The VAT Treatment of Real and Immovable Property in Canada

Benjamin Alarie and Pierre-Pascal Gendron

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Chapter 3
Canada

Benjamin Alarie and Pierre-Pascal Gendron

3.1 INTRODUCTION

This chapter provides an overview of Canada’s federal VAT, the ‘Goods and Services Tax’ (‘GST’), as it applies to real property. In addition to the federal GST, Canada has two other VATs: (1) the ‘Harmonized Sales Tax’ (‘HST’), which applies in several participating provinces; and (2) the ‘Québec Sales Tax’ (‘QST’). The application of all three VATs to real property is addressed.

Some context is appropriate at the outset. Canada’s GST was introduced almost twenty years ago in what can accurately be described as an ‘unreceptive’ political climate. Shortly thereafter, a special report was commissioned federally to consider various options for eliminating the GST and replacing it with an alternative source of revenue.¹ The resulting report concluded, however, that the GST was likely to be a reasonably fair and effective tax, that elimination would be unwise given that many of the transition costs of the introduction of the tax had already been incurred, and that the appropriate solution was to more effectively harmonize the federal GST with the existing provincial Retail Sales Taxes (‘RSTs’).² Harmonization was described as attractive by the special report because it would serve as a way to avoid the high compliance costs for businesses.

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¹ Finance Committee, Special Report, Replacing the GST: Options for Canada (North York, Ontario: CCH Canadian Limited, 1994).
² Ibid., at 39.

associated with multiple sales taxes with multiple bases. Three provinces – New Brunswick, Newfoundland, and Nova Scotia – harmonized their sales taxes with the federal GST in the late 1990s. There was then more than a decade-long lull in harmonization activity. More recently, progress is suddenly being made on this front.

The governments of Ontario and British Columbia have both decided to harmonize their RSTs with the GST from 1 July 2010.3 At the time of writing, some but not all of the legislative details of the harmonization of Ontario and British Columbia VATs with the federal GST have been made public. It is understood that work is ongoing. For the purposes of this chapter, although the newly harmonized regimes have not yet been put into place, it is assumed that the current proposals will be adopted as currently shaped and the features known at this time will be discussed alongside those that have already been implemented.

The federal GST applies in all ten provinces and the three (i.e., non-provincial) territories at a rate of 5%. The HST (normally referred to as ‘GST/HST’ in government literature, and treated as a single tax for administrative purposes in the participating provinces) is a joint federal-provincial VAT that applies at a combined rate of 13%, with the exception of British Columbia, where the combined rate is 12%.4 The QST is a VAT that applies in Québec at a rate of 7.5% on top of a GST-inclusive price. Unlike many VATs, the GST/HST is not typically included in prices although there are some minor exceptions. One open question is whether the inclusion of Ontario and British Columbia as harmonized provinces will trigger a ‘tax-inclusive’ pricing provision that is currently in the Excise Tax Act that calls for all consumer prices to be GST/HST inclusive once Canadian provinces representing more than 50% of the population of the provinces with RSTs or provincial VATs have harmonized.

Although twenty years is not a long period of time in terms of fiscal history, the lessons to be drawn from the Canadian GST experience are far more substantial than the temporal length of the history might otherwise suggest. Canada’s experience merits examination in a comparative exercise such as the one undertaken in this volume because of: (1) the distinctive design features of the GST as it applies to transactions in real property; (2) the mix of common law and civil law traditions that apply in Canada, with the country’s dual Anglophone and Francophone legal legacy; and (3) Canada’s incremental moves to developing


4. The 13% total reflects the federal GST rate of 5% plus an 8% provincial component; the 12% total reflects the federal GST rate of 5% plus a 7% provincial component in British Columbia.
and (ultimately) widely adopting a harmonized system of taxation between the federal and provincial governments. This could well be instructive as providing examples of what to do (and what not to do) for other developed countries with federal structures considering VAT implementation. The obvious and most significant student of this experience is likely to be the United States, the only remaining large developed country without a VAT.

The chapter is organized as follows. Section 3.2 describes the policy, law, and administration of the GST/HST as it applies to real property transactions in the federal GST and the HST of the ‘participating provinces’ of British Columbia, New Brunswick, Newfoundland, Nova Scotia, and Ontario. Section 3.3 correspondingly addresses the policy, law, and administration of the QST in Quebec. Section 3.4 discusses some other aspects of the taxation of real property in Canada, since an understanding of the VAT treatment should be developed in the shadow of the broader tax context. Section 3.5 concludes.

3.2 FEDERAL VAT: GST/HST

Generally speaking, the federal GST follows the nomenclature that is in prevailing usage in most VAT jurisdictions around the world. All three of the Canadian VAT systems (GST/HST/QST) operating today are destination-based. Although there are numerous and byzantine exceptions and exemptions, all types of goods and services consumed in Canada, whether produced domestically or imported, are prima facie subject to GST. Correspondingly, the proper treatment of exports in the system, because it is destination based, is zero-rating. In the real property context, supplies are generally considered to be supplied in the jurisdiction in which the real property is located.

5. The official name of the (combined) federal-provincial tax is the GST/HST, as discussed further in the text below. It is also common in Canada to refer to all three varieties of subnational sales taxes simply as Provincial Sales Taxes (PSTs): for example, see the discussion in Karin Treff & Deborah Ort, *Finances of the Nation* (Toronto: Canadian Tax Foundation, 2009), Ch. 5. Along the same lines, provincial governments usually refer to their sales tax (regardless of how it is characterized in this paper) simply as a PST (provincial sales tax) rather than an RST (retail sales tax) or a VAT (HST or QST, as the case may be). We have adopted the RST terminology here for clarity.


7. With respect to GST and the determination of the place of supply, see s. 142 of the *Excise Tax Act*. With respect to HST and the determination of the provincial place of supply, see Sch. IX of the *Excise Tax Act* regulations.
All supplies of goods and services in each of the three Canadian VAT systems (GST/HST/QST) are assigned to one of three treatment categories: taxable, zero-rated, or exempt. A **taxable supply** is any supply to which the tax applies at a non-zero rate. The supplier (seller) is entitled to an input tax credit (‘ITC’) for the VAT incurred on the input purchases undertaken to provide the taxable supplies (and only VAT incurred on taxable supplies). As the name suggests, a **zero-rated supply** is a supply to which a 0% tax rate applies. Even though the seller does not collect VAT on such supplies, the seller is entitled to a full refund of the VAT incurred on the purchases undertaken to provide the zero-rated supplies. Under the destination-based VAT system, any exported supplies are zero-rated. Finally, an **exempt supply** is one on which the seller does not collect tax. Unlike the zero-rated case, the seller is not entitled to a refund of the VAT incurred on the input purchases undertaken to provide exempt supplies.

