

Real Property and the Harmonized Sales Tax in British Columbia and Ontario

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This update concerns the effect of sales tax harmonization in Ontario and British Columbia on real property transactions. As is well known, Ontario has announced that it will harmonize its 8% retail sales tax ("RST") with the 5% federal goods and services tax ("GST") to form a 13% harmonized sales tax ("HST") effective July 1, 2010 – the same date on which the harmonization of British Columbia's 7% social services tax ("SST") with the GST (to form a 12% HST) is to take effect.

Managing the transition is one of the main challenges of the HST implementation. To that end, both British Columbia and Ontario released proposed transition rules in October 2009 that will govern the application of the RST, SST and HST to future transactions. On November 18, 2009, British Columbia also released transition rules dealing with residential real property. While the transition rules deal with many types of goods and services, our focus here is on how the HST implementation will affect real property transactions. We first outline a number of issues relating to residential properties before turning to non-residential properties. We conclude with a brief discussion of how the implementation process will handle progress payments.

Residential properties – HST transitional rules

a) Transfer of ownership or possession before July 1, 2010

Generally, a sale of a newly constructed or substantially renovated home (a "New Home") in either Ontario or British Columbia will not be subject to the HST if under a written agreement of purchase and sale (an "Agreement"), either ownership or possession of the home is transferred before July 1, 2010.

b) Transfer of ownership and possession on or after July 1, 2010

In Ontario and British Columbia, generally, sales of New Homes under an Agreement will be subject to HST where ownership and possession of the New Home are transferred to the purchaser on or after July 1, 2010.

c) Exception to (b) where agreement entered into on or before June 18, 2009 in Ontario

In Ontario, if an Agreement for a New Home was entered into on or before June 18, 2009, the sale will generally be grandparented such that only the 5% GST, rather than

the full HST, will apply even where both ownership and possession of the home transfer to the purchaser on or after July 1, 2010. However, purchasers of a grandparented New Home will not be able to claim the Ontario new housing rebate (see below). Further, builders of grandparented homes, generally, will be required to pay a transitional tax adjustment (“TTA”) (see below) where construction of the New Home straddles July 1, 2010.

Traditional apartment buildings, modular homes, mobile homes and homes built or substantially renovated by owners for their personal use will not be grandparented as the general transitional rules apply differently to these homes. Ontario has stated that additional information in respect of sales of these types of homes (and other circumstances) will be provided in the near future.

d) Exception to (b) where agreement entered into on or before November 18, 2009 in British Columbia

In British Columbia, if an Agreement for a New Home was entered into on or before November 18, 2009, the sale, will generally be grandparented such that only the 5% GST, rather than the full HST, will apply even where both ownership and possession of the home transfer to the purchaser on or after July 1, 2010. However, purchasers of a grandparented New Home will not be able to claim the British Columbia new housing rebate as the provincial portion of the HST was not paid (see below). Further, builders of grandparented homes will generally be required to pay a TTA (see below) where construction straddles July 1, 2010.

As in Ontario, please note that traditional apartment buildings, duplexes, mobile homes, floating homes and homes built by owners for their personal use will not be grandparented as the general transitional rules apply differently to these homes. However, other rebates (such as the new rental housing rebate) may apply to sales of these homes.

e) Assignment of Agreements Entered Into On or Before June 18, 2009 (ON) or November 18, 2009 (B.C.)

