresident may otherwise be entitled.[44] In that case, the amount of the refund or rebate retained is deemed to have been paid to the nonresident and then paid back to the CRA as security. The amount retained by the CRA cannot exceed the difference between the security amount required and the amount actually posted by the nonresident.

### D. Importing Goods, Services, and Intangibles

*1. Goods*

The rules that apply to importing goods into Canada cover situations when:

- a nonresident imports goods for its own use in Canada;
- a nonresident imports goods to sell to a customer in Canada; or
- a customer imports goods into Canada after purchasing them from a nonresident outside of Canada.

*a. Importing Into Canada.* GST applies at a rate of 5 percent on the duty-paid value of most goods imported into Canada for commercial purposes.[45] The definition of goods in the ETA[46] is identical to the definition in the Customs Act (Canada)[47]; therefore, GST/HST on the importation of goods applies to the same goods that could be subject to customs duties when imported into Canada. GST payable is determined based on the total value of the goods.

Imported goods must be declared and reported to the Canada Border Services Agency (CBSA) by the importer of record, as named on the customs documents. It is the importer of record who is responsible for accounting for the imported goods and who is liable to pay the GST. Tax on the imported goods becomes payable along with any applicable customs duties when the goods are released by the CBSA. For GST/HST purposes, the importer of record must be distinguished from the de facto importer, who is the person who causes the goods to be imported into Canada and is generally the owner of the goods. This distinction matters because while it is the importer of record that pays tax on the importation of goods into Canada, it is the CRA's position that, absent certain relieving provisions in the ETA discussed below, only the de facto importer can claim an ITC and therefore

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[40]CRA, GST Headquarters Interpretation Letter HQR8405, ''Non-resident Registrant'' (Dec. 6, 1999).

[41]ETA 240(6). *See also* CRA, GST/HST Memoranda (New Series) 2.6, ''Security Requirements for Non-Residents'' (May 1999) [N.M. 2.6].

[42]Security in Canadian funds may be posted in the form of cash or acceptable securities, such as a transferrable Government of Canada Bond. As the CRA does not pay interest, it is generally preferable to use a noncash alternative.

[43]For example, a nonresident that expects to collect GST/HST of C $100,000 in the first year and pay C $30,000 of recoverable GST/HST in the course of its commercial activities will be required to provide security of C $35,000 ((C $100,000 - C $30,000)/2 = C $35,000).

[44]ETA section 240(7).

[45]ETA section 212. Under Schedule VII of the ETA, a limited list of goods that are not subject to duty under the Customs Tariff, SC 1997, c. 36, are designated as nontaxable imports and are not subject to GST/HST on importation.

[46]ETA section 123(1), ''goods.''

[47]Customs Act, RSC 1985, c. 1 (2nd Supp.), section 2, ''goods.''



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recover the tax paid on importation.[48] While the importer of record and the de facto importer often can be the same person, in some cases they are not as a result of industry-specific practices.

When the nonresident importer of record is also the de facto importer and registered for GST/HST, the GST/HST consequences are fairly straightforward — the importer of record will pay the GST to the CBSA at the time of importation and will be entitled to an ITC regarding the tax paid to the extent that the imported goods are for use in the nonresident's commercial activities in Canada. The nonresident will then charge GST/HST at the applicable rate to its customers on the sale price of the goods. However, if the nonresident is not registered for GST/HST, the nonresident will not be entitled to claim ITCs.

Relief for the nonresident in this situation may be available through the mechanism of ''flow-through ITCs.''[49] Flow-through ITCs may be available when the nonresident subsequently sells the imported goods in Canada to a GST/HST registrant. The registrant customer is deemed to have paid the tax that was paid by the nonresident at the border on the importation of the goods and is eligible to claim an ITC.

The flow-through ITC mechanism is also available to nonresidents who give physical possession of goods to a GST/HST registrant so that the registrant can provide a commercial service to the nonresident.

To flow ITCs through to a registrant customer, a nonresident must provide the registrant with satisfactory evidence that the GST was paid on the goods upon importation.[50] The registrant must also be able to demonstrate its relationship with the nonresident and the relevant goods.

When a nonresident supplies goods to a Canadian customer outside Canada and then imports the goods into Canada on behalf of the Canadian customer, an issue arises as to whether the tax paid at the border on importation is recoverable, and if so, by whom. For example, when legal delivery of the goods takes place outside Canada, but the goods are imported by a nonresident before they are delivered to the Canadian customer, the nonresident may consider itself the de facto importer. However, a problem arises because the nonresident is not consuming, using, or supplying the goods in Canada and therefore should not be entitled to an ITC regarding the tax paid at the border. The CRA generally maintains that the nonresident is not entitled to claim an ITC regarding the tax paid on the importation of the goods because either the nonresident did not own the goods at the time of importation or the nonresident was not a registrant.[51] Further, because the purchaser did not pay the tax in this situation, it also is not entitled to an ITC under the general rules.