The patchwork of sales taxes that apply in different provinces is central to the tax consequences associated with real property transactions. It is particularly important to understand the extent of the only partial harmonization of provincial sales taxes (historically RSTs) with the federal GST. Table 3.1 provides an outline of the interactions of the federal GST with the provincial RSTs as they stand at the time of writing, as well as identifying the provinces with HST. Some additional observations are required. First, the Province of Alberta and the three territories (Yukon, Northwest Territories, Nunavut) have no independent VAT or RST. Nevertheless, because it is a federal tax, the GST applies in these jurisdictions, as it does throughout the rest of the country. Second, although Ontario and British Columbia are listed as having RSTs (as indeed they do at the moment), the two provinces will effectively join the GST/HST system with a provincial VAT component of 8% and 7%, respectively, beginning 1 July 2010.8 Third, the remaining provinces with RSTs will almost certainly harmonize eventually.

sales tax imposed on different activities are not necessarily the same as those of the federal component, nor are they consistent across the HST provinces.10

9. This is a revised and updated version of table found in Richard M. Bird & Pierre-Pascal Gendron, ‘Sales Taxes in Canada: The GST-HST-QST-RST “System”’, Revision of paper presented at American Tax Policy Institute Conference on Structuring a Federal VAT: Design and Coordination Issues, Washington, DC, 18–19 Feb. 2009, SSRN Working Paper Series, <http://ssrn.com/abstract=1413333>, (accessed on 7 Jul. 2009). Revenue shares are from authors’ calculations on the basis of data from Karin Treff & Deborah Ort, Finances of the Nation 2008 (Toronto: Canadian Tax Foundation, 2009), Ch. 5 and Appendix A. Tax rates shown are current as of July 2009. Yields for British Columbia and Ontario are based on existing Retail Sales Taxes (RSTs). As discussed infra, the base of the Quebec Sales Tax (QST or TVQ, Taxe de vente du Quebec) differs slightly from that of the GST. The QST rate will rise to 8% effective 1 Jan. 2011. Although the base of the provincial HSTs is the same as that of the GST, each province can alter the effective base by rebating its tax on certain goods, services, or transactions, or by placing restrictions on Input Tax Credits (ITCs) such as in British Columbia and Ontario. Each RST province has its own tax base, generally with considerable taxation of business inputs and with limited coverage of services. These taxes are not coordinated in any way with each other or with the federal GST and are not discussed further in this chapter as they are not value-added taxes.

10. Again, the source of the discrepancy lies in the design of the GST/HST rebate system and in restrictions placed on ITCs for large businesses. The rebate system is a means of providing relief for GST/HST paid on purchases by registrants in the course of providing exempt supplies. ITC restrictions are meant to control revenues and are intended to be temporary in both British Columbia and Ontario.

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Table 3.1. Sales Taxes in Canada, 2009

<table>
<thead>
<tr>
<th>Jurisdiction</th>
<th>Name of Tax</th>
<th>Type</th>
<th>Rate (%)</th>
<th>Yield of total taxes (%)</th>
<th>Administration</th>
</tr>
</thead>
<tbody>
<tr>
<td>Canada</td>
<td>GST</td>
<td>VAT</td>
<td>5</td>
<td>18.1</td>
<td>Federally administered, except provincially in Quebec</td>
</tr>
<tr>
<td>Newfoundland &amp; Labrador</td>
<td>HST</td>
<td>VAT</td>
<td>8</td>
<td>25.2</td>
<td>Federal</td>
</tr>
<tr>
<td>Nova Scotia</td>
<td>HST</td>
<td>VAT</td>
<td>8</td>
<td>23.5</td>
<td>Federal</td>
</tr>
<tr>
<td>New Brunswick</td>
<td>HST</td>
<td>VAT</td>
<td>8</td>
<td>23.0</td>
<td>Federal</td>
</tr>
<tr>
<td>Prince Edward Island</td>
<td>PST</td>
<td>RST</td>
<td>10</td>
<td>26.7</td>
<td>Provincial</td>
</tr>
<tr>
<td>Quebec</td>
<td>QST/TVQ</td>
<td>VAT</td>
<td>7.5</td>
<td>16.6</td>
<td>Provincial</td>
</tr>
<tr>
<td>Ontario</td>
<td>HST</td>
<td>VAT</td>
<td>8</td>
<td>n/a</td>
<td>Federal</td>
</tr>
<tr>
<td>Manitoba</td>
<td>PST</td>
<td>RST</td>
<td>7</td>
<td>23.0</td>
<td>Provincial</td>
</tr>
<tr>
<td>Saskatchewan</td>
<td>PST</td>
<td>RST</td>
<td>5</td>
<td>15.9</td>
<td>Provincial</td>
</tr>
<tr>
<td>British Columbia</td>
<td>HST</td>
<td>VAT</td>
<td>7</td>
<td>n/a</td>
<td>Federal</td>
</tr>
</tbody>
</table>
Businesses that are registered for GST/HST are required to collect GST/HST on their supplies and are generally entitled to claim input tax credits (ITCs) for GST/HST incurred on purchases in the course of commercial activities. The general registration threshold is met when taxable supplies equal or exceed CAD 30,000 per year. Small businesses with taxable supplies falling below the threshold are not required to register and hence do not charge GST/HST on their supplies. As a consequence, small suppliers are also not entitled to claim ITCs. To avoid this disadvantage, small businesses may choose to register voluntarily, entitling them to claim ITCs and requiring them to charge and collect GST/HST.\textsuperscript{11}

Although most supplies of goods and services are taxable, many types of supplies are exempt, while others (aside from exports) are zero-rated. Special treatment is extended in a number of cases to particular goods or services and even to entire sectors. The three most notable sectors that receive special treatment are (1) the financial services industry; (2) the MASH sector;\textsuperscript{12} and (3) the real property sector.

The GST/HST is a comprehensive and complex VAT. Among federal statutes, the *Excise Tax Act* is rivalled only by the *Income Tax Act* in its impenetrability and opacity. Because the GST/HST system is so complex, it should go without saying there is no substitute for consulting the *Excise Tax Act* and its regulations for definitive guidance. With this caution out of the way, the following section strives to outline in general terms the application of the GST/HST system to real property transactions.

### 3.2.1.2 Treatment of Real Property under the GST/HST System

The real property sector is granted special treatment in the GST/HST system. In fact, the application of the GST/HST to real property receives more extensive statutory coverage than any other type of transaction. In part, carving out real property transactions for this special treatment is demanded by the conceptual distinctions raised by real property and the difficulties with applying VAT to real property transactions in an economically neutral way.\textsuperscript{13} In part, it is a result


\textsuperscript{12} ‘MASH’ is an acronym for ‘Municipalities, Academic institutions, Schools, and Hospitals.’ Generally the term is used to refer to public service bodies (government, non-profit organizations, and charitable organizations).

