

GST REDUCTION TRANSITIONAL RULES AND NEW ONTARIO LAND TRANSFER TAX GUIDELINES MAY 10, 2006

OVERVIEW

Following the May 2, 2006 Federal Budget proposal to reduce the GST rate to 6%, we are pleased to provide additional details of the transitional rules and the effect of the new 6% GST rate on residential real property sales in the event: (1) the Builder reduces the GST included prices in order to pass on the GST savings to the Purchaser (scenario 1), and (2) the GST included price is unchanged and the Builder retains the GST savings (scenario 2).

In addition, this Tax News will highlight new guidelines recently issued by the Ontario Ministry of Finance to ensure that land transfer tax applies to the full value of the purchase consideration.

GST TRANSITIONAL RULES FOR SALES OF REAL PROPERTY

Implementation of the GST Reduction to 6% for Sales of Real Property

The following schedule summarizes the GST transitional rules applicable to sales of new residential real property:

<u>Sale Type</u>	<u>Agreement Date</u>	<u>Closing Date (Freehold) Occupancy Date (Condominium)</u>	<u>Builder's Rate of GST to Remit</u>	<u>Transitional Adjustment Available to Purchaser</u>
1	Before May 3, 2006	Before July 1, 2006	7%	No
2	After May 2, 2006	Before July 1, 2006	7%	No
3	After May 2, 2006	After June 30, 2006 ¹	6%	No
4	Before May 3, 2006	After June 30, 2006 ¹	7%	Yes

To receive a Transitional Adjustment, that reflects the GST rate reduction to 6%, net of any corresponding New Housing Rebate adjustment, the Purchaser must file a claim with the Canada Revenue Agency ("CRA").

¹ In the case of a condominium unit, the transfer of both ownership and possession must take place after June 30, 2006.

Application of GST Transitional Rules To The Sale of New Housing – Where Builder Passes on GST Savings to Purchaser (Scenario 1)

This table shows the application of the GST transitional rules where the Builder passes the GST savings to the Purchaser. The calculations assume the Purchaser is eligible for the New Housing Rebate (the “Rebate”) and the Purchaser assigns the Rebate to the Builder.

Desired Purchase Price Exclusive of GST		Sales Type 1 and 2 (Note a)	Sales Type 3 (Note a)	Sales Types 4 (Note a)		
		Current GST Rate of 7%	Proposed GST Rate of 6%	Net GST Remitted by Builder at 7% Rate	Transitional Adjustment Paid to Purchaser	Net GST Paid by Purchaser
\$ 200,000	Gross GST	\$ 14,000	\$ 12,000	\$ 8,960	\$ 1,280 (Note c)	\$ 7,680
	Rebate Assigned ¹	<u>(5,040)</u>	<u>(4,320)</u>			
	Net GST	<u>8,960</u>	<u>7,680</u>			
	GST Included Price (Note b)	<u>\$ 208,960</u>	<u>\$ 207,680</u>			
\$ 300,000	Gross GST	\$ 21,000	\$ 18,000	\$ 13,440	\$ 1,920 (Note d)	\$ 11,520
	Rebate Assigned ²	<u>(7,560)</u>	<u>(6,480)</u>			
	Net GST	<u>13,440</u>	<u>11,520</u>			
	GST Included Price (Note b)	<u>\$ 313,440</u>	<u>\$ 311,520</u>			
\$ 400,000	Gross GST	\$ 28,000	\$ 24,000	\$ 23,625	\$ 3,375 (Note e)	\$ 20,250 (Note g)
	Rebate Assigned ²	<u>(4,375)</u>	<u>(3,780)</u>			
	Net GST	<u>23,625</u>	<u>20,220</u>			
	GST Included Price (Note b)	<u>\$ 423,625</u>	<u>\$ 420,220</u>			
\$ 500,000	Gross GST	\$ 35,000	\$ 30,000	\$ 35,000	\$ 5,000 (Note f)	\$ 30,000
	Rebate Assigned ²	<u>-</u>	<u>-</u>			
	Net GST	<u>35,000</u>	<u>30,000</u>			
	GST Included Price (Note b)	<u>\$ 535,000</u>	<u>\$ 530,000</u>			

Notes:

- (a) Sales Types 1 and 2 include all sales that close before July 1, 2006, regardless of the date of the purchase agreement. Sales Type 3 includes all sales under agreements entered into after May 2, 2006 and closing after June 30, 2006. Sales Type 4 includes all sales under agreements entered into before May 2, 2006 and closing after June 30, 2006. See preceding schedule entitled “Implementation of the GST Reduction to 6% for Sales of Real Property”.
- (b) GST included price (net of Rebate) to yield the desired purchase price exclusive of GST.
- (c) $\$1,280 = \$200,000 \times (0.01 - (5,040/200,000)/7)$
- (d) $\$1,920 = \$300,000 \times (0.01 - (7,560/300,000)/7)$
- (e) $\$3,375 = \$400,000 \times (0.01 - (4,375/400,000)/7)$
- (f) $\$5,000 = \$500,000 \times (0.01 - (0/500,000)/7)$
- (g) \$30 rounding error due to phase-in formula in the draft legislation.

¹ The Rebate is 36% of the GST paid. The maximum Rebate available is \$ 8,750 under 7% GST and \$ 7,560 under 6% GST. The Rebate is phased out for homes priced between \$ 350,000 and \$ 450,000, whereby no Rebate is available for homes priced at \$ 450,000 and more.

