

# LATHEM'S LEGALS

Real Estate Law Series of Newsletters

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## HST on New Home and Condominium Assignments Edition

The main purpose of this edition is to draw attention to Canada Revenue Agencies (CRA) recent interpretation of how HST applies to assignment of New Home and Condominium Contracts. I have to note that there are lots of realtor websites that claim that by assigning an Agreement before closing an "investor" avoids a lot of expenses in particular the HST.

**In fact by assigning the contract before closing the Assignor in fact creates a much bigger potential HST issue.**

### The July 2011 Bulletin

CRA issued a bulletin July of 2011 stating in effect that where HST is applicable to the Assignment of a new Condominium or House contract it is payable on the whole purchase price. To be very specific about what the bulletin says, I will give some useful examples:

1. If the Purchaser (Assignor) enters into an Agreement with the builder for \$300,000.00, HST included as if the Purchaser (Assignor) is moving in, then sells the agreement for an additional \$200,000.00 profit, listing in the Assignment Agreement \$500,000.00 as the purchase price, the HST will be payable on the \$500,000.00 listed as the purchase price (\$65,000.00) and not the \$200,000.00 price (\$26,000.00).
2. The bulletin also suggests that the Assignee would be disqualified from claiming the rebate with the builder which under \$450,000.00 can increase the price as much as 8%.
3. There is a big loophole however. Where the Assignor honestly acquired the property to live in and was forced to assign the unit or even sell because of a change in circumstances, the exemptions relating to acquiring it as your residence still stay in place.

### Golden Rules

Some golden rules when assessing your tax filing position.

1. CRA has an unofficial 1 year rule. Principal residence and HST claims that they review are generally those where the properties are bought and sold within 1 year or less.
2. The burden is on the taxpayer to show that they really did qualify for the tax exemptions. CRA will look at such things as where their tax returns show they are living, their family situation. For example if they are married with 2 minor children does it make sense that they say they are buying a 1 bedroom condominium in Toronto to live in?
3. There is an unofficial 3 transaction rule or pattern rule. Even if a person purchases and sells homes after a year typically if they do 3 purchases in a little more then a year each the CRA may chose to scrutinize the transactions as a business. Real Estate Agents or investors need also to be cognizant of having such transactions treated as sales of Real Estate Inventory and not capital assets.

## **Solution or Risk Reduction Strategy**

Obviously if one really does qualify for the exemption this bulletin is not a problem. I was advised once by CRA on making a GST inquiry years ago that if the sale occurs in less than a year the taxpayer should expect CRA to question the transaction and they should simply be prepared to substantiate their position.

What I am recommending to my clients and all the people that we do business with is that the purchase price in the Assignment Agreement be listed as the Purchase Price of the Assignment Agreement itself, and not the total cost of the acquisition. In other words using the above example the purchase price should be listed as \$200,000.00 and the obligations of the parties should be made clear. That is the assignee is also agreeing to reimburse the buyer for their deposits and assume the buyers obligations under the contract, i.e. pay the balance of purchase price owing on closing.

I call this a risk reduction strategy because there are no CRA rules or Court Decisions addressing this directly and the recommendation to a cautious client is to have their CA obtain a tax ruling. However, I recommend this as a legitimate position to take because an Assignment Agreement is really an agreement to purchase or assign a contract and in and of itself is a contract on its own. The lines seem to have become blurred sometime in the late 1990s and early 2000s when Assignment contracts were most often drawn by lawyers and then the bulk of them started being drawn by Real Estate Agents.

My view is that most lawyers who draft agreements in the absence of the current OREA forms would specify the purchase price as \$200,000.00 in the above example and not \$500,000.00. Real Estate agents have come to typically list \$500,000.00 because it is good for market, commission and financing. However, these issues certainly can be addressed in other ways in the agreement.

In my view if you unwisely list the purchase price as \$500,000.00 then of course CRA is going to take the position that this is the purchase price.

For those of you interested in reading the CRA Bulletin it can be reviewed at:

<http://www.cra-arc.gc.ca/E/pub/gi/gi-120/gi-120-e.pdf>

We hope that you find this issue of our newsletter interesting and we look forward to suggestions regarding what other issues you may want covered in upcoming newsletters.

Yours sincerely,

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