

The HST and real estate – 101 (Enhanced Edition)

Director, New Initiatives and Legal Engagements, Assyst Real Estate, TELUS, backed by Emergis

On July 23, 2009 the government of British Columbia announced its intention to piggy-back the 7% Provincial Sales Tax ('PST') onto the 5% federal Goods and Services Tax ('GST') on July 1, 2010 (the first "key date"). Significant enhancements and transitional rules affecting real estate were announced effective November 18, 2009 (the second "key date"). Assuming the enabling legislation is passed provincially and federally, one 12% value-added tax would be established, to be called the Harmonized Sales Tax ('HST').

Nothing underscores the differences between the PST and GST better than real estate. This newsletter provides an overview of the most common situations facing conveyancing lawyers and notaries.

Resale homes

As with the GST, purchases of resale homes will be exempt from HST. Not so for many of the services associated with resale home transactions, including appraisals and home inspections. Under the HST, the applicable tax rate will more than double, from 5% to 12%.

Commercial tenancies

No significant change is anticipated. Starting July 1, 2010, 12% HST will be collected on commercial rent rather than 5% GST. Like today's GST rules, offsetting input tax credits for the full amount of HST paid will be available to commercial tenants (i) that are GST registrants and (ii) that provide taxable supplies¹ or zero-rated supplies². Providers of exempt supplies³, on the other hand, face rent hikes of 7% as of July 1, 2010.

Purchases of commercial properties

Once again, the net effect of the HST should be nil for buyers of commercial properties who are GST registrants not providing an exempt supply. As under the current GST regime, immediate input tax credits will be available to offset the full HST payable under the "self-assess" rules.



- 1 On taxable supplies, suppliers charge GST at the rate of 5%, and are eligible to claim input tax credits for GST paid on expenses.
- 2 For zero-rated supplies, suppliers charge GST at a rate of 0%, but are still eligible to claim input tax credits for GST paid on expenses. Zero-rated supplies include groceries, prescription drugs and medical devices.
- 3 Suppliers of exempt supplies do not charge GST, and are not entitled to claim input tax credits for GST paid on expenses. Examples of exempt supplies are many health and dental services, long-term residential rents, and domestic financial services.

Residential tenancies

Residential tenancies, an exempt supply under the GST, will also be an exempt supply for HST purposes. That means residential landlords (a) cannot collect HST from residential tenants, and (b) cannot claim input tax credits for HST paid on expenses. Many services not subject to PST today will be subject to HST as of July 1, 2010 (examples: property management fees, maintenance costs, repair services and electricity). As a result, residential landlords will face significantly higher costs under the HST.

Real estate commissions

Under the HST, real estate commissions will be subject to 12% HST, not 5% GST. As with the GST, sellers of commercial properties who are GST registrants and not exempt suppliers can claim a full offsetting input tax credit for HST paid on the commission. This option is not available to individuals selling a personal-use property (such as a principal residence).



What about real estate commission on deals that straddle July 1, 2010 (i.e. a purchase agreement signed before that date, with closing afterwards?) The provincial Ministry of Finance provides some assistance in HST Tax Information Notice No. 1: ***"The HST would generally not apply... to a supply of a service if all or substantially all (90 per cent or more) of the service is performed before July 2010"***⁴

Mortgage broker fees

The services provided by mortgage brokers are an exempt supply under the GST, meaning no GST is charged on their fees. The status quo will likely continue under the HST.

New homes/new condominiums

Most affected by the HST will be new homes and condominiums⁵.

While GST is levied directly on the price of a new home/condominium, that doesn't mean new homes/condominiums are exempt from PST. Instead, a PST component is buried in their sale price (taxes paid on building materials like wood, cement, cabinets, toilets and carpets). According to government estimates, at least 2% of the price of a new home/condominium on average is 'embedded' (or hidden) PST. As a result, the effective rate of PST on a new home/condominium in British Columbia today is about 2%⁶.