\textsuperscript{13} The theory underlying these complications is not specific to Canada. They are well-documented elsewhere. See, for example, Robert F. van Brederode (this volume) & Satya Poddar, ‘Treatment of Housing under VAT for the US’, Revision of paper presented at American Tax Policy Institute Conference on Structuring a Federal VAT: Design and Coordination Issues, Washington, DC, 18–19 Feb. 2009, <www.americantaxpolicyinstitute.org/pdf/VAT/Poddar.pdf> (accessed on 22 Dec. 2009); Richard M. Bird & Pierre-Pascal Gendron, *The VAT in Developing and Transitional Countries* (New York: Cambridge University Press, 2007), Ch. 6; Richard Krever & David White (eds), *GST in Retrospect and Prospect*
of political pressures and resistance to imposing levies on human needs regarded as necessities, including residential real property. We largely set aside both sets of policy concerns in this section, and focus on briefly describing the contours of the design issues relating to the treatment of the real property sector in the GST/HST system.

For the purposes of the GST/HST, ‘real property’ includes all types of land and buildings and every estate or interest in real property, whether legal or equitable. In addition, mobile homes, floating homes and any leasehold or proprietary interest are also considered to be real property. Real property is also defined to include an option to acquire real property. Commercial real property is a subset of real property that is defined residually and understood as including all real property that is not residential real property. Residential real property includes detached, semi-detached, and row houses, residential condominium units, apartments, mobile homes and floating homes. Suites or rooms in hotels, motels, inns, boarding houses, student and senior residences, and any other similar premises are also considered residential real property provided that all or substantially all (normally considered by the CRA to be 90% or more) of the relevant units are occupied continuously by the same individuals for periods of at least sixty days. Surrounding land is included as residential real property to the extent that it is reasonably necessary for the use and enjoyment as a residence of a residential building. In mixed-use building settings, that part of the property that is used as a residence (or reasonably necessary for the use and enjoyment of the property as a residence, such as parking spaces, and storage lockers) is also considered to be residential real property.

As a starting point, generally all real property transactions in Canada involving the transfer, exchange, or sale of interests are prima facie subject to...

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14. Although mobile homes are specifically included, yachts and houseboats are not. The term ‘mobile home’ is defined in subs. 123(1) as a building that has complete plumbing, electrical and heating facilities, and is intended to be installed on a foundation. The definition excludes travel trailers, motor homes and camping trailers intended for recreational use.

15. The term ‘floating home’ is defined in subs. 123(1) as a floating platform and an associated building that is permanently attached to the platform and intended for use as a residence for individuals. A floating home does not include any freestanding appliances or furniture sold with the structure according to the definition, and specifically excluded as well are any structures that are capable of being readily adapted for self-propulsion.

16. According to subs. 123(1) of the federal Excise Tax Act (ETA), for the purposes of the GST/HST, ‘real property’ includes, in the province of Québec, all immovable property and every lease of immovable property. In the rest of Canada, ‘real property’ includes all messuages, lands and tenements, and every estate or interest in real property, whether legal or equitable. Throughout all of Canada (i.e., both inside and outside Québec), ‘real property’ includes mobile homes, floating homes and any leasehold or proprietary interest of a floating home or a mobile home. See also, Canada Revenue Agency, Chapter 19-1 Real Property and the GST/HST, GST/HST Memoranda Series, s. 19-1, (Ottawa: Government of Canada, 1997), 2, <www.cra-arc.gc.ca/E/pub/gm/19-1/19-1-e.pdf>, (accessed 17 Jul. 2009).
GST/HST; that is, GST/HST applies unless the transaction is specifically
exempted from tax. The most important categories of real property transactions
ordinarily regarded as taxable supplies are: (1) sales of commercial-use real
property; (2) leases of commercial-use real property; (3) sales of new residential
real property; and (4) sales of ‘substantially renovated’ used residential real
property.

The word ‘generally’ in the first sentence of the preceding paragraph is impor-
tant, since the system encompasses many exceptions to taxable and exempt status,
contains various deeming rules, and addresses a large number of special situations.
Even though there are a dozen statutory exemptions, many depend on the satis-
faction of numerous detailed conditions and criteria. In fact, the complexity of the
system is such that the CRA has issued detailed and technical administrative
guidance concerning the real property sector. This guidance alone is well over
300 pages in length. Despite the complexity of the details of the system, it is
capable of reasonably clear general description. Table 3.2 presents a brief summary
of the applicable tax treatment.

The most important exceptions from the imposition of GST/HST on real
property transactions involve the sale and lease of used residential real property.
Other exceptions to the taxable treatment of real property include: (1) sale of
farmland by an individual to a related individual where the farmland was only
used in a commercial activity that is the business of farming and the related indi-
vidual is purchasing the farmland for personal use and enjoyment; and (2) sales of
vacant land by individuals. Although the Excise Tax Act and the regulations as
well as the documents and publications of the CRA are silent with respect to
imputed rents associated with owner-occupied housing, these are also exempt.

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17. The extension of the right to use or enjoy real property is considered to be a taxable supply,
regardless of whether the right to use or enjoy real property results from the outright sale of an
interest in real property or by a ‘lease, license or similar arrangement.’ A ‘sale’ of real property
is defined in the ETA as including ‘any transfer of the ownership of the property and a transfer of
the possession of the property under an agreement to transfer ownership of the property.’
The term ‘any transfer of the ownership’ is very broad and can encompass gifts, barter transac-
tions, and also more conventional sales transactions. The phrase, ‘lease, license or similar
arrangement’ is more mysterious, since these terms are left undefined in the legislation. Resort
must therefore be had to the general principles of the common and civil law.

18. In this context, ‘commercial’ means non-residential.

19. The meaning of the term ‘substantially renovated’ is considered in more detail below.


21. Canada Revenue Agency, Special Sectors: Real Property, GST/HST Memoranda Series
(Ottawa: Government of Canada), 19, <www.cra-arc.gc.ca/menu/GTMS_19-e.html>,

22. This set-up closely follows the organization of the text in Joanne Heffernan, GST/HST and Real

23. Canada Revenue Agency, Sales of Vacant Land by Individuals, GST/HST Info Sheet (Ottawa:
17 Jul. 2009).
This exemption for imputed rents is in keeping with the traditional focus of Canadian tax law on legal form and substance, rather than on economic substance. In general, all supplies of real property (including both sales and leases of real property) by public service bodies such as non-profit organizations, charities, municipalities, school authorities, hospital authorities, and public colleges or universities, are exempt supplies. This is part of a wider special treatment for public service bodies under the GST/HST.