A new provision was introduced in the ETA in 2003 to address this problem.[52] When goods are supplied to a Canadian purchaser outside Canada, the provision deems the GST paid on importation to have been paid by the nonresident importer of record acting as the agent of the Canadian purchaser. In turn, the Canadian purchaser is treated as a ''constructive importer'' and is deemed to have paid the GST on importation, which enables it to claim the ITC as long as the goods are to be used in the course of the purchaser's commercial activities. Another option for relief permits the nonresident supplier and the Canadian customer to deem the sale to take place in Canada when the nonresident is registered for GST/HST. The nonresident would thereby be entitled to claim an ITC for the tax paid on the importation of the goods and would charge the Canadian customer GST/HST on the sale price of the goods. Similar relief may be available for third parties who are engaged by the nonresident to import goods into Canada on behalf of a Canadian purchaser.

There is a potential for double taxation when a supply is made in Canada by a registered nonresident supplier and the Canadian customer is the importer of record. In this situation, the nonresident supplier delivers the goods in Canada and the Canadian customer pays GST at the border. However, the nonresident supplier is also required to collect GST/HST from its customer since the supply of the goods will be considered to be made in Canada. The customer will therefore pay tax on the same goods twice. When the customer is entitled to full ITCs, double taxation should not be an issue because the customer will claim ITCs twice. However, if the customer is not entitled to full ITCs (for example, it makes exempt supplies), it may not be able to fully recover all the tax it has paid. For customers that are not entitled to full ITCs, a better arrangement may be for the goods to be delivered outside Canada. When this strategy is used by a nonresident and a Canadian customer that is not entitled to claim full ITCs to avoid double taxation, the parties should ensure that all documentation reflects the fact that delivery took place outside Canada. Alternatively, the parties may choose to have the registered nonresident act as importer of record.

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[48]CRA, GST/HST Policy Statement P-125R, ''Input Tax Credit Entitlement for Tax on Imported Goods'' (June 1, 2007) [P-125R].

[49]ETA section 180.

[50]Satisfactory evidence includes Form B3, ''Canada Customs Coding Form,'' showing that tax was paid upon importation, or a sales invoice from a supplier to the nonresident showing that tax was paid or payable. *See* P-125R, *supra* note 48.

[51]GST/HST meeting between the CRA and the Canadian Bar Association Commodity Tax Section (Feb. 24, 2000), question 48.

[52]ETA section 178.8.

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*b. Importing Into an HST Province.* When goods are imported into an HST province, further considerations apply. Taxable noncommercial goods, except for motor vehicles required to be registered in the relevant province,[53] will be subject to the provincial portion of the HST (in addition to the federal GST portion of the HST) on importation.[54] Taxable noncommercial goods that are brought into a non-HST province are subject to the 5 percent GST only, although provincial sales taxes may also apply.[55]

The provincial portion of the HST will not be payable at the border for commercial goods that are imported into an HST province. However, the Canadian customer of the commercial goods may be required to self-assess, that is, determine on its own how much HST is payable and remit that HST on its own to the CRA, when the goods are brought into the relevant province.

While commercial goods imported into Canada are generally subject to the 5 percent federal GST portion of the HST, and in some cases, the provincial portion of the HST, commercial goods imported on a temporary basis may be eligible for relief from the tax in some circumstances.

*2. Services and Intangibles*

Unlike importations of goods, importations of services and intangibles are not subject to the 5 percent federal GST portion of the HST at the border. The most obvious reason for this distinction is that there would be no practical way to impose the tax at the border since services and intangibles generally do not physically ''cross'' it.

When a nonresident that is not registered (or required to be registered) for GST/HST performs services or provides intangibles to a Canadian customer, the nonresident will not charge GST/HST. If the Canadian customer acquires the services or intangibles 90 percent or more for use in its commercial activities, the customer will not have to self-assess or otherwise pay the 5 percent federal GST portion of the HST. If, however, the Canadian customer does not acquire the services or intangibles 90 percent or more for use in commercial activities, the customer will be required to self-assess the GST portion of the HST on the value of the services or intangibles and remit the tax to the CRA. A customer located in one of the HST provinces will generally be required to self-assess the provincial portion of the HST in addition to the 5 percent federal portion on services or intangibles that are not imported 90 percent or more for use in commercial activities in that province.