The basic rule for new homes/condominiums under the HST is simple. **AS OF JULY 1, 2010, 12% TAX WILL BE CHARGED ON THE ENTIRE PURCHASE PRICE OF ANY NEW HOME OR CONDOMINIUM, (5% FEDERAL, 7% PROVINCIAL), LESS ANY APPLICABLE REBATES (FEDERAL AND PROVINCIAL).**

4 HST General Transitional Rules, Government of British Columbia, page 5, issued October 14, 2009 www.sbr.gov.bc.ca/business/Consumer_Taxes/Harmonized_Sales_Tax/HST_Transitional_Rules.html accessed on October 18, 2009.

5 Unless otherwise indicated, the expression "new home/condominium" includes a home that has undergone a "substantial renovation". For more information on what constitutes a "substantial renovation", see Technical Information Bulletin B-092 Substantial Renovations and the GST/HST New Housing Rebate, available at <http://www.cra-arc.gc.ca/E/pub/gm/b-092/b-092-e.pdf> accessed on November 22, 2009.

6 Government of British Columbia website, www.gov.bc.ca/hst/faq.html accessed on October 18, 2009.

The federal GST New Housing Rebate is well known – 36% of the GST payable on the first \$350,000 of purchase price (maximum \$6,300). Between \$350,000 and \$450,000 the rebate is phased-out pro-rata; it's totally eliminated for new home/condominium prices above \$450,000. These numbers have remained unchanged since the GST was introduced in 1991.

Without any provincial rebate, new home/condominium prices would jump by 5-7% under the HST. To prevent this, a rebate of the B.C. HST will be available in addition to the GST New Housing Rebate.

Initially this rebate was only scheduled to apply to the first \$400,000 of purchase price. As of November 18, 2009 the threshold for the B.C. HST new housing rebate was "enhanced" to \$525,000, a figure higher than the average new home price in the province,⁷ and the highest provincial rebate threshold in Canada.

B.C.'s HST new housing rebate will be 5/7ths of B.C. HST payable (or 5% of the purchase price for a new home/condominium) on the first \$525,000 of purchase price. To qualify for the B.C. new housing rebate, the new home/condominium unit must be the buyer's primary residence.

For new home/condominium prices up to \$525,000, the net B.C. HST is 2% of the purchase price, a figure that is comparable to the amount of embedded PST currently in a new home/condominium. The maximum rebate of \$26,250 would be reached at \$525,000, when the net B.C. HST payable would be \$10,500.

For new home/condominium prices over \$525,000, the net B.C. HST is (a) 2% of the purchase price on the first \$525,000 of purchase price, regardless of the price, and (b) 7% on the balance. For prices over \$525,000, these numbers reflect a flat rebate of \$26,250 (or 5% of \$525,000).

CURRENT SYSTEM – 5% GST	
Price (excluding GST)	Rebate
Less than \$350,000	GST New Housing Rebate (36% of 5% of price)
From \$350,000 to \$450,000	Phase-out of GST New Housing Rebate
Over \$450,000	GST New Housing Rebate eliminated
AS OF JULY 1, 2010 – 12% HST; FEDERAL PORTION (GST): 5%; PROVINCIAL PORTION: 7%	
Price (excluding GST and B.C. HST)	Rebate
Less than \$350,000	Full federal (GST) New Housing Rebate (36% of 5% of price); Full B.C. HST New Housing Rebate (5% of price) (net tax is 2%)
From \$350,000 to \$450,000	Phase-out of federal (GST) New Housing Rebate; Full B.C. HST New Housing Rebate (5% of price) (net tax is 2%)
From \$450,000 to \$525,000	No federal (GST) New Housing Rebate Full B.C. HST New Housing Rebate (5% of price) (net tax is 2%)
Over \$525,000.00	No federal (GST) New Housing Rebate Flat \$26,250 B.C. HST New Housing Rebate (5% of \$525,000.00)

⁷ According to the provincial government, \$400,000 was the median price of new housing in urban areas in B.C. in 2008. See footnote 6

What are the gross sales taxes (GST and HST), the rebates, and the net sales taxes payable on new homes/condos in different prices ranges?