In Ontario and British Columbia, where an Agreement entered into on or before June 18, 2009 in Ontario, or November 18, 2009 in B.C., is assigned to an assignee who receives ownership and possession of the home from the original builder on or after July 1, 2010, generally, the sale to the assignee will be grandparented where certain specified conditions are met (such as there is no novation of the agreement, the purchaser and the original builder deal at arm’s length, and the builder and certain related parties do not reacquire any interest in the property).

f) Resale of a Grandparented Home

Ontario and British Columbia have also released proposed transitional rules which provide relief for the provincial portion of the HST in certain circumstances where a grandparented New Home passes through a chain of resellers before it is occupied by an individual for residential use subject to certain conditions. If these relieving provisions do not apply, and the provincial component of the HST applies to the sale of the grandparented home, the first reseller may be able to recover, by way of an input tax credit or rebate, 2% of the consideration established for GST purposes for the sale of the grandparented home (i.e. the estimated TTA embedded in the price of the home). In order to take advantage of these provisions, the reseller will have to comply with additional disclosure rules. If a builder acquires an interest in a previously grandparented home, special rules could apply to force the builder to self-assess part of the provincial component of the HST.

To date, Ontario has not released similar proposed rules.

g) Transitional Tax Adjustment

In Ontario and British Columbia, when a builder sells a grandparented New Home (i.e. where the Agreement was entered into on or before June 18, 2009 or November 18, 2009, respectively, and both ownership and possession are transferred to the purchaser on or after July 1, 2010) other than grandparented “residential condominium units” or “residential condominium complexes”, the builder would normally not charge the provincial portion of the HST, but would have been able to claim input tax credits for expenses which arose after July 1, 2010. In these circumstances, Ontario and British Columbia created a TTA which is payable by the builder if the New Home sold is less than 90% complete as of July 1, 2010. The TTA is intended to approximate the amount of tax which was not paid by the buyer (and for which a credit was claimed) and which would have been paid on the construction of a new home under the RST or SST regimes.

The TTA payable in Ontario and British Columbia is calculated based on the total consideration¹ payable for the New Home, as determined for GST purposes and the degree of completion of the construction or substantial renovation of the New Home on July 1, 2010 as per the following table.

Degree of completion of construction or substantial renovation on July 1, 2010	TTA rate as a percentage of consideration
Less than 10%	2.0%
Equal to or greater than 10% and less than 25%	1.5%
Equal to or greater than 25% and less than 50%	1.0%
Equal to or greater than 50% and less than 75%	0.5%
Equal to or greater than 75% and less than 90%	0.2%
Equal to or greater than 90%	0.0%

In Ontario and British Columbia, a TTA will also be payable by a builder on grandparented sales of new or substantially renovated “residential condominium units” or “residential condominium complexes”. The TTA will generally be calculated at 2% of the total consideration payable for the unit or complex as determined for GST purposes. However, in these circumstances, a builder should be eligible for the RST transitional housing rebate (“Ontario THR”) or SST transitional housing rebate (“British Columbia THR”), as applicable, where construction is at least 10% complete as of July 1, 2010 (see below).

A builder in Ontario or British Columbia who is required to pay the TTA will report the TTA in its GST/HST return for the reporting period that includes the date possession of the grandparented New Home, “residential condominium unit or building” or “residential condominium” is transferred to the purchaser.

New housing and new residential rental property rebates

Ontario

In Ontario, to ensure that purchasers of New Homes are not subject to an additional tax burden as a result of the HST, the 2009 Ontario Budget proposes a new housing rebate up to a maximum of \$24,000 which is generally available where the home is purchased as a primary residence and where the sale of the home is subject to HST (i.e. the sale is not grandparented and ownership and possession transfer after July 1, 2010). The rebate would be calculated as 75% of the Ontario portion of the HST (i.e. 6% out of the combined 13% HST), up to a maximum of \$24,000. There is also a proposed rebate that would be available for new rental housing, including investment properties to be rented out, for use as primary places of residence. Landlords who purchase new rental homes would be eligible for the rebate up to a maximum of \$24,000 per rental unit.

British Columbia

In British Columbia, a proposed new housing rebate will generally be available where a New Home is purchased as a primary residence and for residential rental properties as long as HST applied to the sale, subject to certain conditions. The rebate will equal 71.43% of the British Columbia portion of the HST (i.e. 5% out of the combined 12% HST) up to a maximum of \$26,250. In the case of purchases of qualifying shares in a cooperative housing corporation or of a New Home with leased lands, the rebate will generally equal 4.47% of the purchase price, also up to a maximum of \$26,250.

