

# GST/HST Technical Information Bulletin

October 2001

B-088

## EXPORT DISTRIBUTION CENTRE PROGRAM

This bulletin does not replace the law found in the *Excise Tax Act* and its Regulations. It is provided for your reference. As it may not completely address your particular operation, you may wish to refer to the Act or appropriate Regulation or contact any Canada Customs and Revenue Agency (CCRA) tax services office for additional information. If you are located in the Province of Quebec, please contact the Ministère du Revenu du Québec (MRQ) for additional information.

This bulletin reflects amendments to the *Excise Tax Act* contained in Bill C-13, which received Royal Assent on June 14, 2001.

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*More Ways to Serve You!*  
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La version française de ce bulletin de l'information technique (BIT) est intitulée  
*Programme de centres de distribution des exportations*

 Canada Customs and Revenue Agency    Agence des douanes et du revenu du Canada

**Canada**

## **Introduction**

The Export Distribution Centre Program (EDCP) permits eligible export-oriented businesses that do not manufacture or produce goods and that add limited value to goods in the course of their processing or distribution activities to use an EDCP certificate to acquire or import, without having to pay the GST/HST, most inventory, property to be added to other goods in the course of processing, and customers' goods on which processing services are provided. The EDCP came into force on January 1, 2001, and applies to supplies made after December 31, 2000, and to goods imported after December 31, 2000.

The EDCP is similar to the Export Trading House Program but allows for an expanded range of activities. As a result, legislative changes to the *Excise Tax Act* (the Act) have been made to the Export Trading House Program to align its rules with those of the EDCP. In addition, there have been legislative amendments to the Act to provide for the tax-free importation of replacement goods under warranty, to enhance the drop-shipment rules, and to expand the Exporters of Processing Services Program. A summary of these changes is found under the heading, Other Import/Export Related Changes.

## **Export Distribution Centre Program**

The EDCP targets specific relief for the cash-flow cost that can be incurred by export-oriented businesses that provide limited value added in the course of processing or distributing goods.

For those businesses purchasing or importing goods for export, the advantage of being authorized to use an EDCP certificate is the cash-flow benefit that derives from not having to pay tax at the time of purchase or importation of the goods and later claim back the tax as an input tax credit (ITCs). The same cash-flow advantage would accrue to businesses that import goods for the purpose of providing a service in respect of those goods. Without the benefit of the EDCP, such service providers would have to pay tax on the importation of the goods and later claim the offsetting ITCs. The EDCP rules simplify the system for both the service provider and the owner of the imported goods by relieving the goods of tax if the service provider has been granted an authorization under section 273.1.

Section 273.1 empowers the Minister of National Revenue to authorize the use of EDCP certificates where certain criteria are satisfied (as explained below).

## Eligibility Criteria

### Persons who are eligible

(ss 273.1(7))

A person who is registered for purposes of the GST/HST and who is engaged exclusively in commercial activities may apply to the Minister of National Revenue for authorization to use an EDCP certificate to purchase inventory or import certain goods on a tax-free basis. For the person to be so authorized, it must reasonably be expected that the following three criteria will be met:

- the person will not engage in the substantial alteration of property in the year;
- either the person's percentage value added attributable to non-basic services in respect of customers' goods for the year will not exceed 10% **or** the person's percentage total value added in respect of customers' goods for the year will not exceed 20%; and
- the person's export revenue percentage for the year will be at least 90%.

When a person first requests to be authorized under section 273.1, all of the eligibility tests will be applied, on the basis of reasonable expectations, with reference to the fiscal year of the person in which the authorization is to take effect. The actual value added and export revenue percentages would then be determined at the end of that year, and again at the end of each subsequent fiscal year for which the authorization was in effect, to determine if the person continued to be eligible to use the EDCP certificate.

### Substantial alteration of property

This first criterion relates to the nature of the person's business activities in the year. The term "substantial alteration of property" (defined in Appendix A) includes any activity that constitutes manufacturing or producing. A person whose activities are expected to include manufacturing or producing, or who engages another person for such activities, will not qualify for an authorization to use an EDCP certificate regardless of the extent of the value added by such activities.

"Substantial alteration of property" also refers to any processing undertaken by or for the person during the year if the specified limits on the extent of processing that may be undertaken by or for the person in respect of finished inventory are exceeded (i.e., if the person's percentage value added attributable to non-basic services in respect of finished inventory of the person for the year (as determined under subsection 273.1(2)) exceeds 10% and the person's percentage total value added in respect of finished inventory of the person for the year (as determined under subsection 273.1(3)) exceeds 20%). If the expectation is that **both** of these limits (the value-added thresholds) will be exceeded, the person does not qualify for an authorization to use an EDCP certificate. On the other hand, satisfying either the 10% or 20% value-added test means that the person will not be considered to be engaged in the substantial alteration of property.

For example, if a person's processing activities do not amount to the manufacture or production of goods, but consist solely of performing basic services (defined in Appendix A), the person is not considered to be engaged in the substantial alteration of property since the percentage attributable to non-basic services is nil. This is the case even if the person's percentage total value added from the performance of basic services in respect of the person's finished inventory for the year exceeds 20%. The eligibility criteria under the EDCP rules do not place any limits on the extent to which a person can add value to goods by the performance of basic services as long as the person's activities do not constitute manufacturing or producing, and there is no performance of non-basic services.