CURRENT SYSTEM – 5% GST			
Price (excluding GST)	Gross GST payable	GST New Housing Rebate	Net GST payable
\$350,000	\$17,500	(\$6,300)	\$11,200
\$400,000	\$20,000	(\$3,150)	\$16,850
\$450,000	\$22,500	NIL	\$22,500
\$500,000	\$25,000	NIL	\$25,000
\$550,000	\$27,500	NIL	\$27,500

AS OF JULY 1, 2010 – 12% HST; FEDERAL PORTION (GST): 5%; PROVINCIAL PORTION: 7%							
Price (excluding GST and provincial HST)	Gross federal tax (GST)	Gross provincial tax (HST)	Gross Taxes payable	GST New Housing Rebate	B.C. New Housing Rebate	Total Rebates	Net Taxes payable
\$350,000	\$17,500	\$24,500	\$42,000	(\$6,300)	(\$17,500)	(\$23,800)	\$18,200
\$400,000	\$20,000	\$28,000	\$48,000	(\$3,150)	(\$20,000)	(\$23,150)	\$24,850
\$450,000	\$22,500	\$31,500	\$54,000	NIL	(\$22,500)	(\$22,500)	\$31,500
\$500,000	\$25,000	\$35,000	\$60,000	NIL	(\$25,000)	(\$25,000)	\$35,000
\$550,000	\$27,500	\$38,500	\$66,000	NIL	(\$26,250)	(\$26,250)	\$39,750

To illustrate how the B.C. new housing rebate works, assume a new home is bought for \$600,000. The total net B.C. HST would be \$15,750: (a) 2% on the first \$525,000 [or \$10,500] and (b) 7% on the remaining \$75,000 [or \$5,250]. The rebate would be \$26,250 (or 5% of the first \$525,000). Without a provincial rebate, the total B.C. HST would have been \$42,000. According to the original government proposal, the net B.C. HST on that \$600,000 purchase would have been \$22,000 (with the provincial rebate being \$20,000).

In a nutshell:

- for new homes/condominiums priced up to \$525,000, 2% net provincial HST will be payable
- for new homes/condos priced \$525,000 and over
 - 2% net provincial HST will be payable on the first \$525,000 (i.e. \$10,500)
 - 7% provincial HST will be payable on the portion over \$525,000

Different thresholds govern the GST and B.C. New Housing Rebates. The following chart, based on one published by the B.C. Real Estate Association, illustrates the available rebates at various price ranges.

What are the gross sales taxes (GST and HST), the rebates, and the net sales taxes payable on new homes/condos in different prices ranges?

New residential rental property ('investor') rebate

When the GST was established in the early 1990s, the GST New Housing Rebate was limited to individuals buying a new home/condominium as their primary residence. After years of investor lobbying for a level playing field, the rules were changed in 2001 when the GST New Residential Rental Property Rebate (aka the GST Investor Rebate) was introduced for investors who buy or build new residential housing.

The HST will include a similar rebate, with the same monetary thresholds, tax rates and maximum rebate as the B.C. new housing rebate.

The B.C. HST investor rebate will also include the two 1-year qualifying conditions in the GST investor rebate program: (a) landlords owning the property for a year; and (b) the first tenant being 'reasonably expected' to occupy it for a year. Due to these two qualifying conditions, builders can't credit investors/buyers with the GST investor rebate on closing. Instead, investors must pay the amount of the "lost rebate" to the builder as a closing adjustment, and apply to the Canada Revenue Agency after closing to recoup it. The same will apply under the B.C. HST.



Transitional rules

Not only are transitional rules a key component of any new tax regime, they are the most important rules for existing clients. Of concern are transactions that straddle the July 1, 2010 start date. Issues to be addressed include what deals to grandparent (i.e. to exempt from HST); what is 'closing' for new condominiums (possession or title transfer); and the need to avoid double taxation.

