

Clarity is seeing  
the path to your

**Potential**

# HST AND REAL PROPERTY ISSUES

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**December 9<sup>th</sup>, 2014**



**Collins Barrow**

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## HST AND REAL PROPERTY - AGENDA

- Presentation summary:
  - Real property and the operation of the Excise Tax Act
  - Burden of collection – real property
  - Exemption provisions – summarized
  - Common exemption provisions – details
  - Tips/Traps – house flipping
  - Specific examples to review
- Overriding notes on GST/HST:
  - Presentation is an overview
  - Covering only a few common situations
  - HST is a transactional tax – every detail can be important
  - Break down situation into specific transactions
  - Understand taxing concepts



- Real property includes:
  - (a) In respect of property in the Province of Quebec, immovable property and every lease thereof,
  - (b) In respect of property in any other place in Canada, messuages, lands and tenements of every nature and description and every estate or interest in real property, whether legal or equitable, and
  - (c) A mobile home, a floating home and any leasehold or proprietary interest therein.

### Charging provision

165(1) Imposition of goods and services tax -- Subject to this Part, every recipient of a **taxable supply** made in Canada shall pay to Her Majesty in right of Canada tax in respect of the supply calculated at the rate of 5% on the value of the consideration for the supply.



“**taxable supply**” means a **supply** that is made in the course of a **commercial activity**



“**commercial activity**” of a person means  
(c) the making of a **supply** (**other than an exempt supply**) by the person of real property of the person, including anything done by the person in the course of or in connection with the making of the supply;



“**supply**” means, subject to sections 133 and 134, the **provision of property or a service in any manner**, including sale, transfer, barter, exchange, licence, rental, lease, gift or disposition;

What does this mean?

All real property transactions are  
taxable unless you can find an  
exemption!

This is where the client conversation should start?

### ETA 221(1) Obligation to collect tax

- Sets out the basic obligation on the supplier to collect the tax as an agent of her Majesty.

### ETA 221(2) Exception

- A supplier who makes a taxable supply of real property by way of sale is “not required” to collect tax where one of the following situations occur:
  - (a) Supplier is a non-resident,
  - (b) The recipient is registered under Subdivision d (excluding – recipient individual where the property is a residential complex nor cemetery plot),
    - (b.1) Supplier and recipient have made an election under section 2 of Part I of Schedule V, and
  - (c) The recipient is a prescribed recipient.

### Exception 221(2)(b) – supply between registrants most common

#### What are the mechanics of 221(2)(b).

- Vendor is “not required” to collect [ETA - 221(2)],
- Purchaser is “required” to self assess and remit [ETA - 228(4)],
- Reporting requirements:
  - Purchaser uses primarily in commercial activities – report on regular HST return in reporting period
  - Purchaser does not use primarily in commercial activities – report on GST60 by end of following month

#### Typical issues with the 221(2)(b) exception:

1. Real estate agent tells purchaser to register to avoid paying HST,
2. Purchaser pays vendor the HST,
3. Purchaser was not an HST registrant – 221(2)(b) exception did not apply, and

### Typical issues with 221(2)(b) exception

#### Real estate agent tells purchaser to register to avoid paying HST:

- This is a very common situation (*be careful of ability to claim ITC's*)
- 228(4) requires the purchaser to self-assess the HST payable,
- 169(1) allows an ITC subject to ETA 141 & 208:
  - ITC claimed based on % of usage in commercial activities,
  - 90/10 rule
  - If Individual purchaser – be careful of personal usage (50% rule)
- 169(4) restricts ability to claim ITC if self-assessed HST not reported
- 225(4)(b) provides a general four year period from original due date of return to claim ITC
  - What if don't report the HST transaction – and ITC available?
    - Voluntary disclosure – CRA admin policy is to allow a wash transaction
    - CRA audit – CRA may impose interest and penalties
    - CRA audit – four year limitation on ITC claim – possible denial of ITC as well



## Typical issues with 221(2)(b) exception

### Purchaser pays vendor HST:

- 221(2) **Vendor not required** to collect
- 228(4) **Purchaser required** to self-assess the HST payable (**not optional**)
- 222 states Vendor must remit HST to CRA if Vendor voluntarily collects HST
- Vendor can't act as agent for purchaser – purchaser still on hook for unremitted HST
  
- If purchaser does not pay HST to vendor:
  - CRA has no legislative authority to assess vendor for uncollected HST

### Typical issues with 221(2)(b) exception

#### Purchaser was not registrant – 221(2)(b) exception did not apply

- 221(1) **Vendor required** to collect and remit HST,
- 221(2)(b) did not apply, so **purchaser not required** to self-assess
- CRA has **no legislative authority** to assess purchaser for unremitted HST
- Vendor responsible for collection/remittance of HST
  - No due diligence defence
  - Case law supports “no due diligence defence”
  - Liable for interest and penalties
- 224 – Legislative right of vendor to sue purchaser for HST, if criteria met:
  - Supplier made a taxable supply,
  - Supplier was required to collect tax,
  - Supplier complied with 223(1) “proper documentation “,
  - Supplier accounted for or remitted the tax payable, and
  - Purchaser did not pay tax to Supplier.
  
- Note 221(2) does not apply on sales of real property as part of a sale of business if an election is made under S.167.