The GST/HST treatment of real property reflects several important special rules and policy measures that are specific to the sector. The third column of Table 3.2 indicates the most notable of those measures that depart from taxable or exempt treatment, as applicable.

Sales of commercial real property are straightforward since in general everything is taxable and businesses can claim full ITCs for the GST/HST paid on

<table>
<thead>
<tr>
<th>Table 3.2. GST/HST Treatment of Real Property</th>
<th>Taxable</th>
<th>Exempt</th>
<th>Note</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales of new and used commercial real property</td>
<td>✓</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td>Sales of new residential housing</td>
<td>✓</td>
<td></td>
<td>Subject to new housing rebate and new residential rental property rebate</td>
</tr>
<tr>
<td>Sales of previously-occupied residential real property</td>
<td>✓</td>
<td>✓</td>
<td></td>
</tr>
<tr>
<td>Leases of commercial real property</td>
<td>✓</td>
<td></td>
<td>Public service bodies are exempt</td>
</tr>
<tr>
<td>Leases of residential real property</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Self-supply of commercial real property</td>
<td>✓</td>
<td></td>
<td>Public service bodies are exempt</td>
</tr>
<tr>
<td>Self-supply of residential real property for lease</td>
<td>✓</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Self-supply of residential real property for personal use</td>
<td>✓</td>
<td>✓</td>
<td></td>
</tr>
</tbody>
</table>

25. The list is not meant to be exhaustive. The full list of special rules and measures are found throughout Canada Revenue Agency, n. 21 supra.
26. Sources: Authors’ compilation based on organization of text in Joanne Heffernan, n. 22 supra.
purchases made in the course of their commercial activities. Leases\textsuperscript{27} of commercial real property are fully taxable regardless of whether the property is new or used. The self-supply of new commercial real property through development activities typically triggers GST/HST liability on the fair market value of the self-supplied real property at the time that the property is ‘substantially completed’. This treatment results regardless of whether the commercial real property is going to be used by the developer directly, or leased to others for their commercial-use. The development of commercial real property by public service bodies can present challenges for GST/HST because the supplies made by such bodies are generally exempt, although they give rise to a partial (in most cases) rebate of GST/HST paid. Such bodies can affect the size of their GST/HST liabilities by the choice of contractual arrangements.\textsuperscript{28}

The development of new residential real property, including houses, condominiums, and apartments, is generally a taxable activity. Special rules have been implemented to treat businesses that purchase and substantially renovate used residential buildings for subsequent resale or lease similarly to new home builders. ‘Substantially renovated’ buildings are treated like new residential real property, so in both cases, the business that carries out the renovations charges GST/HST on the full sale price and claims ITCs (the issue of what constitutes a ‘substantial renovation’ has caused considerable controversy in the courts, as discussed below). Residential real properties undergoing non-substantial renovations are accorded exempt treatment since the threshold of ‘substantial renovation’ is not met. The idea is that the activities that have been undertaken are not on par with home-building. The self-supply rules require a builder to self-assess GST/HST on the fair market value of new residential real property that is being rented, since the occupants will not pay GST/HST on rental payments. For example, suppose that a builder erects a multiple-unit residential complex for the purpose of leasing the units. The self-supply rule removes the tax advantage that would accrue to the builder in contrast to a situation where a landlord buys a new residential complex for the same purpose by subjecting the fair market value of the complex to GST/HST. Finally, conversions from commercial to residential use in the absence of renovation (substantial or not) trigger a variant on the self-supply

\textsuperscript{27} In the Canadian provinces aside from Québec, leases can be distinguished from licenses according to the general principles of the common law. Broadly speaking, a lease is a transferable right granting the exclusive use of land to the lessee. A leasehold right typically (though not always) survives the transfer of legal title to a third party. A license to use real property, on the other hand, is typically a non-exclusive right to use the land for a specific purpose that is a personal right that survives only as long as the licensor holds legal title to the property; a license is usually not transferable by the licensee without the consent of the licensor. The addition of the phrase ‘or similar arrangement’ is apparently intended as a gap-filling measure to capture hybrid or intermediate interests in real property that are difficult to classify as either leases or licenses, such as an easement. In Quebec, the distinction between leases and licenses turns on the relevant provisions of the Civil Code of Quebec [Code civil du Québec] (‘CCQ’).

\textsuperscript{28} Joanne Heffernan, n. 22 supra, 64.
Sales of used residential real property are usually considered exempt supplies. Although there are, naturally enough, transition issues, in the long-run it is assumed that whoever purchased the property from the builder would have paid the GST/HST on the purchase of the new residential property. Therefore, if the home is being purchased from a party that is not a builder, the purchase price is considered to indirectly include the historical burden of GST/HST and no additional GST/HST is payable. Also, a sale by a builder (subsequent to self-supply for lease, for example) is exempt. Consequently, if a builder erects a home for the purposes of earning rental income, the builder will be deemed to have self-supplied the property upon occupation by a tenant, and at this moment there will be a taxable self-supply. If the rental property is subsequently sold, there will be no further GST/HST payable; in the absence of this rule, double-taxation could potentially arise.

This leaves sales of new residential housing. Such transactions feature rebate schemes implemented to facilitate access to affordable housing. This is a major consideration for end-users of housing given the significance of housing expenditure in overall household expenditures. The relatively high price of housing in some Canadian cities such as Vancouver, Calgary, and Toronto makes this latter problem acute, though the design of the rebate system tends to cut at cross-purposes to these concerns by ignoring the local effects of differences in the cost of housing, as is clear from the design of the rebates. There are in fact two GST/HST rebate schemes that apply to new residential real property, as mentioned in Table 3.2, above: the New Housing Rebate, and the New Residential Rental Property Rebate.

The New Housing Rebate is a rebate available to individuals who have purchased a new residential unit from a builder or, alternatively, built or substantially renovated a residential unit themselves. The rebate allows for the recovery of part of the GST or the federal part of the HST that was paid on the purchase price or cost of building a new house. Houses located in Nova Scotia are entitled to an additional rebate for the provincial portion of the HST. The house must be intended as the primary place of residence to qualify for the rebate. The programme covers the following: (1) new (or substantially renovated) residential real property (including mobile and floating homes); (2) new housing purchased from builders that has been constructed on leased land; (3) co-operative housing; (4) owner-built

31. This is addressed in more detail, below.
32. See subs. 254(2) of the Act.
33. See subs. 254.1(2) of the Act.
34. See subs. 255(2) of the Act.
homes; and, (5) land transferred by an owner or lessee pursuant to a lease for residential purposes. If an individual is purchasing a residential real property as an investment property from the builder, the purchase is not eligible for the New Housing Rebate. The New Housing Rebate must be applied for within two years of the transaction entitling the owner to the rebate.