If a person performs some non-basic services but the person's percentage total value added in respect of the finished inventory for the year is below 20%, the person is not considered to be engaged in the substantial alteration of property, provided the person is not otherwise engaged in manufacturing or producing. Persons in such a position will have no need to further ascertain their percentage value added attributable to non-basic services in respect of the finished inventory since they will not have exceeded both thresholds.

To illustrate the application of these criteria, Example 1 below involves a person who operates a business that involves purchasing plain shirts and processing them for retailers according to their specifications. The business dyes the shirts according to the customers' orders for each colour option and sews on the customers' logos or emblems. It then tickets and individually packages the shirts in the coverings in which they will be sold to consumers by the retailers. The ticketing and packaging activities constitute basic services and the dyeing and sewing activities constitute non-basic services.

*Example 1 — Finished inventory — customized shirts*

Direct material cost per item	\$27.00
Labour cost per item:	
Non-basic services	\$4.20
Basic services	\$1.60
Other indirect cost per item	<u>\$0.70</u>
Total product cost per item	\$33.50
Percentage value added attributable to non-basic services ( $\$4.20 \div \$33.50$ )	12.5%
Percentage total value added ( $\$5.80 \div \$33.50$ )	17.3%

In this example, the business is not considered to be engaged in the substantial alteration of property because, although its percentage value added attributable to non-basic services exceeds 10%, the business's percentage total value added does not exceed 20%.

### Percentage value added in respect of customers' goods

A person's eligibility to use an EDCP certificate also depends on the extent and nature of the person's processing activities in respect of customers' goods (defined in Appendix A), as these activities are measured by the percentages determined under subsections 273.1(4) and (5).

To qualify for an authorization to use an EDCP certificate, it must reasonably be expected that either:

- the person's percentage value added attributable to non-basic services in respect of the customers' goods (as determined under subsection 273.1(4)) will not exceed 10%; **or**
- the person's percentage total value added in respect of those goods (as determined under subsection 273.1(5)) will not exceed 20%.

To illustrate the application of these criteria, Example 2 below involves a person processing goods for a fee as in Example 1, except that it performs this activity on its customers' goods that it has imported. The person imports 120,000 shirts in the year, each with a base value (i.e., the value for purposes of Division III (tax on importation of goods)) of \$27 per shirt.

*Example 2 — Imported customers' goods — customized shirts*

Total processing fees charged for the year	\$ 810,000
Processing fees attributable to non-basic services (70%)	\$ 567,000
Total of base values of customers' goods and processing fees for the year (3,240,000 + 810,000)	\$ 4,050,000
Percentage value added attributable to non-basic services (567,000 ÷ 4,050,000)	14%
Percentage total value added (810,000 ÷ 4,050,000)	20%

In this example, the business satisfies the value-added test with respect to its customers' goods because, although its percentage value added attributable to non-basic services exceeds 10%, its percentage total value added in respect of those goods does not exceed 20%.

### Export revenue percentage for the year is at least 90%

The final eligibility criterion that must be satisfied by a business in order for it to be authorized to use an EDCP certificate relates to the extent to which the business serves the domestic and export markets. The EDCP is aimed at export-oriented businesses.

To qualify initially for an authorization to use an EDCP certificate, the person's export revenue percentage for the year must reasonably be expected to be at least 90%. The export revenue

percentage of a person for a year is calculated by dividing the person's export revenue (defined in Appendix A) for the year by the person's specified total revenue (defined in Appendix A) for the year. The person's total export revenue for the year is generally arrived at by aggregating:

- its zero-rated export sales, and sales made outside Canada, of domestic inventory;
- its sales of added property acquired for use or supply in processing goods in Canada for export; and
- its sales of processing, storage and distribution services in respect of goods that are exported after the processing is complete.

To calculate the export revenue percentage for the year, a person takes into account only those inventory items, added property and customers' goods that have been acquired in Canada, imported into Canada or transferred to the business in Canada. The calculation of the export revenue percentage is not affected by the operations of a foreign branch that does not deal in goods that have been processed or acquired in Canada. The export revenue percentage is based entirely on the person's domestic business operations.

## **Authorization and Revocation of the EDCP Certificate**

### **Applying for authorization to use an EDCP certificate**

(ss 273.1(7) and (8))

A person who meets the eligibility criteria described above may apply to the Minister of National Revenue for authorization to use an EDCP certificate. The application for authority to use an EDCP certificate must be made in prescribed form containing prescribed information and be filed with the Minister of National Revenue in prescribed manner.

While an application form for the EDCP is being developed, eligible persons may apply in writing to the Verification and Enforcement Division of the nearest CCRA tax services office. The applicant must provide in its letter of application its Business Number, legal and trade names, and the date that it would like its application to be effective. Upon receipt of this letter, a representative from the Verification and Enforcement Division will contact the person to review its application. Once the review is complete, the person will be notified in writing of the decision concerning the application.

### **Notice of authorization to use an EDCP certificate**

(ss 273.1(9))

Where the Minister of National Revenue authorizes a person to use an EDCP certificate, the Minister will notify the person in writing of the authorization, its effective date, its expiry date, and the number assigned by the Minister that identifies the person or the authorization (i.e., Business Number). This information must be disclosed by the person when purchasing property on a zero-rated basis under section 1.2 of Part V of Schedule VI to the Act, or when accounting for imported goods where tax relief is being claimed under section 11 of Schedule VII to the Act.