### Risk Management

- Certification by purchaser in agreement stating the following:
  - Purchaser not acting as agent, nominee or bare trustee of another person
  - Purchaser is registered for HST under Part IX of the ETA
    - Provides HST number (important)
    - Provides CRA registration confirmation number (optional)
    - Acknowledgment by purchaser – vendor is relying on certification and not collecting HST
    - Provides indemnity to vendor for HST, interest and penalties
- Consider if vendor wants to use Subsection 221(2) – legislation states “not required”.
  - Purchaser may have issue with this due to 228(4) self-assessment requirement,
  - Lawyer hold funds in trust until collection burden confirmed
- Consider verifying HST number with CRA:
  - **Use GST/HST registry on CRA website <http://www.cra-arc.gc.ca> when enough information to get immediate verification**
  - **Call CRA 1-800-959-5525 when not enough information to verify on line**
  - **Ensure the G.S.T. # and business name match the purchaser.**
  - **Ensure all information correct when entered**

## Verifying HST number with CRA

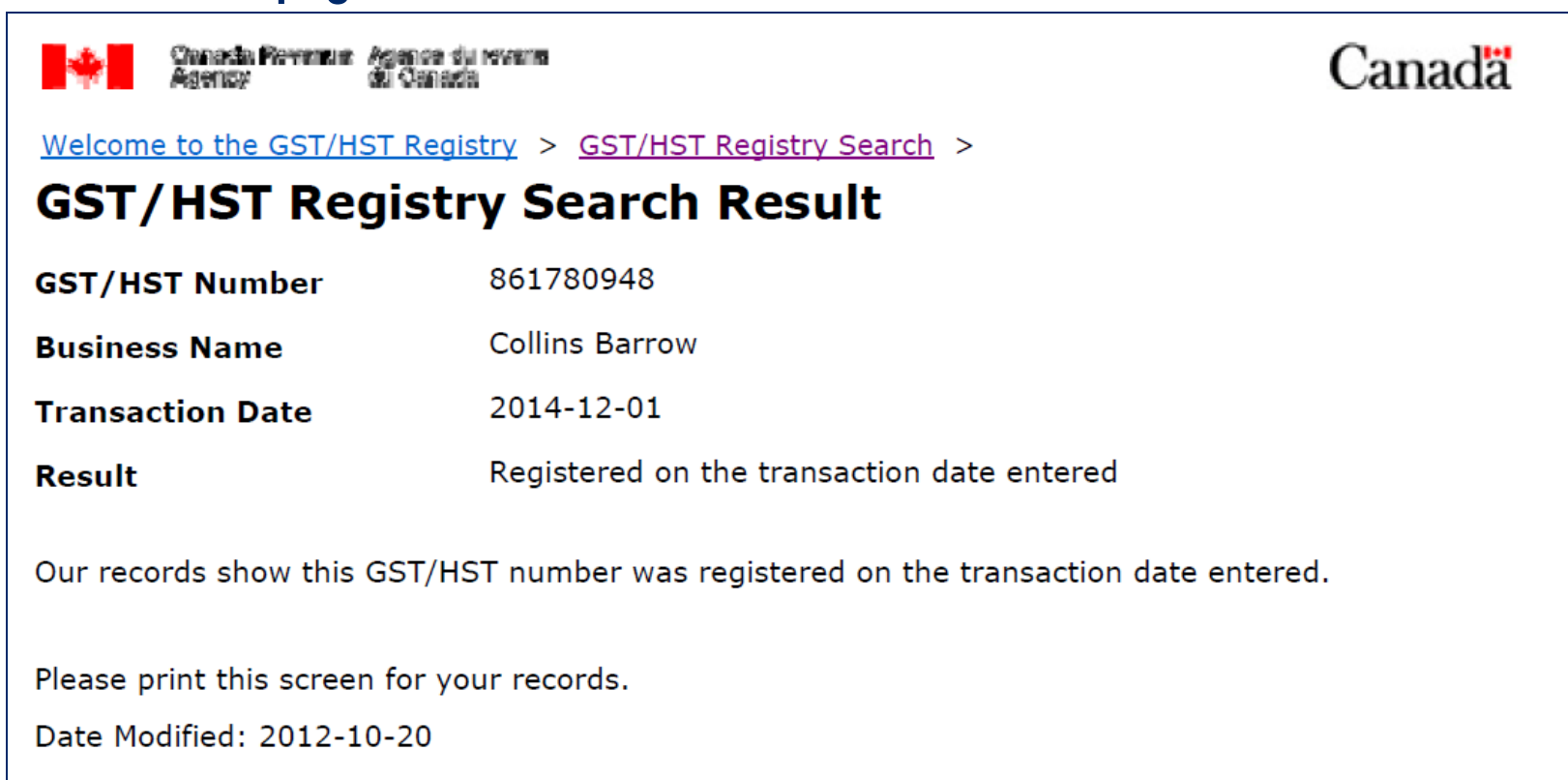
- Input page



The screenshot shows the CRA GST/HST Registry Search page. At the top left is the Canadian flag and the text "Canada Revenue Agency / Agence du revenu du Canada". Below this is a link "Welcome to the GST/HST Registry >". The main heading is "GST/HST Registry Search". A note states "All fields must be entered." The search criteria are: "GST/HST Number" 861780948, "Business Name" Collins Barrow, and "Transaction Date" 2014-12-01. A "Search" button is located below the criteria. At the bottom left of the page, it says "Date Modified: 2012-10-20".