Residential real property (including the building, land, and other structures) qualifies for the federal new housing rebate only if the real property's fair market value is below CAD 450,000, the purchaser is the first occupant, and the vendor paid GST/HST on the land or construction materials and services related to the construction or substantial renovation. The base of the rebate calculation incorporates the full value of the federal component of GST/HST paid on the house if the fair market of the house is CAD 350,000 or less. In that case, the rebate rate is 36% of the federal component of the GST/HST paid. For residential real property with fair market values between CAD 350,001 and CAD 449,999, the value of the rebate is decreased proportionally. The federal New Housing Rebate is phased-out entirely for a new residential real property with a fair market value of CAD 450,000 or more. Table 3.3 summarizes the key features of the rebates for residential real property and illustrates a key difference between the GST and HST: the treatment of the New Housing Rebate and the New Residential Property Rebate under the GST or federal portion of the HST versus the provincial portion of the HST. The rebate for the GST or the federal part of the HST is moderate in its amount. The recently harmonized provinces of Ontario and British Columbia are almost twice as generous in their rebates for the sale of new housing as the federal government with no rebate phase out. The rebate rate in the Province of Nova Scotia is about one half as generous as the GST rebate rate and is available only to first-time home buyers. There is no rebate in New Brunswick and Newfoundland and Labrador. The New Residential Rental Property Rebate works in a similar way and is generally subject to the same thresholds (applied at the single residential unit level). The difference is that it applies to the following types of residential real property: (1) new or substantially renovated residential rental property; (2) additions to multiple-unit residential complexes; (3) conversions of

35. See subs. 256(2) of the Act.
36. See subs. 256.1(1) of the Act.
37. See subs. 254(3) of the Act.
39. Refer to Table 3.1 for details.
Table 3.3. GST/HST Real Property Rebates in the HST Provinces

<table>
<thead>
<tr>
<th></th>
<th>New Brunswick, Newfoundland</th>
<th>Nova Scotia</th>
<th>Ontario</th>
<th>British Columbia</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>GST</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>New Housing Rebate</td>
<td>36%; max. rebate CAD 6,300</td>
<td>No rebate</td>
<td>18.75%; max. rebate CAD 1,500</td>
<td>71.43%; max. rebate of CAD 26,250</td>
</tr>
<tr>
<td>New Residential Rental Property Rebate</td>
<td>36%; max. rebate CAD 6,300</td>
<td>No rebate</td>
<td>No rebate</td>
<td>71.43%; max. rebate of CAD 26,250</td>
</tr>
</tbody>
</table>

41. Note that the rebate is only available to first-time home buyers, and is gradually reduced for homes valued between CAD 350,000 and CAD 450,000. The rebate is fully phased out for homes valued at CAD 450,000 or more. This table is adapted from one appearing in Richard M. Bird & Pierre-Pascal Gendron, n. 6 supra.
commercial properties into residential rental properties; and, (4) land that is leased for residential purposes.

It is important to note that registrants (both businesses and public service bodies) face restrictions in obtaining ITCs for GST/HST paid on capital commercial real property (in contrast with real property held as inventory, such as by a land developer looking to resell real property as a business, including as ‘an adventure or concern in the nature of trade’). The restrictions related to capital real property are based on the proportion of the real property (typically assessed and measured by the area of floor space) that is devoted to commercial activities (but not including exempt supplies of any kind).\footnote{It should be noted that the term ‘commercial activities’ does include only those activities that are considered to be taxable supplies (i.e., exempt supplies are not considered to be commercial activities). The term is also broad enough to include any taxable supply of real property. See Heffernan, n. 22 supra, at 3 for a description of the applicable definition of commercial activity.} Table 3.4 summarizes those restrictions.

A supply of real property that consists of residential and non-residential real property is treated as two separate supplies. The legislation does not provide allocation methods to deal with specific mixed use situations. It is required that

<table>
<thead>
<tr>
<th>Proportion of Use (x) in Commercial Activities</th>
<th>Partnerships and Corporations</th>
<th>Individuals</th>
<th>Public Service Bodies</th>
<th>Financial Institutions</th>
</tr>
</thead>
<tbody>
<tr>
<td>x ≤ 10%</td>
<td>None</td>
<td>None</td>
<td>None</td>
<td>Actual % of use</td>
</tr>
<tr>
<td>10% &lt; x ≤ 50%</td>
<td>Actual % of use</td>
<td>Actual % of use</td>
<td>None</td>
<td>Actual % of use</td>
</tr>
<tr>
<td>50% &lt; x ≤ 90%</td>
<td>Actual % of use</td>
<td>Actual % of use</td>
<td>100%</td>
<td>Actual % of use</td>
</tr>
<tr>
<td>x ≥ 90%</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
<td>Actual % of use</td>
</tr>
</tbody>
</table>

\footnote{Notes: Individuals cannot claim an ITC if the property is used more than 50% for their personal use or that of a related individual. Those numbers apply where the body has not made an election to have the change in use rules for corporations apply and to treat its property as taxable real property. See Canada Revenue Agency, \textit{General Information for GST/HST Registrants} (Ottawa: Government of Canada, 2008), 46, <www.cra-arc.gc.ca/E/pub/gp/rc4022/rc4022-08e.pdf>, (accessed 17 Jul. 2009).}
methods actually used be fair, reasonable, and consistent in their application.\textsuperscript{44} In practice, floor space is a simple and attractive allocator to calculate actual use. It is also used in calculations of office use of home, under the income tax.

The treatment of public service bodies differs from the treatment accorded to other registrants in that there is a bright-line rule of ‘primary use’ of real property. Where the real property is primarily used for commercial activities, there is 100\% entitlement to claim ITCs. When the real property is less than 50\% used for commercial activities, the treatment of a public service body is harsh in that no ITCs may be claimed at all. These restrictions and the associated rules (e.g., the special treatment of public service bodies and GST/HST rebate system that applies to it\textsuperscript{45}) add substantial complexity to the GST/HST system. In addition, the concessions built into the system result in different effective tax rates depending on the nature and location of transactions, while the GST/HST system is presented to the public as based on a single rate of 5\% (or 13\% in the HST participating provinces, except for British Columbia where the blended rate is 12\%).