¹ In British Columbia, where the total consideration paid for a grandparented New Home is less than what the fair market value of the home would have been if the home had been substantially completed on July 1, 2010, the consideration for purposes of calculating the TTA is deemed to be equal to the fair market value of the home as if the construction or substantial renovation of the home was substantially completed on July 1, 2010.

Transitional Housing Rebate (“THR”)

In Ontario and British Columbia, to provide relief in respect of embedded RST or SST, a purchaser of certain non-grandparented New Homes may be able to claim the proposed Ontario THR or the proposed British Columbia THR, as applicable, where the construction or substantial renovation of the home straddles July 1, 2010 and HST is payable on the sale. Please note that the Ontario THR would generally not be available for mobile homes, modular homes and New Homes built by owners for their personal use. Similarly, the British Columbia THR will generally not be available for New Homes built by owners for their personal use, mobile homes and floating homes.

In both provinces, to claim a THR, the home must be at least 10% complete on July 1, 2010. In Ontario, a purchaser will be able to claim the rebate from the builder or apply directly to the Canada Revenue Agency (“CRA”). Applying to the CRA would generally require the purchaser to obtain a certification of the degree of completion of construction or substantial renovation on July 1, 2010 from the builder.

A builder can also claim the Ontario THR or the British Columbia THR, as applicable, where the construction or renovation of the home straddles July 1, 2010 and the builder was required to self-assess HST on the home (for instance where it is rented out) or was required to pay the TTA on the home. To be eligible, the construction or substantial renovation must be at least 10% complete on July 1, 2010.

Generally, a purchaser or builder who is eligible to claim the Ontario THR or the British Columbia THR, can claim such amount in addition to the Ontario or British Columbia new housing rebate (if applicable).

The Ontario THR and the British Columbia THR will be calculated as a proportion of the estimated embedded RST or SST, respectively, in a New Home, based on the degree of completion (i.e. the extent of construction or substantial renovation) of the home as of July 1, 2010 and apply as per the following table:

Degree of completion of the housing on July 1, 2010	Percentage of RST or SST that would be rebated
Less than 10%	0%
Equal to or greater than 10% and less than 25%	25%
Equal to or greater than 25% and less than 50%	50%
Equal to or greater than 50% and less than 75%	75%
Equal to or greater than 75% and less than 90%	90%
Equal to or greater than 90%	100%

Eligible applicants will be permitted to calculate the estimated embedded RST and SST, as applicable, either (i) at a prescribed amount² per square metre of floor space in the home (the “Floor Space Method”) or (ii) on the selling price of the home, calculated at 2% of the total consideration or fair market value, as the case may be, established for GST purposes (the “Selling Price Method”).

An application for the Ontario THR or British Columbia THR must generally be filed before July 1, 2014. However, where a THR is calculated based on the Floor Space Method, such an application can be filed anytime on or after July 1, 2010. If the Selling Price Method is used, the applicant cannot claim it before the day the HST will be payable or the TTA is deemed to have been collected, as applicable.

² In British Columbia the prescribed amount is \$60.00 per square metre. In Ontario the prescribed amount is \$45.00 per square metre.

Builder disclosure requirements

Where an Agreement for a New Home (or rental home for Ontario purposes) is entered into after June 18, 2009 for Ontario or November 18, 2009 for British Columbia, and before July 1, 2010, the builder must disclose in the Agreement whether the provincial portion of the HST applies to the sale and whether the stated price in the Agreement includes the applicable provincial portion of the proposed HST, net of the new provincial housing rebate. In British Columbia, the builder must also disclose whether the price is net of the British Columbia THR. If the builder fails to disclose that the transaction would be subject to the provincial portion of the HST, then the stated price in the Agreement will be deemed to be inclusive of the provincial portion of the HST. In such a case, the purchaser would not be required to pay the provincial component of the HST in addition to the stated price in the Agreement.