[53]When applicable, taxes will be levied and collected by the relevant province on the registration of the motor vehicle.

[54]ETA section 212.1. *See also* Guide RC4027, *supra* note 19, at 20.

[55]ETA section 212.

## III. Purchasing From Canada

The GST/HST considerations for a nonresident that simply purchases supplies from Canada, rather than selling supplies in Canada, are generally less onerous and more straightforward. Responsibility for ensuring the correct GST/HST treatment is applied to exported supplies typically lies, in the first instance, with the Canadian-resident supplier. Also, because the GST/HST is a tax on consumption, supplies that are ultimately consumed outside Canada generally will not be subject to the tax. Compliance requirements for such supplies generally focus on ensuring that the supplies are truly intended for consumption outside Canada.

### A. Exporting Goods, Services, and Intangibles

Under the general place of supply rules described above, goods delivered or made available outside Canada, services performed wholly outside Canada, and intangibles that cannot be used in Canada, among other things, do not attract GST/HST as they are considered to be supplies made outside Canada. However, different rules apply when goods, services, and intangibles are supplied in Canada and then exported. Most supplies of goods, services, and intangibles made in Canada and then exported for consumption outside Canada will be zero rated provided specific conditions are met.[56] Many exports therefore receive favorable GST/HST treatment since zero rating permits the supplier to claim ITCs for GST/HST paid to produce the supplies and the recipient does not have to pay GST/HST on the supplies. This results in no GST/HST being imposed on Canada's exports, either directly or indirectly.

*1. Goods*

Goods exported from Canada are generally zero rated for GST/HST purposes.

One zero rating provision of note may apply when some goods are delivered in Canada for export outside Canada. Such goods will be zero rated provided all the following conditions are met:

- the recipient exports the goods as soon after they are delivered to the recipient as is possible having regard to the facts of each situation (such as the type of goods involved and the normal business practices of the recipient);
- the recipient has not acquired the goods for consumption, use, or supply in Canada before exportation;
- the goods are not processed, transformed, or altered further in Canada after delivery and before exportation, except to the extent reasonably necessary or incidental for their transportation; and

[56]ETA Schedule VI, Part V.

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- the original supplier of the goods maintains satisfactory evidence of the exportation of the property by the recipient.

Regarding the third condition listed above, the CRA has indicated that some services will not constitute further processing, transformation, or alteration, such as export labeling, consolidation, export packing or repacking, export crating, and dismantling for transportation purposes.[57]

Whether evidence of exportation is considered satisfactory will generally depend on whether the shipment of the goods can be traced from its origin in Canada to the point where it leaves Canada on its way to a foreign destination.[58]

When the conditions for zero rating described above are not met and GST/HST is charged to a nonresident regarding the exported goods, the nonresident may be entitled to claim a rebate to recover the tax paid.[59] The nonresident will generally be entitled to claim a rebate when the goods at issue were acquired for commercial use primarily (that is, more than 50 percent) outside Canada and were exported by the nonresident from Canada within 60 days of delivery. However, alcoholic beverages; tobacco products; and gasoline, diesel fuel, and other motive fuels will not be eligible for the rebate under any circumstances.

*2. Services*

Services performed wholly outside Canada are considered to be supplied outside Canada under the general place of supply rules described above and therefore are not subject to GST/HST. However, services that are performed in whole or in part in Canada are considered to be supplied in Canada.

Many services supplied in Canada to a nonresident are zero rated for GST/HST purposes.[60] For example, many advisory, professional, consulting, and research services are zero rated. Agency services provided to a nonresident are also zero rated in many circumstances.

*3. Intangibles*

Intangibles supplied to unregistered nonresidents are generally zero rated,[61] with the following exceptions:

- intangibles supplied to an individual who is in Canada when the supply is made;
- intangibles that relate to real property or goods situated in Canada;
- intangibles that relate to services provided in Canada that are not zero rated as an export, transportation service, or financial service;
- intangibles that can be used only in Canada; and
- intangibles available for use in providing a telecommunication service.

Intellectual property (for example, an invention, trade secret, trademark, trade name, copyright, or industrial design) is zero rated when supplied to an unregistered nonresident.

*4. Proof of Residence and Registration Status*

For an export to be eligible for zero rating, the exported supply must be made to a nonresident. The CRA's administrative position is that registrant suppliers are responsible for determining the residency and registration status of their customers.[62] The CRA has indicated that before proceeding to zero rate a supply, a supplier should verify and obtain satisfactory evidence that the recipient of the supply is a nonresident under the ETA.[63] When it is a condition of zero rating that the nonresident is unregistered for GST/HST, the supplier should obtain satisfactory evidence of that requirement. While obtaining such evidence is not a legislative requirement, complying with the CRA's administrative position will undoubtedly make matters easier for a vendor should an issue arise on audit. As such, vendors have a strong incentive to ask their nonresident customers for evidence of residence and registration status.