Where there has been a change in use from primarily non-commercial activities to primarily commercial activities by real property of a public service body, the public service body can claim full ITCs relating to the property at that time. Conversely, when the real property of a public service body changes from primarily commercial to primarily non-commercial, the public service body must self-assess and remit GST/HST on the deemed disposition of the real property at that time.\textsuperscript{46}

The change of use rules that apply to public service bodies are similar to those that apply when real property changes in use from a commercial real property to a residential real property. In these circumstances, the conversion is deemed to be a taxable supply, even where the property has not been sold or transferred and there has been no substantial renovation.\textsuperscript{47} As noted earlier, the special treatment accorded to public service bodies is part of a wider special treatment for public service bodies as a whole. A more complete discussion of that overall special treatment lies beyond the scope of this chapter.

3.2.2 Frequently Litigated Legal Issues

There are two sources of law governing the GST/HST system in Canada. The first important source of law is the \textit{Excise Tax Act} and the associated regulations.\textsuperscript{48}

\textsuperscript{44} Heffernan, n. 22 \textit{supra}, at 114–115.
\textsuperscript{46} Heffernan, n. 22 \textit{supra}.
\textsuperscript{47} \textit{Ibid.}, at 52–53.
\textsuperscript{48} Many of the most important provisions of the \textit{Excise Tax Act} and the regulations have been referred to in the footnotes to Part II.1 in the text above.
The second relates to the accumulated body of case law interpreting and applying the governing GST/HST legislation and regulations. This section reports on the GST/HST issues surrounding transactions in real property that have frequently been litigated, principally at the Tax Court of Canada.\(^\text{49}\)

Although there are literally scores of cases that have been litigated through to final disposition involving GST/HST in the past twenty years, many of these disputes are heavily fact-specific and do not turn on or raise important legal questions that are left unanswered or unresolved in the *Excise Tax Act* and the regulations. While there are many cases that raise these kinds of fairly isolated issues, a survey of the case law reveals that there are also three clusters of legal issues in which litigation has been frequent.

These three clusters of cases comprise: (1) disputes surrounding the acceptable methods for arriving at fair market valuations of real property for GST/HST purposes – an important issue for determining liability for GST/HST under the self-supply rules; (2) disputes surrounding whether a particular renovation of a previously-occupied residential property constitutes a ‘substantial renovation’ – an important question for determining whether the renovations trigger treatment on resale as a new taxable supply of real property and/or are eligible for the New Housing Rebate; and, finally, (3) cases relating to the coordination of collecting and remitting GST/HST on sales of real property. These three clusters of cases are described in order.

The details surrounding the cases dealing with fair market valuation tend to pit differing valuation methodologies against each other and can be quite fact-specific. A nice example of this type of situation is the case of *Marall Homes Ltd v. Canada*.\(^\text{50}\) The taxpayer had claimed a fair market value of CAD 5.81 million for a new building that it had constructed itself for the purposes of paying GST/HST on it as a taxable self-supply. The tax authorities rejected the CAD 5.81 million valuation by the taxpayer and asserted that it was worth CAD 7.96 million. The taxpayer’s expert had based his valuation of CAD 5.81 million using two methods – an ‘income’ method and a ‘comparison’ method. The income method calculated the net present value of the net income that the property could generate based on expected rental rates and expected expenses. The comparison method looked to the prevailing market prices for sales of similar properties. In arriving at his estimate of CAD 7.96 million, the expert for the tax authorities used a ‘comparison’ approach and a ‘cost’ approach. While the comparison approach was similar to the one used by the taxpayer’s expert, the expert for the tax authorities made assumptions that yielded a higher estimate. The cost approach looked to the estimated cost of replacing the building and buying similar land, and also yielded a

\(^{49}\) Some of the cases discussed in this section were decided at the Federal Court of Appeal, which has appellate jurisdiction over the Tax Court of Canada. Other cases discussed were decided by courts of general jurisdiction, typically referred to as ‘superior courts.’ The cases that are referred to that were decided by superior courts involve private law disputes between taxpayers that arise out of the VAT consequences of real property transactions.

higher estimate. Without endorsing or criticizing any of the valuation methods, the Tax Court of Canada held that neither of the valuations was entirely persuasive, but found overall that a valuation of CAD 6.08 million – closer to the taxpayer’s claimed value that that of the tax authorities – was the most plausible on the basis of the evidence.\footnote{Ibid., at para. 19.} The Marall Homes decision is not alone in not attending to the basis of various methodologies in reaching a conclusion. For example, in \textit{Pinelli v. Canada},\footnote{1998 GTC 2192 (TCC).} the Tax Court of Canada simply found that the taxpayer’s valuation of CAD 600,000 was ‘fair and equitable’ and favoured it over the value CAD 710,000 asserted by the tax authorities.

In \textit{Sira Enterprises Ltd v. Canada},\footnote{[2000] T.C.J. No. 804 (TCC).} however, the valuation methodologies were directly at issue. The taxpayer argued that the cost method was the best method for valuing six new low-rise apartment buildings it completed building in 1995 in Moncton, New Brunswick, since the actual cost of constructing the property should not depart dramatically from its fair market value when it is first occupied. The tax authorities, in response, contended instead that the income and comparison methods should be preferred and that the cost method should be rejected. The Tax Court of Canada sided with the taxpayer, subject to some specific adjustments in some of the construction costs to reflect arm’s-length pricing. The court did not reject the income and comparison methods, but found that the cost method was a reasonable and most accurate method in the circumstances, in large part because there were no closely comparable properties nearby.\footnote{Ibid., at para. 82.}

In \textit{9103-9438 Quebec Inc. v. The Queen},\footnote{2005 GTC 940 (TCC).} the Tax Court of Canada considered the aforementioned judgments and other decisions relating to the methodologies used to value real property in remarking:

> When determining a building’s market value, the value must correspond to the definition of the fair market value. Also, the approach used to determine the fair market value must take into consideration the nature of the building. The decisions referred to above clearly establish that, when constructing a new building, the cost approach seems to be the most appropriate approach since a building’s fair market value does not normally exceed its cost.\footnote{Ibid., at para. 33.}

In more recent cases, however, it has been recognized that there can be significant limitations to the cost method, as well.

In \textit{Quereshi v. The Queen}\footnote{2006 GTC 506 (TCC).} the taxpayer built a house in Listowel, Ontario, for her own personal use. The taxpayer claimed the New Housing Rebate on the fair market value of the self-supplied house. The tax authorities claimed that because the construction cost of the property was CAD 497,000 (i.e., in excess of the CAD 450,000 limit), the taxpayer was ineligible to claim the New Housing Rebate.
The Tax Court of Canada held that in light of the relatively low property prices in the Listowel area, the cost method significantly overstated the fair market value of the property. According to the court, the following is observed:

There is simply no justification for using cost or replacement cost as a measure of valuing when there is a market in which comparables are available. Cost [does] not indicate [fair market value] where we are dealing with a home that is being constructed to a homeowner’s specifications. If one buys a fully constructed house in the open market the price paid will generally be an indication of [fair market value].

