

HST- IN TRANSITION

I have sent out previous newsletters about the effect of the pending HST on new housing sales. This newsletter will summarize some of the transitional rules as set out by the Ministry in their publication “**Helping Homebuyers and the Housing Industry with an Enhanced New Housing Rebate, a New Rental Housing Rebate and Transitional Rules**” (the “Ministry Publication”) (please see <http://www.rev.gov.on.ca/english/notices/str/pdf/02.pdf> for a copy or contact the writer). This is meant to be applicable for houses or condominium units being sold, not rental property.

First, a few points of clarification. Most people have been referring to the new regime as the Harmonized Sales Tax or HST. The Province of Ontario in the Ministry Publication has used the phrase “Single Sales Tax”. So be aware that may become the official name, but I will continue in this newsletter to call the 13% regime the HST.

Next, in my newsletter of June 22nd, I indicated that the transitional rules do not involve the purchaser. As discussed below, this is not always the case.

Finally, the Ministry Publication is not legislation and cannot be considered as the last word and is vague and missing some details, but it is important that if you are dealing with new homes that you be familiar with it. This newsletter cannot be relied upon as a legal opinion or a statement of the law but is intended to be a quick summary.

Grandparented Deals

Agreements for freehold homes or residential condominium units signed on or before June 18, 2009 are not subject to the HST, only the 5% GST, no matter when they close. But, these deals may be subject to transitional adjustments and transitional rebates if they close on or after July 1st, 2010 (the “Effective Date”). These are called **grandparented** deals.

Agreements for freehold homes or residential condominium units signed after June 18, 2009 and closing on or after July 1st, 2010 (the “Effective Date”) will be subject to 13% HST and may be subject to transitional adjustments and transitional rebate. These are called **non-grandparented** deals.

It should be noted that for condominium units to be subject to HST, both possession **and** title must be transferred after the Effective Date. If for example, a buyer is in possession as of June 30, 2010 but final closing takes place after that date, the unit will be subject to 5% GST only, even if the Offer was signed after June 18, 2009.

Please also note that besides the transitional rebates, the New Housing Rebates are also applicable.

The Novation Trap

Builders should be aware that material amendments to these grandparented agreements may cause the Canada Revenue Agency to consider them to have been rewritten. In legal terms this is called novation. Novation of a contract means when an existing agreement is so changed that it is considered at law to be a new contract. The precise boundaries of novation are hard to define. Red flags would definitely include assignment of an agreement, adding new parties as purchaser or a change of lot or unit purchased. Be cautious when considering changing elevation, model types or material price changes as a result of extras on these deals. It would be good practice to add a clause to amendments to grandfathered agreements which are closing after the Effective Date, to define who is to be responsible for any increased taxes if the amendment leads to an increase in the tax exigible or a reduction in a rebate.

TRANSITIONAL TAX ADJUSTMENTS AND REBATE FOR FREEHOLD HOMES

With the imposition of HST, the Retail Sales Tax (RST) will no longer be payable. The Province has determined that the RST paid by builders and buried in the price of a new home was approximately 2% of the sales price of new homes. The HST is imposed in the same manner as GST in that builders will be entitled to input tax credits for HST paid on their inputs and will remit the amount of HST collected on their sales. The reason why there are transitional issues is that the province basically wants to ensure that they get their 2% of the sales price no matter when the deal closes.

Tax Adjustment Payable

- applies to **grandparented** deals when the house is under construction as of the Effective Date. As noted the Purchaser will pay only the 5% GST on closing.
- payable by the builder.
- based on the percentage completion as of the Effective Date calculated on a sliding percentage of 2% times the sales price. Please see the Ministry Publication at page 3 for the exact formula.
- Example: If the sales price is \$400,000 (based on the calculation for GST purposes) and the house is 80% complete on the Effective Date, using the Ministry's formula, the tax adjustment payable will be 10% of 2% of the sales price or \$800.
- The theory is that the Province wants to collect 2% of the sales price as its sales tax. It is assumed that the builder would have paid 90% of that by paying the RST on its inputs up to the Effective Date and this adjustment picks up the balance.

RST Transitional Housing Rebate

- for **non-grandparented** freehold houses which were under construction or completed as of the Effective Date. The Purchaser will be paying the 13% HST on closing.
- payable to the buyer but can be assigned to the builder
- based on degree of completion of the home as of the Effective Date.

- can be calculated by either the floor space method (to be prescribed by regulations) or on 2% of the selling price as calculated for GST purposes. Please see the Ministry Publication at page 5 for the exact formula.
- Example: if the sales price is \$400,000 (based on the calculation for GST purposes) and the house is 80% complete on the Effective Date, using the Ministry's formula, the rebate payable will be 90% of 2% of the sales price or \$7,200.
- The theory is that as the Province is now picking up its tax on closing, the hidden RST component in the value of construction in place as of the Effective Date, estimated at \$7,200, is refunded.

TRANSITIONAL TAX ADJUSTMENTS AND REBATE FOR CONDOMINIUM UNITS

Tax Adjustment Payable

- applies to **grandparented** deals for condominium units closing after the Effective Date
- payable by the builder
- calculated as 2% of the sales price as calculated for GST purposes

RST Transitional Housing Rebate

- for **grandparented or non-grandparented** condominium units closing after the Effective Date
- payable to the builder
- based on degree of completion as of the Effective Date. See the Ministry Publication at page 5 for the exact formula.
- can be calculated by either the floor space method (to be prescribed by regulations) or on 2% of the selling price as calculated for GST purposes.
- Example: if the sales price is \$400,000 (based on the calculation for GST purposes) and the "home" is 80% complete on the Effective Date, the rebate payable will be 90% of 2% of the sales price or \$7,200. (Please note I have used the word "home" as it is the word used by the publication even though it obviously ambiguous as to what it includes. The legislation and regulations will hopefully be more precise).
- This adjustment and rebate taken together approximate 2% sales tax on the value of the unit.

Conclusion

Tax statutes are never easy to comprehend but I hope this article will help you understand the rules a little better. The OHBA website www.homesontario.com contains more material which would assist in learning more about this topic.

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