## Verifying HST number with CRA

- Correct results page





The screenshot shows the CRA website interface for the GST/HST Registry Search. At the top left is the CRA logo with the text "Canada Revenue Agency" and "Agence du revenu du Canada". At the top right is the "Canada" wordmark. Below the logos are navigation links: "[Welcome to the GST/HST Registry](#) > [GST/HST Registry Search](#) >". The main heading is "GST/HST Registry Search Result". Below this is a table of search results:

<b>GST/HST Number</b>	861780948
<b>Business Name</b>	Collins Barrow
<b>Transaction Date</b>	2014-12-01
<b>Result</b>	Registered on the transaction date entered

Below the table, the text reads: "Our records show this GST/HST number was registered on the transaction date entered." followed by "Please print this screen for your records." and "Date Modified: 2012-10-20".

## Verifying HST number with CRA

- **Incorrect results page**



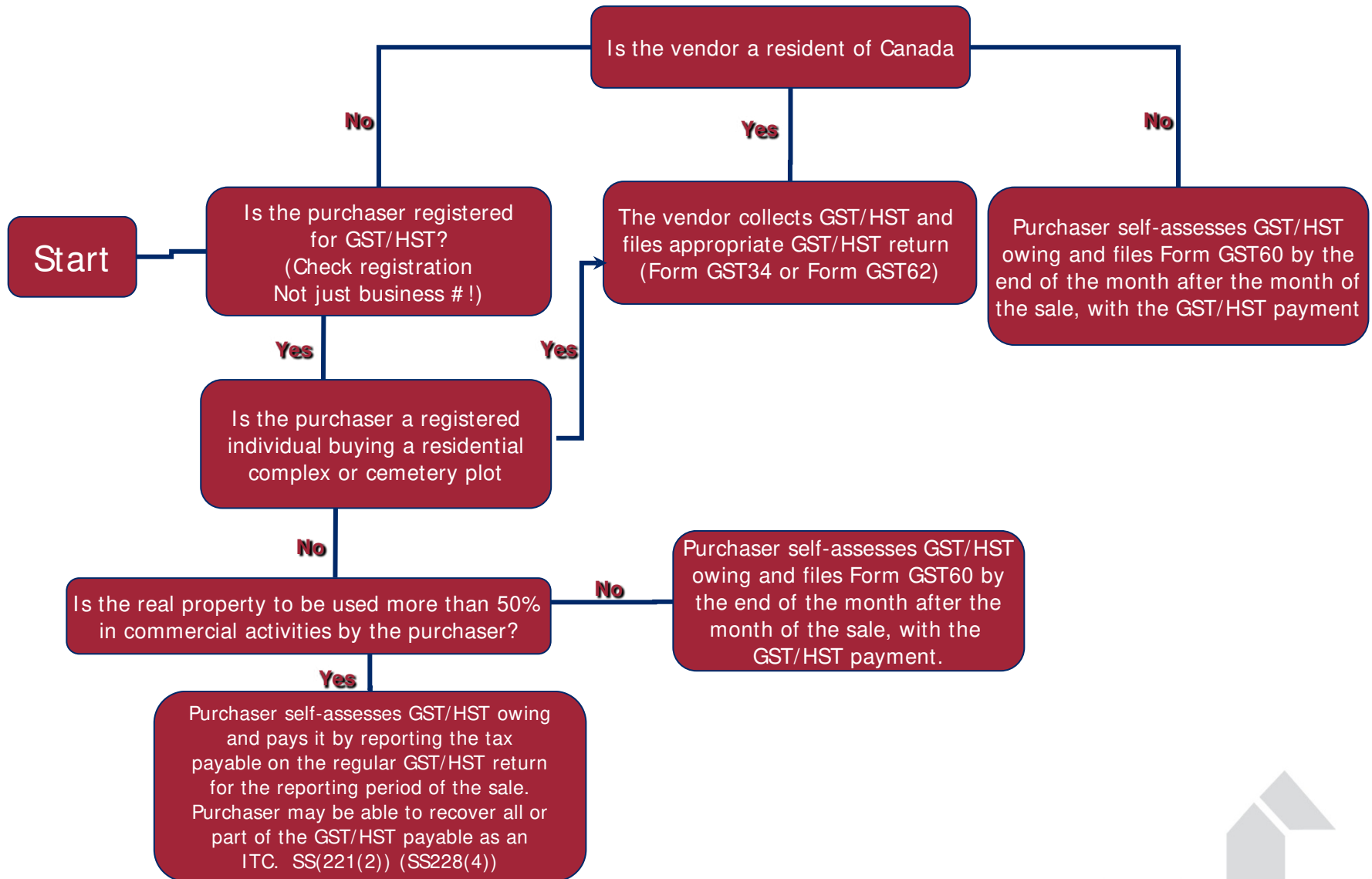
[Welcome to the GST/HST Registry](#) > [GST/HST Registry Search](#) >

### **GST/HST Registry Search Result**

<b>GST/HST Number</b>	861780948
<b>Business Name</b>	Collin Barrows
<b>Transaction Date</b>	2014-12-01
<b>Result</b>	Insufficient information entered

We are unable to validate the information entered. Please verify the business name, GST/HST number and transaction date, and then try again. If you continue to have trouble, contact your supplier or consult our [frequently asked questions](#).