Impact of 6% GST Rate for the Sale of New Housing – Where Builder Retains GST Savings (Scenario 2)

This table shows the application of the GST transitional rules where the Builder charges the same GST included price for a housing unit subject to the 6% GST rate, as the price that applied under the 7% GST regime. The schedule applies to sales of new residential real property entered into after May 2, 2006 and closing after June 30, 2006, which are eligible for the proposed 6% GST rate (i.e., Sales Type 3 in the first schedule entitled “Implementation of the GST Reduction to 6% for Sales of Real Property”). This schedule shows the additional proceeds to the Builder, where the Builder retains the GST savings.

The calculations assume the Purchaser is eligible for the Rebate and the Purchaser assigns the Rebate to the Builder.

This schedule does not apply to sales made under agreements entered into before May 3, 2006 and closing after June 30, 2006 (Sales Type 4), since the Transitional Adjustment is paid by the CRA directly to the Purchaser. In addition, this schedule does not apply to sales that close before July 1, 2006 (Sales Types 1 and 2), since the 7% GST rate applies.

Purchase Price Inclusive of GST		Proposed GST Rate of 6% (Note a)	Current GST Rate of 7%	Additional Proceeds to Builder (Sales Type 3)
\$ 200,000	Purchase Price exclusive of GST Gross GST Rebate Assigned ² GST Included Price (Note b)	\$ 192,604 11,556 <u>(4,160)</u> <u>\$ 200,000</u>	\$ 191,424 13,400 <u>(4,824)</u> <u>\$ 200,000</u>	\$ 1,180
\$ 300,000	Purchase Price exclusive of GST Gross GST Rebate Assigned ³ GST Included Price (Note b)	\$ 288,906 17,334 <u>(6,240)</u> <u>\$ 300,000</u>	\$ 287,136 20,100 <u>(7,236)</u> <u>\$ 300,000</u>	\$ 1,770
\$ 400,000	Purchase Price exclusive of GST Gross GST Rebate Assigned ³ GST Included Price (Note b)	\$ 382,194 22,932 <u>(5,126)</u> <u>\$ 400,000</u>	\$ 379,590 26,571 <u>(6,161)</u> <u>\$ 400,000</u>	\$ 2,604
\$ 500,000	Purchase Price exclusive of GST Gross GST Rebate Assigned ³ GST Included Price (Note b)	\$ 471,698 28,302 <u>-</u> <u>\$ 500,000</u>	\$ 467,290 32,710 <u>-</u> <u>\$ 500,000</u>	\$ 4,408

Notes:

- (a) Assumes Builder charges same GST included price.
(b) GST included price (net of Rebate).

² The Rebate is 36% of the GST paid. The maximum Rebate available is \$ 8,750 under 7% GST and \$ 7,560 under 6% GST. The Rebate is phased out for homes priced between \$ 350,000 and \$ 450,000, whereby no Rebate is available for homes priced at \$ 450,000 and more.

NEW ONTARIO LAND TRANSFER TAX (“LTT”) GUIDELINES

In a recent LTT bulletin, the Ontario Ministry of Finance (the “Ministry”) released guidelines to clarify amounts included in the value of the consideration for the LTT on the purchase of a newly constructed home. Currently, the practice used to calculate LTT has generally been to include the base price of the home (not including GST) plus extras and upgrades acquired by the Purchaser. The Ministry states that the definition of the value of the consideration is broad and should not be limited to the purchase price stated in an agreement of purchase and sale.

Additional Amounts Subject to LTT

The Ministry indicates that the value of the consideration for LTT purposes is to include the following:

1. The value of extras and upgrades. Some examples of extras and upgrades that are part of the structure are:
 - upgraded flooring, cupboards, doors, windows, counters, etc.,
 - architectural changes,
 - extra doors and entrances,
 - whirlpool baths,
 - finished basements,
 - roughed in washrooms,
 - fireplaces.
2. The value of upgrades to the land such as:
 - lot premiums,
 - tree planting,
 - sodding and grading,
 - driveway paving.
3. In a new home, Builders typically install gas, hydro and water meters. Where the Builder adds the cost of installation, over and above the purchase price stated in the agreement of purchase and sale, the value of these installations are to be included in determining the value of the consideration.
4. The definition of value of consideration includes the value of any liability assumed and the value of any benefit conferred as part of the arrangement relating to the conveyance. Where the Builder has incurred miscellaneous costs, which it has passed onto the Purchaser as part of the arrangement relating to the conveyance, such amounts form part of the value of the consideration. Some examples are:
 - lot levies,
 - development charges,
 - school levies,
 - increases in development levies imposed by a municipality,

- the vendor's Law Society of Upper Canada transaction levy surcharge,
- a late request for upgrades fee,
- the Ontario New Home Warranty Plan fee,
- architect's fees.

5. Where a Purchaser of a new home assigns an agreement of purchase and sale to another Purchaser, the value of the consideration for LTT on the transfer to the second Purchaser includes:

- the consideration for the assignment;
- the purchase price in the agreement assigned and
- the value of extras, upgrades, installations, and miscellaneous costs passed onto the Purchaser by the Builder.

Entering into separate agreements for the purchase of the land and the construction of a new home thereon will not reduce the value of the consideration, as the cost of both of the agreements would be subject to LTT. Furthermore, the LTT on the sale of a newly constructed home to a second Purchaser will include in its value of consideration not only the purchase price in the resale agreement but the value of any costs and liabilities assumed by the second Purchaser. The amount of a GST New Housing Rebate assigned by a Purchaser to a Builder must also be included in the consideration for LTT purposes.

Amounts Not Included In The Value Of Consideration For LTT

The following amounts included in the selling price of a house are not required to be included in the value of consideration in calculating LTT:

- GST paid on newly constructed homes,
- The value of chattels, such as appliances, and furniture and equipment, that are included in the purchase of the homes, as the amounts paid for these items are subject to Ontario Retail Sales Tax.

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To discuss the impact of these matters on your business, please contact your advisor at Goldfarb, Shulman, Patel & Co. LLP.