



GST Transitional Rules for Construction Contractors November 2007

Effective January 1, 2008, the Goods and Services Tax ("GST") rate will be reduced from 6% to 5%, and the Harmonized Sales Tax ("HST") rate will be reduced from 14% to 13%.

The general transitional rule for the implementation of the GST reduction to 5% is based upon the time at which the GST in respect of a transaction becomes **payable**. Generally, GST is **payable** on the taxable supply of goods and services, on the earlier of the day payment is made and the day the supplier issues an invoice. The general transitional rules are as follows:

- If GST becomes **payable or is paid** before January 1, 2008, the rate of 6% will apply.
- If GST becomes **payable** and is not paid until after December 31, 2007, the rate of 5% will apply.

Often, construction contracts extend over a period of time in accordance with a written contract. The contract usually stipulates that a customer will make progress payments as the work on the project reaches certain levels of completion, as defined. The timing of when the progress payments are **payable** pursuant to the terms of the contract will generally determine when the GST liability arises.

Where a contract stipulates that predetermined amounts are **payable** on specific dates, the GST is **payable** by the customer on the earlier of (a) the day the particular payment becomes **payable** or (b) the day the customer makes the payment. This rule applies even if the customer does not make a payment, or makes a payment for less than the full amount.

Where a contract states that payments are to be **payable** within a certain number of days after the work is certified by a third party (such as a consultant, engineer or architect), a construction contractor's request for payment is not considered to be an invoice, as it is merely a request that a certificate for payment be issued, as stipulated in the contract. Consequently, the GST becomes **payable** by the customer on the amount shown on the certification on the earlier of (a) the day the customer makes the payment, or (b) the day the customer is required to pay the amount in accordance with the terms of the contract. For example, consider the case where a contractor issues a monthly progress application on December 27, 2007 for work completed in the previous 30 days and the contract stipulates that the amount is not **payable** until 10 days after certification by the engineers. If the work is certified by the engineers on January 5, 2008, the amount becomes **payable** by the customer on January 15, 2008 in accordance with the contract. Consequently, since the amount becomes **payable** after December 31, 2007, the GST should be charged at the rate of 5%. However, if the amount is paid by the customer before January 1, 2008, the GST should be charged at the rate of 6%.

The GST on a holdback pursuant to a written contract or in accordance with federal or provincial laws does not generally become **payable** until the earlier of (a) the day that the holdback is paid, and (b) the day the holdback period expires in accordance with the written contract or the federal or provincial laws, as applicable. Consequently, if a construction contract is subject to a statutory holdback, and the holdback period expires after December 31, 2007, the rate of GST that should be charged on the holdback is 5%, regardless of when the work was performed (provided the customer does not make the payment before January 1, 2008).

* * *

If you would like to discuss these issues further, please contact your advisor at Goldfarb, Shulman, Patel & Co. LLP.