# BURDEN OF COLLECTION – REAL PROPERTY



# REAL PROPERTY EXEMPTION PROVISIONS SUMMARIZED

## Common exemption provisions:

- Section 2 – Used residential property
- Section 9 – Vacant land
- Section 10 – 12 Farmland



## SECTION 2 – USED RESIDENTIAL PROPERTY

### Schedule V, Part I, Section 2 of ETA:

#### Used residential property:

- A particular supply by way of sale of a residential complex or an interest in a residential complex made by a particular person who is not a builder of the complex...and the particular person did not claim an input tax credit.
- The scheme of the ETA is to **tax each newly-constructed property once, and once only**.
- The exemption provision “used residential property” is a misnomer
- Exemption for a sale of residential property by a person who is not the “builder”.
- IT is all about fairness – focus on builder not “used residential”
  
- **Important terms defined in section 123(1):**
  - Residential complex,
  - Builder – (*we get caught here a lot*)

## SECTION 2 – USED RESIDENTIAL PROPERTY

### Used residential property:

- **“residential complex”**
  - The term is designed to separate real property that is only to be taxed once “residential” from real property that is to be taxed on every lease or sale “commercial”
  - The definition is very detailed and complex
  - 136(2) provides for a separate supply between commercial/residential in mixed use properties
  - Generally defined as a building or part thereof which includes a residential unit **used or intended for use as a place of residence of lodging**
  - Includes: house, townhouse, condo, apartment, mobile home, floating home
  - Buildings with multiple units is separately defined as a multi-unit residential complex
- Does not include:
  - Hotel, Inn, Boarding house, or similar premises (further defined with reference to periods of continuous possession or use of less than sixty days)
  - Excess land not reasonable and necessary for place of residence (1/2 hectare – general policy)
  - Be careful with non-residential use of property

## SECTION 2 – USED RESIDENTIAL PROPERTY

### Used residential property:

- **“builder”**
  - The term **“builder”** is used only in reference to a “residential complex”
  - Has interest in residential complex
  - Defined as person that carries on or engages another person to carry on:
    - Addition to multiple unit residential complex,
    - Substantial renovation of a residential condominium unit (bill C-43 “first reading Oct 23/14”)
    - In any other case, construction or substantial renovation of a complex
  - The term is more detailed than outlined here – (RISK MANAGEMENT - always use general concept):
    - HST applies to real property transaction unless an exemption can be verified
- Builder does not include
  - an individual who carries on or engages another person to carry on addition, construction or substantial renovation (listed above) otherwise than in the course of a business or an adventure or concern in the nature of trade,
- Lots of commentary and jurisprudence in relation to:
  - Business,
  - Adventure or concern in the nature of trade

## SECTION 2 – USED RESIDENTIAL PROPERTY

### Used residential property:

- **“Substantial renovation”**
  - Defined in 123(1) of the ETA
    - means the renovation or alteration of a building to such an extent that **all or substantially all** of the building that existed immediately before the renovation or alteration was begun, other than the foundation, external walls, interior supporting walls, floors, roof and staircases, has been removed or replaced where, after completion of the renovation or alteration, the building is, or forms part of, a residential complex
  - Information Bulletin B-092 provides CRA commentary
  - Legislation does not use the phrase “substantial”, so common definition not applicable
  - Legislation uses “all or substantially all” interpreted by CRA as 90%
  - Legislation defines what is generally considered as substantial
  - Significant jurisprudence related to the definition of substantial renovation

## SECTION 2 – USED RESIDENTIAL PROPERTY

### Used residential property:

- **Adventure or concern in the nature of trade**
  - Not defined in the ETA
    - Refer to CRA policy P-059
      - “Generally, a sale made in the course of a business may be differentiated from a sale made in the course of an adventure or concern in the nature of trade by the amount of time, attention and resources accorded to the transaction or by the frequency or regularity of similar transactions. In this regard, a sale made in the course of an adventure or concern in the nature of trade normally involves acquiring property on an isolated basis with the primary or secondary intention of resale at a profit and only passive or limited activities related to the resale (i.e. those required to facilitate its resale). Regular sales of property or sales made in a business-like manner would normally be considered a sale made in the course of a business.”
  - Significant jurisprudence and commentary related to this concept
- **Business**
  - **123(1) “business”** includes a profession, calling, trade, manufacture or undertaking of any kind whatever, whether the activity or undertaking is engaged in for profit, and any activity engaged in on a regular or continuous basis that involves the supply of property by way of lease, licence or similar arrangement, but does not include an office or employment

## SECTION 2 – USED RESIDENTIAL PROPERTY

### Used residential property exemption:

- Must meet definition of residential complex,
- Can have separate supplies – utilize exemption for part of property
- Must avoid definition of builder, which is dependent on:
  - Substantial renovation,
  - Business,
  - Adventure or concern in the nature of trade
  
- Owner renovating principal residence
  - Generally will not be a problem,
    - Not a business or adventure/concern in the nature of trade
  - Owner will try to support “substantial renovation” definition to get new housing rebate
  
- House flippers
  - Generally will be a problem
    - Adventure or concern in the nature of trade is very broad
  - Substantial renovation definition will become very important in order to gain access to exemption

## SECTION 9 – VACANT LAND

- **9(2)** A supply of real property made by way of sale by an individual or a personal trust, other than:
  - Capital property used primarily in a business
  - Vendor is GST registrant and property used primarily to make taxable rentals
  - Vendor in business of selling real property
  - Sale is an adventure or concern in the nature of trade and vendor elects to be taxable
  - **Land sold is part of larger parcel previously subdivided into more than two parts**
  