Information on imported goods is found under the heading, Imported Goods Relieved under the EDCP.

### **Revocation**

(ss 273.1(10))

The Minister of National Revenue may, after giving a person reasonable written notice, revoke a person's authorization to use an EDCP certificate, effective on a day in a particular fiscal year of the person if:

- the person fails to comply with any condition attached to the authorization or with any GST/HST provision;
- it can reasonably be expected that
  - (i) the person will be engaged in the substantial alteration of property in that year;
  - (ii) the person's percentage value added that is attributable to non-basic services in respect of customers' goods for that year will exceed 10% **and** the person's total value added in respect of customers' goods for that year will exceed 20%; or
  - (iii) the person's export revenue percentage for that year will be less than 80%; or
- the person has requested in writing that the authorization be revoked as of that day.

### **Deemed revocation**

(ss 273.1(11))

Subject to subsection 273.1(10), a person's authorization to use an EDCP certificate is deemed to have been revoked immediately after the end of a fiscal year of the person if:

- the person had engaged in the substantial alteration of property in that year;
- the person's percentage value added attributable to non-basic services in respect of customers' goods for that year exceeds 10% **and** the person's percentage total value added in respect of customers' goods for that year exceeds 20%; or
- the person's export revenue percentage for that year is less than 80%.

The difference between the discretionary revocation authority of the Minister of National Revenue under subsection 273.1(10) and the automatic revocation under subsection 273.1(11) is that the Minister may revoke an authorization effective on any day in the year that the Minister specifies. For example, if it can reasonably be expected, given a change in a person's business, that the person will be engaging in manufacturing or producing, the Minister can revoke the person's authorization to use an EDCP certificate on a day specified in the revocation notice without waiting until the beginning of the next year for an automatic revocation to take effect.

While the initial eligibility criterion requires that a person's export revenue percentage be expected to be at least 90%, the authorization once obtained is not revoked under subsections 273.1(11) and (10) on the basis of this criterion unless the person's actual export revenue percentage falls below 80%. There is, however, an adjustment to net tax that is required under subsection 236.3(2) whenever the export revenue percentage is below 90% for any year in which the EDCP certificate was at any time in effect.

### **Cessation**

(ss 273.1(12))

An authorization to use an EDCP certificate ceases to have effect on the earlier of

- the day on which a revocation of the authorization becomes effective; and
- the day that is three years after the day on which the authorization became effective.

An authorization to use an EDCP certificate must be renewed every three years to remain valid. A person must apply to renew the authorization three months prior to the expiry date of the current authorization.

Where a person's authorization has been revoked or is deemed to be revoked, the person will not be granted a new authorization to use an EDCP certificate until a certain period of time has elapsed (see below).

### **Application after revocation**

(ss 273.1(13))

If a person's authorization is revoked because the person failed to comply with any condition attached to the authorization or any GST/HST provision of Part IX, a new authorization may not be granted for at least two years after the date of revocation.

If the authorization is revoked for any other reason (e.g., substantial alteration or value-added percentage thresholds exceeded), a new authorization may not be granted until the first day of the second fiscal year of the person beginning after the day on which the revocation is made (i.e., the person may not be granted a new authorization for at least one full fiscal year).

## **Zero-Rated Supplies for which an EDCP Certificate is Provided**

A registrant who is authorized to use an EDCP certificate may purchase inventory or goods to be added to customers' goods on a zero-rated basis. Section 1.2 of Part V of Schedule VI to the Act zero-rates a supply by way of sale of property to a recipient registered for GST/HST purposes where the recipient provides the supplier with an EDCP certificate (within the meaning of section 273.1) certifying that an authorization to use the certificate is in effect when the supply is made and that the property is being acquired for use or supply by the recipient as domestic inventory or as added property. The recipient must also disclose to the supplier the identification number (i.e., Business Number) of the recipient or the authorization to use the certificate as well



as the expiry date of the authorization. Another condition is that the total amount of consideration for eligible property purchased with the use of the certificate and included in a single invoice or agreement must be at least \$1000.

This zero-rating provision does not apply to excisable goods or to continuous transmission commodities to be transported by or on behalf of the recipient by means of wire, pipeline or other conduit. The latter are covered by separate zero-rating provisions.

Under section 1.2 of Part V of Schedule VI, the supply is zero-rated provided the above conditions are met and as long as the supplier did not know and could not reasonably be expected to have known that the recipient's authorization to use the certificate was not in effect or that the property was not being acquired for use or supply as domestic inventory or as added property. In this case, the recipient alone remains potentially liable under subsection 236.3(1) and/or under Division IV as a result of paragraph 217(e).

The EDCP certificate may be in the form set out in Appendix B.

Section 1.2 of Part V of Schedule VI applies to supplies made after 2000.

### **Imported Goods Relieved under the EDCP**

A registrant who is authorized to use an EDCP certificate may import goods on a non-taxable basis. Section 11 of Schedule VII to the Act provides relief from the GST/HST on the importation of inventory, added property or customers' goods by a person who has been authorized to use an EDCP certificate. When the goods are accounted for under section 32 of the *Customs Act*, the importer must certify that the importer's authorization to use an EDCP certificate is in effect and must disclose the identification number (i.e., Business Number) as well as the effective date and expiry date of the authorization. The importer must also provide any security that may be required under section 213.1. This provision applies to goods imported after 2000.