Non-residential properties – HST transitional rules

In Ontario and British Columbia, HST will generally apply to the sales of non-residential real property (a “Commercial Property”) where both ownership and possession of the property are transferred to the purchaser on or after July 1, 2010. Sales of real property that are currently exempt under the GST rules will similarly not be subject to HST.

Non-residential properties - leases

In Ontario and British Columbia, the HST will generally apply to a Commercial Property that is supplied by way of lease, licence or similar arrangement (a “Leased Property”) for the part of the lease interval that occurs on or after July 1, 2010. The HST would not, however, apply to a supply of property by way of lease, licence or similar arrangement if the lease interval begins before July 2010 and ends before July 31, 2010. However, Leased Property that is currently exempt from GST will similarly be exempt from HST.

Consideration due or paid after October 14, 2009 and before May 2010

In Ontario and British Columbia, where the lessee is not a consumer (e.g. a business) the HST will generally apply to any lease payment that becomes due or is paid without having become due after October 14, 2009 and before May 2010. However, only the portion of the payment that is for the part of a lease interval that begins on or after July 1, 2010 is subject to the HST. If the lease interval begins before July 2010 and ends before July 31, 2010, then the HST will not apply.

In both provinces, where the lessee is not a consumer, the lessee may be required to self-assess the provincial portion of the HST, either (i) in their GST/HST return for the reporting period that includes July 1, 2010, if the due date for that return is before November 2010, or (ii) in any other case, before November 2010.

Consideration due or paid on or after May 1, 2010 and before July 2010

In Ontario and British Columbia, the HST will generally apply to any lease payment that becomes due or is paid without having become due on or after May 1, 2010 and before July 2010. However, only the portion of the payment that is for the part of a lease interval that occurs on or after July 1, 2010 is subject to HST (unless the lease interval begins before July 2010 and ends before July 31, 2010, in which case no HST will apply). In such a case, the lessor must account for the provincial portion of the HST in their GST/HST return for the reporting period that includes July 1, 2010, and would charge the lessee the HST. The lessee would generally be able to claim input tax credits for the HST paid if they would normally be entitled to claim input tax credits for any GST they pay.

Consideration due or paid on or after July 1, 2010

In Ontario and British Columbia, the HST will generally apply to a lease payment that becomes due or is paid without having become due on or after July 1, 2010 to the extent that the consideration is for the part of a lease interval that occurs on or after July 1, 2010 unless the lease interval begins before July 2010 and ends before July 31, 2010.

Progress payments

Payment before or on October 14, 2009

In Ontario and British Columbia, the provincial portion of the HST will not apply to a progress payment that becomes due or is paid on or before October 14, 2009.

Payment after October 14, 2009

In Ontario and British Columbia, the HST will generally apply to a progress payment made under contracts to construct, renovate, alter or repair real property (a "Construction Contract") where the progress payment becomes due after October 14, 2009 to the extent that the payment can reasonably be attributed to property delivered or services performed on or after July 1, 2010. Where the progress payment can be attributed to property delivered or services performed before July 1, 2010, the payment will not be subject to the provincial portion of the HST.

Where a progress payment becomes due or is paid without having become due after October 14, 2009 and before July 2010, the payment will be deemed to become due, and paid on July 1, 2010. To the extent that the progress payment is for property delivered or services performed on or after July 1, 2010, the HST will be deemed to become payable on July 1, 2010. In these circumstances, the supplier must account for the provincial portion of the HST in its GST/HST return for the reporting period that includes July 1, 2010, and if eligible, the payor can claim an input tax credit for the provincial portion of the HST in their return that includes the July 1, 2010 period.

For further information, please contact your Stikeman Elliott representative, the authors listed above or any other member of our Tax Group listed at www.stikeman.com

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