The transitional rules for new home/condominiums were announced as of November 18, 2009. On that day, the door also closed on any further "grandparented" deals, as described below.

Three criteria determine whether B.C. HST is payable on the purchase of a new home/condominium:

- When the contract was entered into (the key date being November 18, 2009);
- When occupancy or ownership of the property is transferred (the key date being July 1, 2010);
- What is being bought (a new home or a new condominium).

Four scenarios are possible, each applying equally to owner-occupants and investor/buyers:

- Where a contract is entered into on or before November 18, 2009, and either occupancy⁸ or ownership of a new home/condominium is transferred before July 1, 2010, the deal is not subject to B.C. HST, based on the occupancy/closing date
- Where a contract is entered into on or before November 18, 2009, and both occupancy and ownership of a new home/condominium are transferred after June 30, 2010, the deal is not subject to B.C. HST, based on the grandparent exemption (this is the only time the grandparent exemption applies)

⁸ Reference to "occupancy" addresses the uniqueness of new condominium transactions, where possession is transferred to a purchaser at interim closing, while ownership is transferred at final closing.

- 3) Where a contract is entered into after November 18, 2009, and either occupancy or ownership of a new home/condominium is transferred before July 1, 2010, the deal is not subject to B.C. HST, based on the occupancy/closing date
- 4) **Where a contract is entered into after November 18, 2009, and both occupancy and ownership of a new home/condominium are transferred after June 30, 2010, THE DEAL IS SUBJECT TO B.C. HST, as the occupancy/closing date exemption and the grandparent exemption do NOT apply. However, the buyer may be entitled to receive the PST Transitional Housing Rebate**

A chart at the end of this newsletter illustrates how these scenarios fit together.

PST Transitional housing rebate

New homes/condominiums that close after June 30, 2010 could have a significant amount of PST embedded in the price, as PST had been paid on the building materials used in their construction. The PST Transitional Housing Rebate is designed to prevent double taxation (buyers paying both HST plus embedded PST).

The PST Transitional Housing Rebate reflects the estimated embedded PST in a new home/condominium, based on the state of construction on July 1, 2010. Two ways to calculate it are proposed: (a) the "floor space" method (\$60 per square metre of floor space), and (b) the "selling price" method (2% of the purchase price of the new home/condominium).

This chart describes how the degree of completion translates into estimated embedded PST content (to qualify for the PST Transitional Housing Rebate, HST must have been paid on closing):

% COMPLETE AS OF JULY 1, 2010	% OF ESTIMATED PST CONTENT
Less than 10%	0%
10% or more, but less than 25%	25%
25% or more, but less than 50%	50%
50% or more, but less than 75%	75%
75% or more, but less than 90%	90%
90% or more	100%

To illustrate, a new home is bought for \$600,000. Closing is July 15, 2010 and B.C. HST is payable. On closing, the total net B.C. HST payable is \$15,750 (2% on the first \$525,000 [or \$10,500] and 7% on the remaining \$75,000 [or \$5,250]). As the home was 95% complete on July 1, 2010, the estimated PST content is 100%. Using the selling price method, the estimated embedded PST (and PST Transitional Housing Rebate) is 100% of 2% of the \$600,000 price, or \$12,000. That rebate slashes the buyer's overall provincial tax liability from \$15,750 to \$3,750.

Eligibility for the PST Transitional Housing Rebate will not affect the buyer's ability to claim either the B.C. new housing rebate or the investor rebate.

Buyers could obtain the PST Transitional Housing Rebate in one of two ways: (a) from the builder as a closing adjustment, or (b) by applying to the Canada Revenue Agency after closing (buyers would have until July 1, 2014 to apply for the rebate). In the second situation, the buyer would have to obtain a prescribed certificate from the builder on closing stating the degree of completion on July 1, 2010. Unfortunately, there appears to be no obligation that builders provide buyers with the required certificate.