Persons with an EDCP certificate must indicate the authorization number 99-0000 in the special authority field (field 26) of Form B3, *Canada Customs Coding Form*, to obtain relief from paying the GST/HST on imported goods.

Persons who are authorized to participate in both the EDCP and the Duties Relief Program must indicate the authorization number 99-1111 in the special authority field (field 26) of Form B3, *Canada Customs Coding Form*, to obtain relief from paying the GST/HST and customs duties at the time of importation.

Persons who are not authorized to participate in the EDCP and/or the Duties Relief Program will have their accounting documents (Form B3, *Canada Customs Coding Form*) rejected, if they enter these codes on their Form B3.

## **Adjustments to Tax**

### **Net tax adjustments**

(s 236.3)

A registrant may be authorized by the Minister of National Revenue to provide an EDCP certificate to a supplier resulting in that supply being zero-rated under section 1.2 (zero-rated supply for which an EDCP certificate is provided) of Part V of Schedule VI to the Act. Subsection 236.3(1) deals with situations where an EDCP certificate is used to acquire property when the authorization to use the certificate is not in effect, or the property is not acquired for use or supply as domestic inventory or added property. In this case, the registrant is required, under subsection 236.3(1), to add an amount to the registrant's net tax. This addition to net tax reflects the fact that the registrant received a cash-flow benefit by acquiring the property on a zero-rated basis.

Subsection 236.3(1) requires the recipient to add an amount to the net tax of the recipient for the reporting period that includes the earliest day on which tax would have become payable in respect of the supply if it had not been received on a zero-rated basis. The amount required to be added is equal to interest, at the rate prescribed for purposes of paragraph 280(1)(b) plus 4% per year compounded daily, calculated on the total amount of tax that would have been payable in respect of the supply. The prescribed rate of interest is the rate in effect on the earliest day on which tax would have become payable in respect of the supply. It is computed for the period beginning on the earliest day on which tax would have become payable in respect of the supply and ending on the due date for the return for the reporting period that includes that day.

Subsection 236.3(2) requires a net tax adjustment where a registrant's export revenue percentage for a fiscal year is less than 90% or the registrant's authorization to use an EDCP certificate to acquire property on a zero-rated basis is deemed to have been revoked effective immediately after a fiscal year. Subsection 236.3(2) requires the registrant to add an amount to the registrant's net tax for the first reporting period that follows that fiscal year.

The amount required to be added to net tax is equal to the total tax that would have been payable in respect of purchases and importations for which the registrant used the EDCP certificate in the year multiplied by an interest rate, for one month, based on 4% per year plus the annualized prescribed rate of interest in effect on the last day of the first reporting period following the year. This adjustment recognizes that a cash flow benefit was obtained in using the certificate which, on average, would have been enjoyed for a period of one month.

The calculation of the adjustment under subsection 236.3(2) does not include any purchase that is included in determining a net tax adjustment under subsection 236.3(1).

Section 236.3 applies to supplies made after 2000.

### **Self-assessment**

Paragraph 217(e) of the definition of imported taxable supply includes a supply of property that is zero-rated by virtue of section 1.2 of Part V of Schedule VI to the Act where the recipient is

not acquiring the property for consumption, use or supply exclusively in the course of its commercial activities, and

- the authorization for the recipient to use the EDCP certificate is no longer in effect, or
- the recipient is not acquiring the property for use or supply as domestic inventory or as added property.

The recipient would therefore be required to self-assess tax under Division IV.

Where paragraph 217(e) applies, subsection 236.3.(1) will also apply.

Paragraph 217(e) applies to supplies acquired after 2000.

## **Other Import/Export Related Changes**

### **Drop-shipments**

(ss 179(2), (3) and (7))

The following changes have been made to the drop-shipment rules:

- The supply of storage services is now included among those services that can be provided tax free under the drop-shipment rules.
- The use of railway rolling stock in the course of its exportation qualifies for tax-free treatment, provided that the railway rolling stock is exported within 60 days after the supplier transfers physical possession of it to the exporter.

These two amendments apply to supplies for which all of the consideration became due after February 28, 2000, or was paid after that day without having become due.

Information on the rules respecting drop-shipments is available in GST/HST Memorandum 3.3.1, *Drop-Shipments*.

### **Export Trading House Program**

(s 236.2 and Sch. VI, Part V, s 1.1)

The Export Trading House Program has been changed to align its rules with those of the EDCP. As a result, upon revocation of its authorization or where there has been improper use of the certificate, an export trading house will be required to make adjustments to its net tax to ensure that no cash-flow benefits are realized from having used the certificate.

Information on the Export Trading House Program is available in Memorandum 4.5.2, *Exports – Tangible Personal Property*, of Chapter 4, *Zero-Rated Supplies*, of the GST/HST Memoranda Series.

**Non-taxable imported goods**  
(Sch. VII, s 5.1)

Section 5.1 of Schedule VII to the Act provides that, in situations where a replacement good is provided under warranty for no additional consideration, other than shipping and handling charges, and is exported in place of the original defective good, no GST/HST is payable under Division III in respect of the importation of the defective good. For this relief to apply, the replacement good cannot be used or consumed in Canada except to the extent reasonably necessary or incidental to its transportation. This amendment applies to goods imported after February 28, 2000.

**Exporters of Processing Services Program**  
(Sch. VII, s 8.1, 8.2 and 8.3, and s 213.2)

The Exporters of Processing Services Program has been expanded to allow for storage and distribution services on goods imported after February 28, 2000. Detailed information on this program is available from the nearest CCRA tax services office.