- This section intended to ensure that most sales of personal use property (other than residential complex) is exempt.
  - Exceptions listed above tend to deny exemption when “other than” personal use
- This section commonly provides tax relief on the excess land portion of a residential complex
- Remember concept – help with analysis

## SECTION 9 – VACANT LAND

- **9(2)(c) subdivided or severed into more than 2 parts:**
  - Denies exemption if land severed too many times
  - This rule applies for duration of a person's ownership
    - Subdivision of land before 1991 (before GST) does not matter
    - The subdivision rule resets upon new ownership
    - Exemption for sale to family members (for personal use only)
  
- Most common situation requiring analysis is “subdivided vacant land”
  
- **Example:**
  - Mr. Altaf has three separate parcels of land (3 separate titles)
  - The three separate parcels of land are odd shapes adjacent to each other
  - Mr. Altaf would like to consolidate the properties and subdivide into three equal sized properties
  - Mr. Altaf would then like to sell one of the parcels of land
  - **Taxable or not taxable on sale?**



## SECTION 9 – VACANT LAND

Diagram 1: original ownership of properties

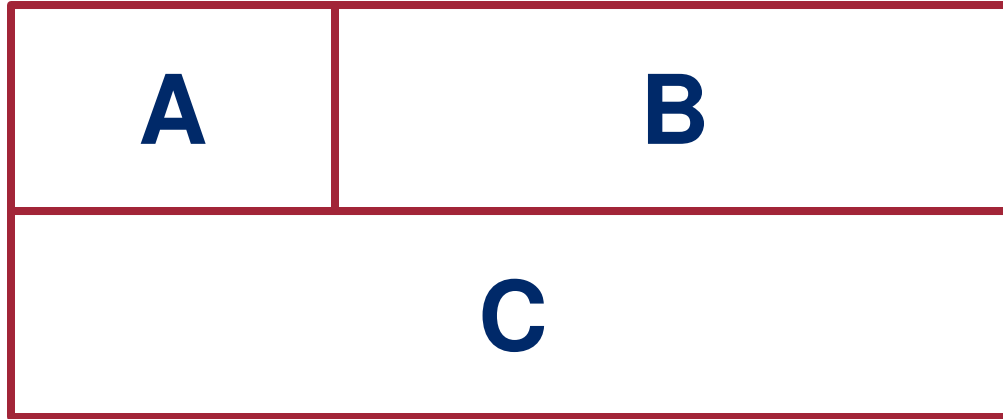


Diagram 2: consolidation of properties into one property

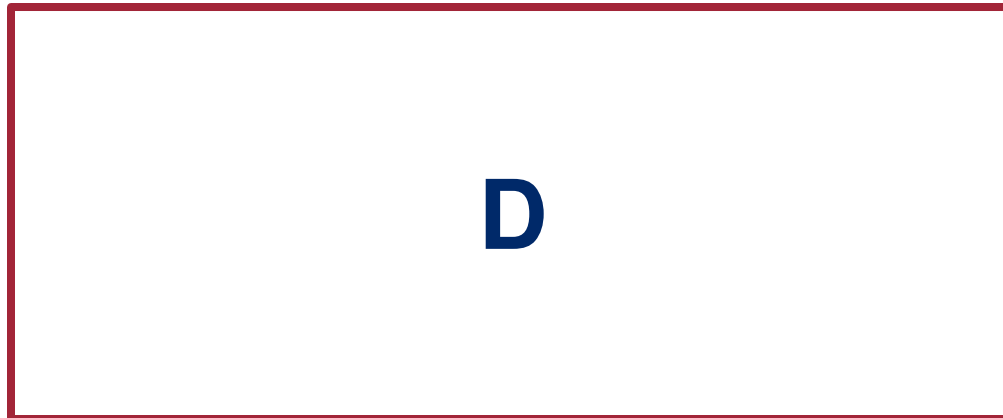


Diagram 3: three subdivided properties



- Is the exemption denied under subparagraph 9(2)(c)(i) – subdivided into 2 parts, and that parcel not subdivided from another parcel of land
- The original parcel of land was divided into three parts – therefore the exemption is denied
- **Sale of property G is taxable**
- Future sale of property E and F would also be taxable

## SECTION 9 – VACANT LAND

- **Second Example:**
  - Mr. Altaf has three separate parcels of land (3 separate titles)
  - The three separate parcels of land are odd shapes adjacent to each other
  - Mr. Altaf would like to consolidate the properties and subdivide into two separate properties as follows:
    - 1/3 of property to be subdivided and sold
    - 2/3 of property to be kept and not sold
  - **Taxable or not taxable on sale?**