Who would be eligible for the PST Transitional Housing Rebate?

- Buyers of new/substantially renovated homes
- Builders who first rent a new home after June 30, 2010
- But not buyers of new condominium units. The PST Transitional Housing Rebate is only available to builders, not buyers, of new condominiums.

Property transfer tax ('PTT')

How will the HST mesh with B.C.'s Property Transfer Tax? PTT is paid on the fair market value of a property being transferred. Today, GST payable is deducted from the fair market value of a new home/condominium in calculating PTT, to avoid paying tax (PTT) on tax (GST). Similar rules will govern the HST (i.e. a property's fair market value would be lowered by the B.C. HST payable, in calculating the PTT).

Other HST rules

Builder contracts for new homes/condominiums must disclose (a) if the deal is subject to the B.C. HST, and (b) if so, does the price include the B.C. HST net of the B.C. new housing rebate. If inadequate or incomplete disclosure is

made, the purchase price is deemed to include the B.C. HST (i.e. the builder is responsible for paying it). This arrangement is designed to provide certainty to both buyers and builders.

A separate set of transitional rules will govern the following situations (the scope of this newsletter does not allow a more detailed description of these transactions):

- Purchases of new homes on leased land
- Purchases of new mobile/modular homes and floating homes
- Purchases of qualifying shares in a housing co-op
- Construction of owner-built homes
- Construction of traditional apartment buildings and long-term care residential facilities
- Assignments and flips

HST Transitional rules chart

With this chart, users can determine at a glance the provincial tax consequences for any particular new home/condominium purchase, and why:

DESCRIPTION	NEW HOME	NEW CONDO UNIT
CONTRACT ON OR BEFORE NOVEMBER 18, 2009; EITHER OCCUPANCY OR CLOSING BEFORE JULY 1, 2010	B.C. HST does NOT apply (based on occupancy/ closing date)	B.C. HST does NOT apply (based on occupancy/ closing date)
CONTRACT ON OR BEFORE NOVEMBER 18, 2009; BOTH OCCUPANCY AND CLOSING AFTER JUNE 30, 2010	B.C. HST does NOT apply (grandparented)	B.C. HST does NOT apply (grandparented)
CONTRACT AFTER NOVEMBER 18, 2009; OCCUPANCY OR CLOSING BEFORE JULY 1, 2010	B.C. HST does NOT apply (based on occupancy/ closing date)	B.C. HST does NOT apply (based on occupancy/ closing date)
CONTRACT AFTER NOVEMBER 18, 2009; BOTH OCCUPANCY AND CLOSING AFTER JUNE 30, 2010	B.C. HST applies; No occupancy/closing date or grandparent exemption; Buyer MAY BE eligible for PST Transitional Housing Rebate	B.C. HST applies; No occupancy/closing date or grandparent exemption; Buyer NOT eligible for PST Transitional Housing Rebate



Alan G. Silverstein is the Director, National Legal Engagements for Assyst Real Estate. After 29 years in private practice in the Toronto area, Alan joined the team in 2006 to head up the adoption of Assyst Real Estate by real estate lawyers. A Bencher at the Law Society of Upper Canada, Alan is also a member of its Real Estate Working Group.

assyst
Real Estate

Assyst Real Estate is a web-based application that electronically links lenders and lawyers, simplifying how mortgage transactions are instructed, funded and reported. By streamlining the way mortgage files are processed, it increases staff efficiency, saving valuable time and money. Assyst Real Estate is Canada's #1 electronic mortgage processing program. More legal professionals in Canada use it today to complete mortgage transactions electronically than any other program.

 **TELUS**
the future is friendly®

For further information, please visit telus.AssystRealEstate.com.

The purpose of this newsletter is to provide information as to developments in the law. It does not contain a full analysis of the law nor does it constitute a legal opinion.

The Assystant logo and name are trademarks of TELUS.

© TELUS 2009. All rights reserved THE ASSYSTANT 0903