The court elaborated in conclusion, stating the following:

The emphasis is of course on the market. If there is a market it is to that market that one must turn. The comparables used by the respondent’s expert to rationalize and bolster a [fair market value] that is close to cost do not have the effect of supporting a realistic [fair market value] of [CAD] $500,000 in the market as it existed in Listowel at that time.

It thus now appears that a reasonable reading of the results of the case law suggests that the preferred methodology is that of comparison or comparables approach, where directly or closely comparable properties are available. When there are no comparable properties available, then the cost method will be taken to be a reasonably reliable indicator of value, insofar as the building is new and there have not been delays, cost overruns, or other anomalies in construction. Lastly, an income approach might also be used to supplement the other two valuation methods, but it is the most sensitive to the assumptions made in formulating the valuation and likely to be the least reliable of the three methods.

Consider now the second cluster of litigated cases involving GST/HST. When ‘substantial renovations’ are made to previously-occupied residential property, the property is treated for GST/HST purposes as having been newly constructed and, hence, as a taxable supply, since it is regarded as being a close substitute for a newly built residential property. The issue of whether certain renovations constitute a ‘substantial renovation’ within the meaning of the Excise Tax Act has been litigated on numerous occasions.

Where a renovation falls short of a ‘substantial renovation’, it may nevertheless be considered to fall within a special self-supply rule when the property that is improved is used in the course of a business of making taxable supplies of

58. Ibid., at para. 10.
59. Ibid., at para. 17.
60. Subsection 123(1) defines ‘substantial renovation’ as ‘the renovation or alteration of a building to such an extent that all or substantially all of the building that existed immediately before the renovation or alteration was begun, other than the foundation, external walls, interior supporting walls, floors, roof and staircases, has been removed or replaced where, after completion of the renovation or alteration, the building is, or forms part of, a residential complex.’
61. Many, though not all, of these cases are discussed in the following text.
residential property for resale or for lease. The base on which GST/HST in these circumstances is payable is the amount by which the capital value of the improvements (as determined by the amount that would be the increase to the adjusted cost base of the property for income tax purposes if it were held as capital property rather than inventory) exceeds the proportion of the costs that have borne GST/HST.

It will often be advantageous for taxpayers to seek to avoid characterization of certain renovation activities as a 'substantial renovation'. For example, if renovation work is done to a previously-occupied residential housing by a builder, depending on the relationship between the cost of the renovations and the expected proceeds of resale, he or she may want to avoid having the work characterized as a 'substantial renovation'. An example of a builder seeking to avoid characterization of certain renovations is the case of Seabrook Investments Ltd v. Canada. In this case, the taxpayer was in the business of buying, renovating, and reselling residential properties. While the facts of the case are not entirely straightforward, one of the central issues related to the characterization of the taxpayer’s purchase of a five unit apartment building in Vancouver. Before marketing any of the units, the taxpayer refurbished and renovated the existing previously-occupied units, and added two new units to the basement of the building. The taxpayer subsequently sold the seven units individually for a significant return on the original purchase price and did not claim or remit GST on any of the seven sales, although the taxpayer did claim ITCs on the materials. The CRA reassessed the taxpayer on the basis that two of the seven units were newly constructed and that the remaining five had been ‘substantially renovated’, requiring GST to be payable on the full purchase price received by the taxpayer on the sale of the units. The Tax Court of Canada agreed, holding that the two new basement units were new residential units, and that the five renovated apartments had been subject to ‘substantial renovation’ within the meaning of the Excise Tax Act and therefore that the full purchase price of all seven units should be considered to be taxable supplies.

A second illustration of an attempt to avoid characterization as a ‘substantial renovation’ recently arose in 1096288 Ontario Ltd v. Canada. In 1096288, the taxpayer was a developer that had removed and relocated eleven previously-occupied houses from other land it was developing onto new residential building lots. The relocations occurred between 1 September 2000 and 30 November 2004. Before the houses were relocated, the new residential building lots were prepared for the relocation of the existing houses by installation of new foundations, new driveways, new water supplies, and septic systems. The existing houses were then transported from their original foundations to the new foundations and the new residential lots were sold. The developer treated the relocation of

62. Section 192.
63. Paragraph 192(a).
64. 2001 GTC 422 (TCC).
65. Ibid., at paras 18–20.
66. 2009 TCC 292 (TCC) [‘1096288’].
the houses as an exempt supply on the basis that the activities involved in moving
the buildings did not constitute a ‘substantial renovation’ and that the relocation
and reinstallation activities did not make the developer a ‘builder’ with respect to
the new residential lots with the relocated dwellings upon resale. The tax author-
ities objected, claiming first that the developer was a ‘builder’ of a new residential
complex and in the alternative that the developer should be denied exempt supply
treatment because the developer claimed ITCs with respect to the cost of the new
residential lots and the preparatory work that had been done.67 The Tax Court of
Canada held that although the taxpayer was correct that the relocation of the houses
did not result in a ‘substantial renovation’, the relocation did result in the taxable
supply of new residential complexes.

A third example of taxpayers seeking to avoid meeting the threshold of work
being a ‘substantial renovation’ is Sviros et al. v. The Queen.68 In this case, the
taxpayers (members of a partnership) bought a previously-occupied residence for
CAD 270,000 with the intention of fixing it up and reselling it at a gain. The taxpayers
sold the home fourteen months later for CAD 475,000 after having incurred estimated costs in labour and materials of CAD 105,000. They had done
considerable work to the house, including replacing all plumbing and electrical
wiring, installing new drywall and new flooring throughout, adding new kitchen
ceilings and countertops, replacing staircases, etc. Despite this, the Tax Court of
Canada found that the renovation was not a ‘substantial renovation’, observing the
following:

The total renovation would replace all of the building that existed immediately
before the renovation or alteration was begun, other than the foundation,
external walls, interior supporting walls, the roof and staircases. By what
amount then did the Appellants’ work fall short of that? They did not replace
the outside doors. They did not replace some of the windows. The exact
number of windows in the house is not known, and there is an invoice for
two windows, but the Appellant stated that there were new windows through-
out the house. They did not replace the framing of the partition walls. They did
do not replace the furnace. They did not replace the ductwork. They apparently
did not replace the ceilings.69

It is quite difficult to reconcile this judgment in this case with the judgment in
Seabrook Investments, which had held that less intensive renovations of five apart-
ment units had met the definition of ‘substantial renovation’. It is also difficult to
reconcile with several other cases, discussed next.