Diagram 4: original ownership of properties

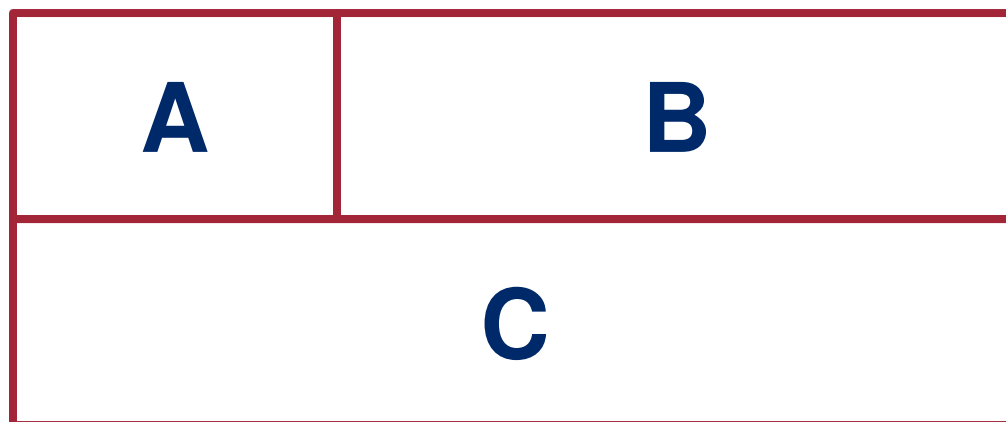


Diagram 5: consolidation of properties into one property

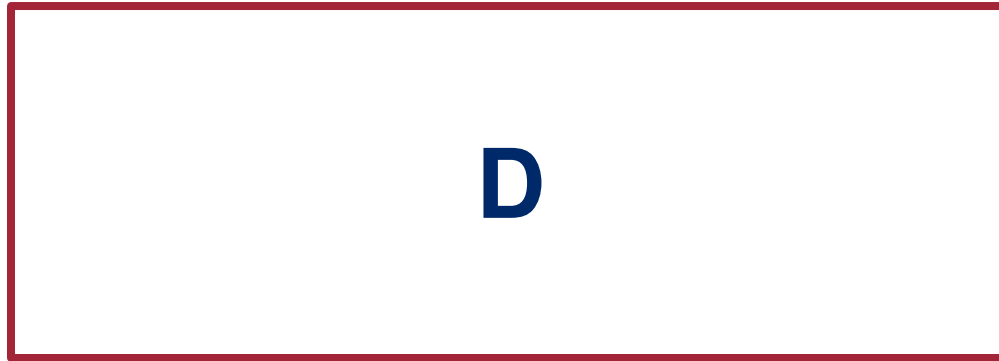
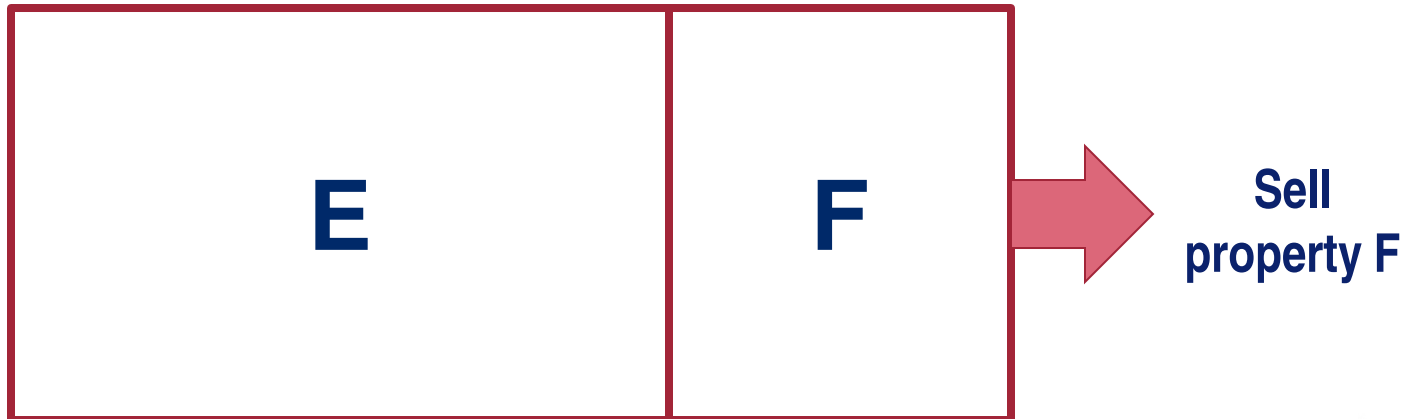


Diagram 6: Two subdivided properties

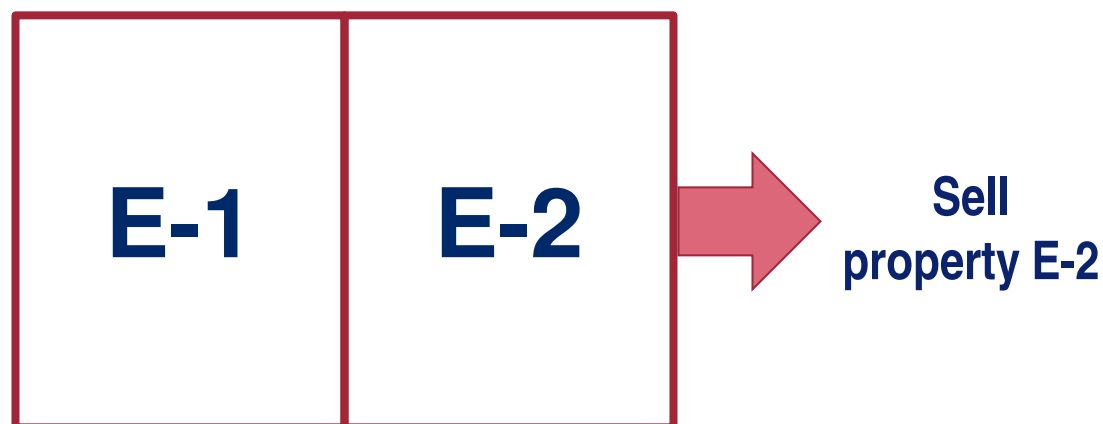


**Taxable or not taxable?**

## SECTION 9 – VACANT LAND

- The sale of parcel F in diagram 6 would **not be taxable**
  - Property D (one parcel of land) was only subdivided into two separate parcels of land
  - Exemption not denied
- What if Mr. Altaf now decided to subdivide parcel E into two parcels of land (previously property D subdivided into property E and F - diagram 5 & 6)

