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May 7, 2009

To: All Trade Associations

RE: Tax Treatment of Limited Time Offers and GST on Other Promotional Allowances

On April 9th, I issued a memo to all trade associations regarding the GST treatment of all promotional allowances. The LCBO has received a number of questions and this memo will clarify our position.

Tax Treatment of Limited Time Offers (“LTO”)

The LCBO treats the Limited Time Offer (“LTO”) program as a deferred price adjustment with no sales tax consequences. This treatment is based primarily on the underlying agreement outlined in the October 21, 2005 memo to the trade associations which indicated that, commencing period 4, 2007/08, the chargeback to the Supplier/Agent would be based fully on the difference between the regular and the LTO retail prices for products under this program.

A promotional allowance generally refers to situations in which a registrant, such as a retailer, acquires goods for sale in the course of its commercial activities and is paid, credited, or allowed a discount on future purchases by another registrant, such as a manufacturer, for the promotion of the goods by the retailer. The manufacturer must have originally sold the goods being promoted, though the retailer may have acquired them from a third party, such as a distributor.

Under the GST rules for promotional allowances, the LTO paid to the LCBO is deemed *not* to be consideration for a supply made by the LCBO to the manufacturer. Instead, where the LTO is provided by way of after-the-fact discount on, or credit against, the price of specific goods or services previously invoiced by the manufacturer, the allowance is considered an adjustment to the original sale price under subsection 232(2) of the *Excise Tax Act* (“ETA”). If the allowance is not provided by way of a credit or discount on goods sold by the manufacturer to the retailer (i.e., where it is paid by cheque), the amount allowed is deemed to be a rebate paid under section 181.1 of the ETA.

Under both subsection 232(2) and section 181.1, the tax status of the supplies made by the manufacturer determines whether or not GST is included in the adjustment or rebate, and at what rate. In addition, under both of these provisions, the person providing the credit or rebate (i.e., the supplier) has the option not to adjust tax on the credit or rebate.

The LCBO has consistently treated chargebacks under the LTO program as a deferred price adjustment. The amount of the retail discount provided to the consumer is fully charged back to the product supplier. In generating the debit note or invoice, the LCBO has always taken the position that the *option* to adjust tax has not been exercised, since no indication that GST is included in the price adjustment is provided to the supplier. In order to adjust the tax on these transactions, the legislation would require a credit or debit note, including prescribed information, to be issued in support of the adjustment.

The LTO program charge is also treated as a price adjustment for ORST purposes, with no tax being reflected in the chargeback amount. This is consistent with the fact that no ORST is generally payable by the LCBO on the acquisition of the product, which is purchased exempt from tax as goods for resale. Since ORST was not paid on the product acquisition, no tax should be included in any price adjustment related to that purchase.

The LCBO’s treatment of GST and ORST with respect to the LTO program is permitted within the ETA and Ontario *Retail Sales Tax Act*.



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Tax Treatment of Other Promotional Allowances

In addition to the LTO program, the LCBO has many other promotional programs in place for foreign and domestic suppliers. The letter I issued to the trade associations on April 9, 2009 has drawn inquiries from several suppliers regarding the potential implications of the change in the GST status of certain promotional programs. The change in GST status will have very few implications for most participants in these promotional programs.

Foreign Suppliers

The vast majority of supplies made by the LCBO under promotional programs to unregistered non-residents of Canada qualify for zero-rating under provisions in Part V of Schedule VI to the ETA. Please note that these zero-rating provisions generally require that the item in question qualify as an eligible service (based on the nature of the supply) and that the purchaser (in this case, the supplier making the payment to the LCBO) is in fact a non-resident, or an unregistered non-resident, as the case may be.

Furthermore, any deferred price adjustments (i.e., promotional allowances, volume rebates, etc.) in relation to supplies made by unregistered non-residents would generally not be subject to GST, since tax would not have been collected by the supplier on the original sale to the LCBO.

Domestic Suppliers

All domestic suppliers to the LCBO are GST registrants. As such, domestic suppliers are entitled to claim input tax credits for any GST paid on taxable supplies acquired in relation to their commercial (i.e., taxable) activities. Consequently, any change in the GST status of the LCBO's promotional programs should have no impact on the net tax position of its domestic suppliers, since any GST paid in relation to such programs will be fully recoverable as input tax credits.

If you require more information, please email either Carol Lyons, Controller carol.lyons@lcbo.com or Patrick Parainfo, Manager, Accounts Payable and Receivable patrick.parainfo@lcbo.com. Further details can be provided upon request.

Sincerely,

Shari Mogk-Edwards
Vice President, Merchandising

cc. B. Downey
B. Ewing
C. Lyons
P. Parainfo