### **Enquiries**

If you wish to make a **technical enquiry** on the GST/HST by telephone, please call one of the following toll-free numbers:

1-800-959-8287 (English service)  
1-800-959-8296 (French service)

**General enquiries** about the GST/HST should be directed to Business Enquiries at one of the following toll-free numbers:

1-800-959-5525 (English service)  
1-800-959-7775 (French service)

If you are in the Province of Québec, please call the following toll-free number:  
1-800-567-4692 (Ministère du Revenu du Québec)

All GST/HST Technical Information Bulletins are available on the Internet at the CCRA site <http://www.cca-adrc.gc.ca/> under the heading "Technical Information" in "Tax". All other CCRA publications are also available at this site.

APPENDIX A

DEFINITIONS AND EXPLANATIONS OF SIGNIFICANT TERMS USED IN THIS PUBLICATION

(s 273.1 unless otherwise specified)

The following sets out the definitions of significant terms used in this publication and, where necessary, provides additional explanations.

Added property ..... 1
Base value..... 2
Basic service..... 2
Bonded warehouse..... 4
Customer’s good..... 4
Domestic inventory ..... 4
Export revenue..... 4
Export revenue percentage ..... 5
Finished inventory ..... 5
Labelling..... 5
Packing ..... 6
Processing..... 6
Specified total revenue ..... 6
Substantial alteration of property ..... 7
Total value added in respect of customers’ goods..... 7
Total value added in respect of finished inventory ..... 7
Value added attributable to non-basic services in respect of customers’ goods ..... 8
Value added attributable to non-basic services in respect of finished inventory ..... 8

Added property

“Added property” that is in the possession of a person means tangible personal property (other than property that serves as evidence of the payment of postage) or software that the person incorporates into, attaches to, combines or assembles with, or uses to pack, other property that is not property of the person held otherwise than for sale by the person.

The term “added property” refers to tangible personal property or software that is a component part or property (such as a label or a screw) that is incorporated or combined with other property. Added property also includes packing materials used in packing other goods. With the use of a valid EDCP certificate, a registrant is entitled to import, or acquire in Canada, property for use or supply as added property without having to pay the GST/HST.

Added property held by a person who has been authorized to use an EDCP certificate does not include goods or software that are to be added to capital property of the person or that are to be added to any property of the person that is not intended for sale by the person. Added property

acquired or imported by a person, therefore, does not include, for example, parts for the person's own capital equipment. However, added property does include parts for any type of customers' goods even if those customers' goods were capital property of the customers. Added property also includes property to be added to goods that are inventory held for sale by the person or by the person's customers.

### **Base value**

“Base value” of property that a particular person imports or obtains physical possession of in Canada from another person means

- (a) if the particular person imports the property, the value that is or would be, but for subsection 215(2) of the Act, deemed under subsection 215(1) of the Act to be the value of the property for the purposes of Division III of Part IX of the Act; and
- (b) in any other case, the fair market value of the property at the time the particular person obtains physical possession of it in Canada.

Base value, in the case of imported goods, refers to the value of the goods for purposes of Division III (tax on imported goods) before the application of any rules for reducing that value such as those with respect to temporary imports. In any other case, the base value of property refers to the fair market value of the property. The term "base value" is used in subsection 273.1(4) to determine the percentage value added by a registrant authorized to use an EDCP certificate in respect of goods not owned by the registrant (which are referred to as customers' goods and defined in subsection 273.1(1)).

### **Basic service**

“Basic service” means any of the following services performed at any time in respect of goods, to the extent that, if the goods were held in a bonded warehouse at that time, it would be feasible, given the stage of processing of the goods at that time, to perform the service in the warehouse and it would be permissible to do so according to the *Customs Bonded Warehouses Regulations*:

- (a) disassembling or reassembling, if the goods have been assembled or disassembled for packing, handling or transportation purposes;
- (b) displaying;
- (c) inspecting;
- (d) labelling;
- (e) packing;
- (f) removing, for the sole purpose of soliciting orders for goods or services, a small quantity of material, or a portion, a piece or an individual object, that represents the goods;
- (g) storing;

- (h) testing; or
- (i) any of the following that do not materially alter the characteristics of the goods:
  - (i) cleaning,
  - (ii) complying with any applicable law of Canada or of a province,
  - (iii) diluting,
  - (iv) normal maintenance and servicing,
  - (v) preserving,
  - (vi) separating defective goods from prime quality goods,
  - (vii) sorting or grading, and
  - (viii) trimming, filing, slitting or cutting.

The term “basic service” refers to any of the services enumerated in paragraphs (a) to (i) of the definition of that term found in subsection 273.1(1), which are services that, at the time of announcement of the export distribution centre rules on February 28, 2000, were services that could be performed in a customs bonded warehouse pursuant to the *Customs Bonded Warehouses Regulations*. The definition of basic service does not require that the service be performed in a bonded warehouse only that it be a service that could be performed in a bonded warehouse if the goods in respect of which it is performed happened to be situated in such a warehouse at the time.