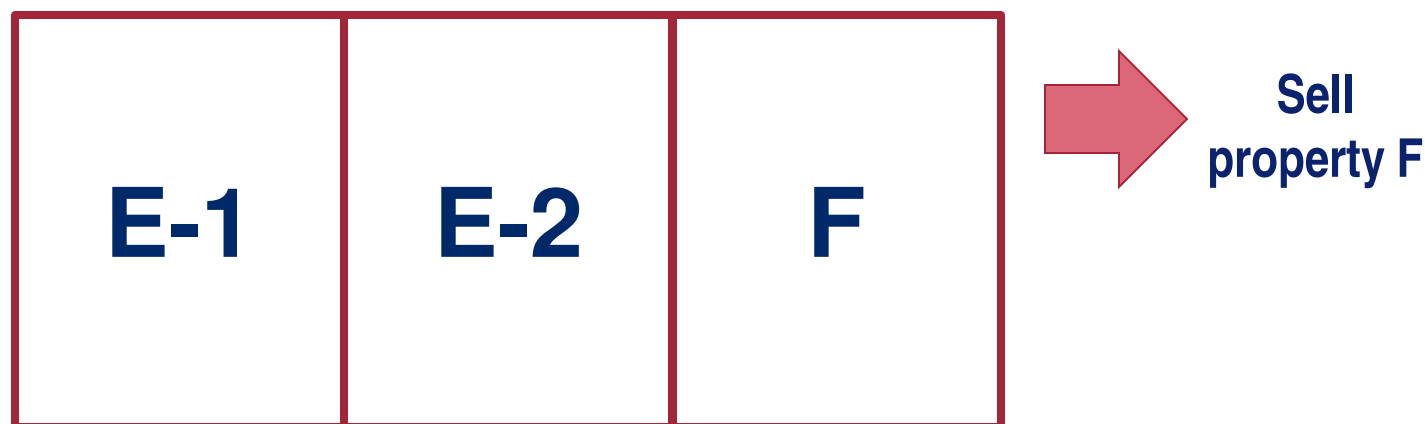
Diagram 7: Subdivide property E into two separate properties



**Taxable or not taxable?**

## SECTION 9 – VACANT LAND

- The sale of property E-2 would be taxable
  - Property E was formed from subdividing property D into two separate properties (property E and Property F)
  - Remember – a parcel of land can only be subdivided into two parcels before exemption denied
  - Subdivision of property D into property E and F was dividing the original property into two parcels of land. Any further subdivision would result in future taxable sales
- What if property F never sold right away and it was still owned?



**Taxable or not taxable?**

## SECTION 9 – VACANT LAND

- The sale of property F would continue to be **Not taxable**
  - Property F was formed from subdividing property D into two separate properties (property E and Property F)
  - Remember – a parcel of land can only be subdivided into two parcels before exemption denied
  - Property F resulted from a single subdivision into two separate parts with no further subdivision of property F
  - Therefore the exemption would not be denied
  - If property F subdivided into property F-1 and F-2, then the sale of both properties would be taxable
- History of the property extremely important
- Be careful that subdivision of properties and sale not considered a “business”

**Taxable or not taxable?**

## SECTIONS 10 - 12 – FARM LAND

- Supplies of farmland between registered farmers are taxable. The purchaser is eligible for an ITC for the GST paid
- The exemption provisions under section 10 to 12 in Part I of Schedule V apply when the farmland leaves farming
- Remember that all supplies of real property are taxable unless you can find an exemption provision in Part I of Schedule V of the ETA.
- With regard to Farming, we have the following specific exemptions:
  - Section 10 – Transfer of Farmland to family member for personal use and enjoyment,
  - Section 11 – Deemed “change in use” rules on converting farmland to personal use and enjoyment, and
  - Section 12 – Transfer of Farmland from corporation, partnership or trust to family member for personal use and enjoyment



- **ETA 10. Farmland to relative** – A supply of farmland by way of sale made by an individual to another individual:
  - That other individual is **related** (same definition as Income Tax Act 252(2) – 252(6)), or
  - That other individual is the former spouse or common-law partner,  
***AND (meet all three of following)***
- a) The farmland **was used at any time** by the individual **in a commercial activity** that is the **business of farming**;
- b) The farmland **was not used, immediately before the time** ownership of the property is transferred under the supply, by the individual **in a commercial activity other than the business of farming**
- c) The other individual is **acquiring the farmland for the personal use and enjoyment** of that other individual or any individual **related**