## B. Purchasing and Reselling in Canada

When an unregistered nonresident purchases goods from a Canadian vendor and subsequently resells those goods to a customer in Canada, the transfer of the goods directly from the vendor to the customer may be characterized as a drop shipment and is subject to special rules.

[57]Guide RC4027, *supra* note 19, at 25.

[58]CRA, GST/HST Memoranda (New Series) 4.5.2, ''Exports — Tangible Personal Property'' (Nov. 1997). Satisfactory evidence of exportation includes a certificate from an export trading house, a copy of a sales invoice or purchase contract that identifies the goods and the recipient (which should be matched with the respective shipping or delivery instructions on the purchase order), a copy of the transportation document that describes the delivery of service (for example, a bill of lading), customs brokers' or freight forwarders' invoices that relate to the exported goods or shipments of exported goods, import documentation required by the country to which the goods are exported, and any other evidence not generated internally by the recipient that is satisfactory to the CRA to show that the goods have been exported.

[59]ETA section 252(1).

[60]ETA Schedule VI, Part V.

[61]*Id.* at section 10.1.

[62]CRA, GST/HST Memoranda 4.5.1, ''Exports — Determining Residence Status'' (Mar. 1998), at para. 16.

[63]The CRA has provided a sample of the documentation that it will generally accept as proof that a person is a nonresident, or a nonresident and a non-registrant, in one of its administrative publications. This sample is not the only form that will be accepted, however, and the CRA has indicated that it will consider other forms of documentation as proof of nonresident and nonregistered status. See *id.*

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The drop shipment rules apply when a GST/HST registrant makes a taxable supply in Canada of a service of manufacturing or producing goods for the nonresident person, or acquires physical possession of goods for the purpose of making a taxable supply of a commercial service regarding the goods to the nonresident.

The drop shipment rules ensure that GST/HST is collected and remitted for an arrangement that is essentially a sale in Canada between a Canadian vendor and a Canadian customer with a nonresident in the billing chain. The rules also simplify GST/HST compliance for nonresidents in some circumstances by relieving them of the obligation to pay GST/HST.

Possession of the goods in these circumstances is generally transferred directly from the Canadian vendor to the Canadian customer. However, a Canadian service provider may also perform some commercial services regarding the goods, such as further manufacturing, repair, or storage before final delivery to the Canadian customer.

*1. Drop Shipments to GST/HST Registrants*

Under the general rule, when a Canadian vendor delivers the goods in Canada to a Canadian customer on behalf of a nonresident, the Canadian vendor would be required to collect GST/HST from the nonresident. The GST/HST is calculated on the fair market value of the goods at that time.

However, when the Canadian vendor delivers the goods in Canada to a GST/HST registrant (known as a ''consignee''), the consignee may issue a drop shipment certificate to the Canadian vendor with the result that the Canadian vendor is not required to collect GST/HST from the nonresident. In the same way, each person in the supply chain that is a GST/HST registrant and supplies a commercial service for the goods may issue/accept a drop shipment certificate so that no GST/HST is required to be charged for each respective commercial service.

A drop shipment certificate also ensures that each consignee acknowledges that it may be liable for any GST/HST applicable to the goods if the conditions for it to issue the certificate are not met.

To be valid, a drop shipment certificate must contain the following information:

- the consignee's name and business number;
- an acknowledgment that the consignee has taken or will take physical possession of the goods;
- a statement that the goods are acquired for the purpose of performing a commercial service on them or that they are for the consignee's consumption, use, or supply; and
- an acknowledgement that the consignee assumes liability to pay or remit any GST/HST that may become payable.

Blanket drop shipment certificates can be used to cover more than one transfer of possession of goods from a Canadian vendor to a consignee.

*2. Transfers to a Carrier or Warehouse*

When the Canadian vendor transfers possession of the goods to a carrier or warehouse (known as a ''bailee'') and instructs the bailee to transfer the goods to a third party, the third party must provide a drop shipment certificate in order for GST/HST not to apply to the sale of the goods from the Canadian vendor to the nonresident.

If the nonresident has not found a purchaser for the goods and the Canadian vendor transfers the goods to a warehouse for storage until a purchaser is found, the Canadian vendor does not have to charge GST/HST to the nonresident at the time the goods are transferred to the warehouse. However, the Canadian vendor will be liable for GST/HST on the fair market value of the goods when the goods are ultimately transferred to the purchaser or to a consignee unless the Canadian vendor receives a drop shipment certificate from the purchaser or consignee.