In addition, a service listed in any of paragraphs (a) to (i) of the definition of “basic service”, which is found in subsection 273.1(1), is only a basic service if the stage of processing of the goods in respect of which the service is performed at any time is such that it would be reasonable to perform that service at that time in a customs bonded warehouse. For example, if the service involved testing the operation of some function of goods at an intermediate step in their processing before they were further processed and ready for distribution, that testing would not qualify as a basic service. It is not reasonable to perform that service in a customs bonded warehouse given that the further processing required could not be undertaken in the warehouse. This particular testing service is excluded from the definition of "basic service" notwithstanding the fact that “testing” is on the list of services that do constitute a basic service in other circumstances such as the testing of the final processed goods prior to their export.

The term "basic service" is used in the definition of "processing" in subsections 273.1(1), (2) and (4). The purpose for distinguishing between basic services and other services is to ensure that the specified limits on value added that restrict eligibility to use an EDCP certificate do not apply to services that a registrant could, without the EDCP certificate, perform without losing the benefit of tax relief under the Customs Bonded Warehouse Program.



### **Bonded warehouse**

“Bonded warehouse” has the meaning assigned by subsection 2(1) of the *Customs Act*. This term is used in the definition of “basic service” in subsection 273.1(1).

### **Customer’s good**

“Customer’s good” in respect of a particular person, means tangible personal property of another person that the particular person imports, or obtains physical possession of in Canada, for the purpose of supplying a service, or supplying added property, in respect of the tangible personal property. This term is used in subsections 273.1(4) to (7).

### **Domestic inventory**

“Domestic inventory” of a person means tangible personal property that the person acquires in Canada, or acquires outside Canada and imports, for the purpose of selling the property separately for consideration in the ordinary course of a business carried on by the person.

The term “domestic inventory” refers to tangible personal property that a person purchases in Canada or purchases outside Canada and imports for the purpose of selling the property separately for consideration. For example, property that is acquired for use in supplying a service for a single consideration and that is not intended to be sold separately is not part of the domestic inventory of a person. In addition, inventory acquired and sold outside Canada by a person without ever having been brought into Canada by the person is not part of the person's domestic inventory. The term "domestic inventory" is used in defining a person's export revenue for purposes of section 273.1. A person's "export revenue" is derived from sales of domestic inventory made outside Canada and made in Canada for export. The term "domestic inventory" is also used in section 1.2 of Part V of Schedule VI to the Act and in section 11 of Schedule VII to the Act in reference to property that a person authorized under section 273.1 to use an EDCP certificate may purchase or import without paying the GST/HST.

### **Export revenue**

“Export revenue” of a particular person for a fiscal year means the total of all amounts each of which is consideration, included in determining the specified total revenue of the person for the year, for

- (a) a supply by way of sale of an item of domestic inventory of the person that is made outside Canada or included in Part V of Schedule VI to the Act (other than sections 2.1, 3, 11, 14 and 15.1 of that Part);
- (b) a supply by way of sale of added property acquired by the person for the purpose of processing in Canada particular property where the particular property, or all the products resulting from that processing, as the case may be, are exported, after that processing is complete, without being consumed, used, transformed or further processed, manufactured or produced in Canada by another person except to the extent reasonably necessary or incidental to the transportation of the particular property or those products; or

- (c) a supply of a service of processing, storing or distributing tangible personal property of another person if the property, or all the products resulting from that processing, as the case may be, are exported, after the processing in Canada, if any, by the particular person is complete, without being consumed, used, transformed or further processed, manufactured or produced in Canada by any person other than the particular person except to the extent reasonably necessary or incidental to the transportation of that property or those products.

Export revenue of a person for a fiscal year refers to the total consideration paid or becoming due to the person in the year for:

- sales of domestic inventory of the person (as defined in subsection 273.1(1)) that are either made outside Canada or are zero-rated under Part V of Schedule VI (other than section 2.1, 3, 11, 14 and 15.1 of that Part);
- sales of added property (as defined in subsection 273.1(1)) acquired by the person for use or supply in processing in Canada property for export; and
- sales of services of processing, storing or distributing tangible personal property of other persons where the property is exported after the processing is complete.

The term "export revenue" is used in the definition of "export revenue percentage" in subsection 273.1(1).

### **Export revenue percentage**

“Export revenue percentage” of a person for a year means the percentage that the person’s export revenue for the year is of the person’s specified total revenue for the year.

Export revenue percentage of a person is determined by dividing the person's total export revenue for a year (as defined in subsection 273.1(1)) by the person's specified total revenue for the year, also as defined in that subsection. The "export revenue percentage" of a person is relevant in determining the person's eligibility to be authorized under subsection 273.1(7) to use an EDCP certificate to acquire or import certain goods without having to pay the GST/HST. It is also relevant in determining if the person continues to be eligible to use the EDCP certificate after having been so authorized.

### **Finished inventory**

“Finished inventory” of a person means property of the person (other than capital property) that is in the state at which it is intended to be sold by the person, or to be used by the person as added property, in the course of a business carried on by the person.

### **Labelling**

“Labelling” includes marking, tagging and ticketing.

The term “labelling” is defined, for purposes of the definition of "basic service" in subsection 273.1(1).

## **Packing**

“Packing” includes unpacking, repacking, packaging and repackaging.

The term "packing" is defined for purposes of the definitions "basic service" and "added property" in subsection 273.1(1).

## **Processing**

“Processing” includes adjusting, altering, assembling and any basic service.