- **ETA 11. Deemed supply of farmland** – A supply by an individual of farmland deemed under subsection 190(2) or 207(1) of the Act to have been made where
  - a) The farmland was used at any time by the individual in a commercial activity that is the business of farming;
  - b) The farmland was not used, immediately before the time the supply is deemed to have been made, by the individual in a commercial activity other than the business of farming; and
  - c) The farmland is, immediately after the time the supply is deemed to have been made, for the personal use and enjoyment of the individual or an individual related

- **ETA 12. Farmland to shareholder, etc.** – A supply of farmland by way of sale made to a particular individual, an individual related to the particular individual or a former spouse or common-law partner of the particular individual by a person that is a corporation, partnership or trust where:
  - a) immediately before the time ownership of the property is transferred under the supply,
    - i. all or substantially all of the property of the person is used in a commercial activity that is the business of farming,
    - ii. the particular individual is a member of the partnership, a beneficiary of the trust or a shareholder of or related to the corporation, as the case may be, and
    - iii. the particular individual, the spouse or common-law partner of the particular individual or a child (within the meaning of subsection 70(10) of the *Income Tax Act*) of the particular individual is actively engaged in the business of the person; and
  - b) immediately after the time ownership of the property is transferred under the supply, the farmland is for the personal use and enjoyment of the individual to whom the supply was made or an individual related

## HOUSE FLIPPING – TIPS AND TRAPS

- Be careful of house flippers trying to avoid tax (HST and income tax)
- General considerations:
  - House flipping purchase – make profit (business or adventure in the nature of trade)
  - Living in the property for short period of time – does not override primary purpose
  - **New housing rebate** and **Used residential housing exemption** don't work together
    - New housing rebate – requires substantial renovation
    - Used residential housing exemption – requires not to be a builder
      - Substantial renovation a criteria to meet builder definition
      - This is how most house flippers get caught
  - Definition of builder will generally catch house flippers – Taxable supply
    - Almost always an adventure or concern in the nature of trade or a business
    - Substantial renovation vs. non-substantial renovation will be extremely important distinction
      - Substantial – you are a builder
      - Non-substantial – you are not a builder
  - Extent of renovations becomes extremely important:
    - Substantial renovation – no exemption (fully taxable and ITC's available)
    - Non-substantial renovation – Exemption applies but deal with ETA 192 “self-supply”

## HOUSE FLIPPING – TIPS AND TRAPS

- **Non-substantial renovations:**
  - Not considered a builder, so exemption provision most likely available
  - Self-supply rule in section 192 of ETA may apply, but only if you are in the business of making real property supplies
  - Self-supply rule in section 192 of ETA does not consider adventure or concern in the nature of trade
  - Purpose of section 192:
    - Assess GST/HST on employee labour costs and other GST exempt costs that form part of the renovation costs that would be capitalized
      - This taxes the added value to the property that would not be recoverable through the GST/HST system
  
- **Where do house flippers fall:**
  - Substantial renovation – probably considered a builder (Fully taxable – ITC’s allowed),
  - Non-substantial renovation – depends on definition of “business”:
    - In the business of making supplies of real property – Not taxable but subject to self-supply rule in section 192
    - Not in the business of making supplies of real property – Not taxable and not subject to self-supply rule

## VACANT LAND SCENARIOS

- 1. Your clients purchased a parcel of vacant land with the intention of building on it someday. Several years later they decide to sell it. They have not built on it. They own it in their individual names. Is there HST on this sale?

## VACANT LAND SCENARIOS

- 2. Your clients purchased a parcel buys a parcel vacant land. One year later they subdivide one lot from the parcel and transfers it to their son. Is there HST on this transaction?

## VACANT LAND SCENARIOS

- 3. Your clients buy a parcel of vacant land in the name of a corporation. It was not used in the commercial venture. They decide to sell. Is there HST on this transaction? If a buyer of the land is also a registrant, who is responsible to remit the HST?



## VACANT LAND SCENARIOS

- 4. An individual owns land and have subdivided into four lots. They realize HST must be charged on the sale, however, the owner is not a registrant and asks you if he must become a registrant and what it the process to remit the HST

## RESIDENTIAL WITH POSSIBLE COMMERCIAL COMPONENT SCENARIOS

- 5. Your client buys a rural property. There is a house and a barn on the property and 50 acres. The sellers have sold the wood off the land from time to time on the property. The buyers purchased with no intention of selling wood or operating any business. The sellers have been advised to charge HST. Are there any options open to the buyer?

## RESIDENTIAL WITH POSSIBLE COMMERCIAL COMPONENT SCENARIOS

- 6. Your client buys rural property. They put up a barn for horses and have a hobby farm. When they sell are they required to charge HST?

## NEW CONSTRUCTION SCENARIOS

- 7. A corporation buys a new construction condominium unit. The price is \$350,000 plus HST. No rebate has been deducted from the price as is the usual case when the buyer is an individual. Are there any rebates for HST available to the corporation.

## NEW CONSTRUCTION SCENARIOS

- 8. An individual buys a new construction condominium for his son to live in. Title is in the name of the father. The father is resident in Canada. Is the father entitled to the HST rebate? What if the person living in the unit was the father's step daughter?

## MIXED USE SCENARIOS

- 9. A couple purchase a building. The ground floor is being used as a convenience store. The second level contains two residential units, one in which the couple will reside and the other will be rented. The purchase price is \$400,000. The upstairs is not the same square footage as the ground floor. For the purpose of HST on the commercial portion, how is the purchase price allocated to the commercial and residential portions?

Thanks