When the goods are transferred to a warehouse and then released to the nonresident, the Canadian vendor will be required to collect GST/HST. However, if the nonresident plans to sell the goods to a Canadian customer and the goods will remain in Canada, the nonresident can instruct the warehouse to issue a drop shipment certificate to the Canadian vendor so that the nonresident can avoid paying GST/HST to the Canadian vendor. In that case, the warehouse operator will become liable to collect the tax from the nonresident unless the warehouse operator receives a drop shipment certificate from the purchaser or a consignee to whom the goods are ultimately transferred.

*3. Exports*

When a Canadian transfers goods to a person outside Canada or to a carrier, or mails the goods for delivery to a person at a place outside Canada on behalf of a nonresident vendor, the Canadian is not required to collect GST/HST. This treatment also applies when a Canadian causes physical possession of goods to be transferred at a place in Canada to a nonresident person or to any other person for export, if specific conditions are met, such as maintaining evidence of export.

## IV. Leasing Into and Out of Canada

When possession or use of property is given or made available in Canada under a lease, license, or similar arrangement from a lessor to a lessee, the supply will be deemed to be made in Canada under the general place of supply rules. A nonresident lessee will have to pay GST/HST on the lease payments unless the lease is zero rated. When the nonresident is the lessor, the nonresident will be required to charge GST/HST on the lease payments unless the nonresident is not a GST/HST registrant.

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When possession or use of property is given or made available outside Canada under a lease, license, or similar arrangement, the lease payments should not attract GST/HST because the supply will be deemed to be made outside Canada under the general place of supply rules.

For the purposes of determining whether a lease is made in or outside Canada, the CRA has indicated that possession or use of property is given or made available at:

- the place where the lessee obtains physical possession of the property at the time the agreement is entered into; or
- the place where the lessee may obtain or have access to the property, in situations in which physical possession of the property is not obtained at the time the agreement is entered into.

In general, the place where possession or use of the leased property is given or made available is based on the location of the property at the time the agreement is entered into. This is determined by looking at the terms of the agreement or, when there is no agreement or the terms are inconclusive, by looking at the actions of the parties. When lease payments are made on a periodic basis, a separate supply will be deemed to occur in each payment period in which a lease payment is made. However, for the purposes of determining where a lease is supplied, the CRA's view is that possession or use of the leased property is given or made available only once under the lease agreement at the beginning of the lease. As such, even though each payment period is deemed to be a separate supply, the place of supply of the lease for the purposes of determining whether it is made in or outside Canada will need to be done only once.

However, if the lease is deemed to be made in Canada and is not deemed to be made outside Canada under another provision, or zero rated or exempt, the place of supply may need to be determined for each payment period for determining what province each supply is made in and, it follows, what rate of GST/HST to charge.

Nonresident lessors should be aware that administratively, the CRA asserts that a nonresident who delivers goods in Canada and supplies those goods by way of lease is generally considered to be carrying on business in Canada and is required to register for and collect GST/HST. Nonresident lessors who do not wish to assume the compliance obligations associated with registration generally ensure that the leased goods are delivered to the lessee outside Canada and are then imported by the lessee. While this generally means that the lessee must pay the applicable GST/HST based on the full value of the leased asset at the time of importation, this only raises a cash flow issue when the lessee is entitled to recover that amount by way of ITC. The nonresident lessor may be willing to assist the lessee with the costs associated with this cash flow issue to avoid greater compliance costs associated with GST/HST registration and filings.

## V. Conclusion

Whether doing business in Canada or doing business with Canada, nonresidents must keep in mind GST/HST compliance considerations when interacting with Canada. The compliance obligations for nonresidents who simply purchase goods, services, and intangibles from Canada will generally be less onerous than those that apply to nonresidents selling into Canada, particularly nonresidents who carry on business in Canada or nonresidents with PEs in Canada who will typically also be carrying on business in Canada. While the obligation to collect and remit GST/HST may not apply to an unregistered nonresident when the nonresident makes a supply to a GST/HST registrant, the recipient of the supply will instead have an obligation to self-assess and remit. When determining which GST/HST compliance obligations may apply to a nonresident's activities in or with Canada, it is usually prudent to consult a Canadian tax adviser who is familiar with the GST/HST issues applicable to nonresidents. Early advice on how to structure and plan a nonresident's Canadian affairs to account for the GST/HST may mean the difference between full and timely compliance with applicable GST/HST obligations and the imposition of unnecessary penalties, interest, and anxiety. ◆

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