## **Specified total revenue**

“Specified total revenue” of a person for a fiscal year of the person means the total of all amounts each of which is consideration, included in determining the income from a business of the person for the year, for a supply made by the person (or that would be made by the person but for any provision of Part IX of the Act that deems the supply to be made by another person), other than

- a supply of a service in respect of property that the person neither imports nor obtains physical possession of in Canada, for the purpose of providing the service;
- a supply by way of sale of particular property that the person acquires for the purpose of selling the particular property (or selling other property to which the particular property has been added or with which the particular property has been combined) for consideration but that is neither acquired in Canada nor imported by the person;
- a supply by way of sale of an added property that the person acquires for the purpose of processing tangible personal property that the person neither imports nor obtains physical possession of in Canada; and
- a supply by way of sale of capital property of the person.

The term “specified total revenue” of a person for a fiscal year means the total consideration that becomes due, or is paid without having become due, to the person in the year for supplies made by the person and that is included in determining the income from a business of the person for the year, other than consideration for:

- sales of services in respect of property that is not acquired in Canada, imported or transferred to the person in Canada;
- sales of inventory that the person neither acquired in Canada nor imported;
- sales of added property acquired for processing tangible personal property that the person neither imports nor obtains physical possession of in Canada; and
- sales of capital property of the person.

### **Substantial alteration of property**

“Substantial alteration of property” by a person, in respect of a fiscal year of the person, means

- (a) manufacturing or producing, or engaging another person to manufacture or produce, property (other than capital property of the person) at any time in the year in the course of a business carried on by the person; or
- (b) any processing undertaken by or for the person during the year to bring property of the person to a state at which the property or the product of that processing is finished inventory of the person, if
  - (i) the person’s percentage value added attributable to non-basic services in respect of finished inventory of the person for the year exceeds 10%, and
  - (ii) the person’s percentage total value added in respect of finished inventory of the person for the year exceeds 20%.

### **Total value added in respect of customers’ goods**

“Total value added in respect of customers’ goods” - A person's percentage total value added in respect of customers' goods for a year means the percentage that would be determined under subsection 273.1(4) for that year without excluding any amounts relating to the performance of basic services, or added property used in the performance of basic services.

A person's percentage total value added in respect of customers' goods is relevant in determining whether the person qualifies for an authorization to use an EDCP certificate. It is also relevant in determining whether the person can continue to use the EDCP certificate after having been so authorized.

### **Total value added in respect of finished inventory**

“Total value added in respect of finished inventory” - A person's percentage total value added in respect of finished inventory for a fiscal year means the percentage that would be determined under subsection 273.1(2) for the year without excluding any amounts relating to the performance of basic services. The value added percentage in respect of finished inventory is essentially the percentage of the total cost of the inventory that constitutes labour costs, including the labour component of contracted services that is included in the total cost of the inventory.

The percentage total value added in respect of finished inventory of a person is relevant to determining whether the person is considered to be engaged in the substantial alteration of property. Where it can reasonably be expected that a person will engage in the substantial alteration of property, the person will not qualify to be authorized to use an EDCP certificate. If the person begins to engage in the substantial alteration of property after having been authorized to use an EDCP certificate, the authorization will be revoked.

### **Value added attributable to non-basic services in respect of customers' goods**

“Value added attributable to non-basic services in respect of customers' goods” - A person's percentage value added that is attributable to non-basic services in respect of customers' goods for a fiscal year is the amount (expressed as a percentage) that is determined by the formula:

$$A/(A + B)$$

where

A is the total of all consideration, included in determining the income from a business of the person for the year, for supplies of services, or of added property, in respect of customers' goods, other than the portion of such consideration that is reasonably attributable to the performance of basic services or to the provision of added property used in the performance of basic services, and

B is the total of the base values of the customers' goods.

While subsections 273.1(2) and (3) determine value-added percentages with respect to property owned by a person, subsection 273.1(4) determines a value-added percentage with respect to customers' goods.

A person's percentage value added in respect of customers' goods is determined as an aggregate for a fiscal year for all customers' goods in respect of which consideration became due, or was paid without having become due, to the person in the year for processing services or added property supplied by the person. The calculation of a person's percentage value added in respect of customers' goods depends on the total of the base values of those goods, which is essentially the base on which the person adds value through supplying services and added property. The base value of a customer's good means the value of the good for purposes of Division III of Part IX of the Act, in the case of a customer's goods imported by a person and, in any other case, fair market value of the goods at the time possession is transferred to the person.

Under the formula in subsection 273.1(4), the person's total revenue from processing services and sales of added property (i.e., the total of all consideration from the provision of services and added property for the year), excluding amounts attributable to basic services, is divided by the sum of that total and the total of the base values of the customers' goods.

A person's percentage value added attributable to non-basic services in respect of customers' goods is relevant in determining if the person qualifies for an authorization to use an EDCP certificate. It is also relevant in determining if the person can continue to use an EDCP certificate after having been so authorized.

### **Value added attributable to non-basic services in respect of finished inventory**

“Value added attributable to non-basic services in respect of finished inventory” - A person's percentage value added that is attributable to non-basic services in respect of the person's finished inventory for a fiscal year is the amount (expressed as a percentage) that is determined by the formula:

A/B

where

A is the total of all amounts each of which

(a) is part of the total cost to the person of all property that was finished inventory of the person supplied, or used as added property, by the person during the year, and

(b) is reasonably attributable to

- (i) salary, wages or other remuneration paid or payable to employees of the person, excluding any amounts that are reasonably attributable to the performance of basic services, or
- (ii) consideration paid or payable by the person to engage other persons to perform processing, excluding any portion of such consideration that is reasonably attributed by the other persons to tangible personal property supplied in connection with that processing or that is reasonably attributable to the performance of basic services, and

B is the total cost to the person of the property.

A person's percentage value added attributable to non-basic services in respect of finished inventory of the person for a fiscal year is essentially the labour cost component (expressed as a percentage) of the total cost of all property that was finished inventory supplied, or used as added property, by the person during the year. For this purpose, the labour cost component does not include labour relating to basic services. It includes not only the internal labour costs included in the cost of inventory but also the portion of any consideration for outside contractors' processing services (other than basic services), to the extent that the cost of those services is properly chargeable to the inventory. The portion of the contract price that the contractor has attributed to property supplied together with services is excluded from the contractor's fees for purposes of this calculation. Therefore, where a contractor's invoice shows a reasonable breakdown between the charge for materials and the charge for labour, only the labour portion of the total charge is included in the calculation of this value added percentage.

The term "cost" of inventory means the product costs or inventoriable costs. This does not include period costs such as office rent. The cost of inventory ordinarily will be comprised of the laid-down cost of materials plus direct labour applied to the inventory and any applicable share of indirect labour and overhead expense properly chargeable to the inventory. The overhead component may or may not include some indirect labour costs that are treated as part of the total product costs as opposed to period costs.

For the purposes of section 273.1, a person's determinations of the total cost of inventory and of which indirect labour costs, if any, are to be included in the product costs, may be made in accordance with any reasonable method of inventory costing followed by the person. There are several ways in which cost may be determined. In fact, a person may, for different purposes, use different methods. For example, for internal management purposes, the person may use the

absorption costing method while for financial statement purposes the person may use the variable cost method. Also, under each approach, the person can choose between alternatives such as the average-cost or specific-item methods of determining the inventoriable costs. Whichever method is chosen, it is a basic principle of accounting that, once a basis for determining cost has been selected for any purpose, it will be followed consistently for that purpose from one period to another unless circumstances warrant a change.

The percentage determined under subsection 273.1(2) is relevant in determining whether a person is considered to be engaged in the substantial alteration of property. Where it can reasonably be expected that a person will engage in the substantial alteration of property, the person will not qualify to be authorized to use an EDCP certificate. If the person begins to engage in the substantial alteration of property after having been authorized to use an EDCP certificate, the authorization will be revoked.

# APPENDIX B

## TWO SAMPLES OF EDCP CERTIFICATES

### Sample 1

I, \_\_\_\_\_, HEREBY CERTIFY that:

1. The recipient of this supply has been authorized by the Minister of National Revenue under section 273.1 of the *Excise Tax Act* to use an export distribution centre certificate for the purposes of section 1.2 of Part V of Schedule VI to that Act, and the authorization is in effect at the time the supply is made.
2. The property listed below is being acquired for use or supply as domestic property or as added property of the recipient (as those expressions are defined in section 273.1 of the *Excise Tax Act*).
3. I am the recipient or I am authorized to execute this certificate on behalf of the recipient.

\_\_\_\_\_  
Date

\_\_\_\_\_  
Signature

\_\_\_\_\_  
Name (Print)

\_\_\_\_\_  
Office or Position

\_\_\_\_\_  
Name of the Recipient

\_\_\_\_\_  
Recipient's Business/Authorization Number

\_\_\_\_\_  
Authorization Expiry Date

Section 279 of the *Excise Tax Act* states that a certificate made by a person (other than an individual) under Part IX of that Act shall be signed on behalf of the person by an individual duly authorized to do so by the person or the governing body of the person and, where the person is a corporation or an association that has duly elected or appointed officers, the president, vice-president, secretary and treasurer thereof, or equivalent officers, are deemed to be so duly authorized.



**SAMPLE 2**

Blanket Certificate

The following example may be used as an alternative to using a rubber stamp or purchase order printed with the certificate wording as shown above.

I, \_\_\_\_\_, HEREBY CERTIFY that:

1. The (specify name of product or type of property - attach list if necessary), which will be purchased from (name of supplier) during the period from \_\_\_\_\_ to \_\_\_\_\_, will be acquired for use or supply as domestic inventory or as added property of the recipient (as those expressions are defined in section 273.1 of the *Excise Tax Act*).
2. The recipient of the supply has been authorized by the Minister of National Revenue under section 273.1 of the *Excise Tax Act* to use an export distribution centre certificate for the purposes of section 1.2 of Part V of Schedule VI to that Act, and the authorization is to be in effect throughout the period specified in paragraph 1 of this certificate. The recipient will advise you should the authorization be revoked before the end of that period.
3. I am the recipient or I am authorized to execute this certificate on behalf of the recipient.

\_\_\_\_\_  
Date

\_\_\_\_\_  
Signature

\_\_\_\_\_  
Name (Print)

\_\_\_\_\_  
Office or Position

\_\_\_\_\_  
Name of the Recipient

\_\_\_\_\_  
Recipient's Business/Authorization Number

\_\_\_\_\_  
Authorization Expiry Date

Section 279 of the *Excise Tax Act* states that a certificate made by a person (other than an individual) under Part IX of that Act shall be signed on behalf of the person by an individual duly authorized to do so by the person or the governing body of the person and, where the person is a corporation or an association that has duly elected or appointed officers, the president, vice-president, secretary and treasurer thereof, or equivalent officers, are deemed to be so duly authorized.