It is not surprising that the tax authorities and taxpayers will have often
diverging views on whether it is desirable to characterize a given renovation as
‘substantial’ depending on the underlying facts and the tax obligations associated

67. The developer asserted that the ITCs were claimed in error and that this should not affect the
outcome of the appeal.
68. 2008 GTC 456 (TCC).
69. Ibid., at paras 71–74 (paragraph breaks removed from original).

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with each characterization. The tax consequences of a ‘substantial renovation’ can in fact sometimes advantage the taxpayer. If a renovation has been undertaken by a homeowner for personal use, it will not usually be considered a taxable supply, and ITCs will not be claimable. On the other hand, despite not being a taxable supply, if it is extensive enough to be a ‘substantial renovation’ the taxpayer may be eligible to claim the New Housing Rebate.

Claims that renovations amount to ‘substantial renovations’ and so should entitle the owner to a New Housing Rebate have been frequently contested by the tax authorities. For example, in *Warnock v. The Queen*,70 the taxpayer applied for the New Housing Rebate after adding 1,000 square feet of living space to an existing house of 1,200 square feet, replacing the roof, gutting and replacing a bedroom, and adding a bathroom in the basement of the home. The Tax Court of Canada agreed with the tax authorities in denying the taxpayer’s claim that this constituted a ‘substantial renovation’, explaining that ‘it cannot even be said that a majority of the house has been removed or replaced’.71

Similarly, in *McLean v. The Queen*,72 the taxpayers claimed the New Housing Rebate after on the basis that they had ‘substantially renovated’ the house, after renovating about 50% of an existing home of 2,515 square feet and adding 916 square feet of new living space. In denying the claim that this constituted a ‘substantial renovation’ within the meaning of the *Excise Tax Act*, the Tax Court of Canada explained the following:

> The definition of substantial renovation is restrictive. Firstly, it has no reference to the total costs of the renovation in relation to the value of the home. Secondly, renovations or alterations to the foundation, external walls, interior supporting walls, floors, roof and staircases are not taken into account. Thirdly, it appears that additions are not to be considered. The only items that are considered are the renovations or alterations of ‘the building that existed immediately before the renovation or alteration was begun’.73

These cases are representative of the cases that have been brought by taxpayers seeking to bring their activities within the definition of ‘substantial renovation’. Similar rejections of claims by taxpayers that houses were ‘substantially renovated’ have occurred in a number of cases. In *Erickson v. The Queen*74 the taxpayer had built a lateral addition of 960 square feet on an existing house of 1,060 square feet; the claim for the New Housing Rebate was denied.75
In *King v. M.N.R.*\(^{76}\) the Tax Court of Canada held that although the taxpayer had built a new two car garage, repaired windows, painted walls, installed new kitchen cupboards, new flooring, and new trim, extended the kitchen, and finished the attic, that these activities cumulatively did not amount to a ‘substantial renovation’.\(^{77}\) In *Camiré v. The Queen*\(^{78}\), the taxpayer unsuccessfully applied for the New Housing Rebate after transforming her summer cottage into a winterized home in renovating a bathroom, resurfacing kitchen countertops, making some modifications to electrical wiring and plumbing, replacing doors and windows, and adding some closets; in rejecting the claim, the court stated that the ‘rebate sought is very restrictive’.\(^{79}\) Other cases have recently rejected related claims for similar reasons: see *Colosimo v. Canada*,\(^{80}\) *Bellefleur v. Canada*,\(^{81}\) *Harrison v. The Queen*,\(^{82}\) and *Lemieux v. Canada*.\(^{83}\)

Other cases, on the other hand, have found in favour of taxpayers contending that a given renovation was a ‘substantial renovation’. For example, in *Lair v. The Queen*\(^{84}\) the taxpayer modernized a 100-year old personal residence by raising the home off of the concrete blocks supporting it and having a basement dug and foundation installed containing a family room, bathroom, laundry room, and a sewing and crafts room. When the house was raised, there was considerable cracking and buckling of the interior of the house, which the taxpayer subsequently repaired. The tax authorities denied the taxpayer’s claim for the New Housing Rebate on the basis that the renovation was not a ‘substantial renovation’ because not all or substantially all (>90%) of the building had been renovated. The Tax Court of Canada rejected this and agreed with the taxpayer that the renovation had been substantial, noting the following:

> The work carried on was ‘substantial’ in the true sense of the word. I do not think measuring different parts of the residence and comparing the measures, i.e. parts of the residence that incurred the construction and those which did not, or comparing costs and any increase in value of the residence as a result of the construction, is of any assistance in this particular case. On the facts then before me if a reasonable and neutral observer of the building, before and after

\(^{76}\) 2006 GTC 429 (TCC).
\(^{77}\) Ibid., at para. 10.
\(^{78}\) 2008 GTC 411 (TCC).
\(^{79}\) Ibid., at para. 12.
\(^{80}\) 2005 GTC 999-121 (TCC).
\(^{81}\) 2006 GTC 388 (TCC).
\(^{82}\) 2008 GTC 500 (TCC).
\(^{84}\) 2004 GTC 87 (TCC).
construction of the interior and exterior of the building, can conclude that the degree of renovation and alternation was substantial, the definition of ‘substantial renovation’ is satisfied. Mrs. Lair had an old house, ready to collapse, and for practical purposes rebuilt it as a new residence.\textsuperscript{85}

The Tax Court of Canada made the further point that, ‘[T]he Act provides no objective criteria by which to distinguish construction from that which is not construction. The point of distinction between the two is arbitrary, and it is a subjective determination that must be based on the facts in each case.’\textsuperscript{86}

A second example of a case decided in favour of a taxpayer with regard to whether a claim to the New Housing Rebate should be allowed after a renovation is \textit{Shotlander v. The Queen}.\textsuperscript{87} In this case, the issue was whether the taxpayer’s renovation to a condominium unit was a ‘substantial renovation’. Among other things, the taxpayer replaced the interior doors, drywall, walls, ceilings, refinished the floors, added new plumbing fixtures, replaced the kitchen cabinets, and painted the unit. The tax authorities claimed that only 49\% of the unit had been renovated and denied the taxpayer’s claim that the renovation was a ‘substantial renovation’. The Tax Court of Canada disagreed with the tax authorities, recognizing that the condominium’s rules and regulations prevented the taxpayer from making more substantial renovations and that more than 90\%, and hence ‘all or substantially all’ of the unit that could permissibly have been renovated had, in fact, been renovated. The court stated the following:

\begin{quote}
the assessment grid [of the tax authorities] is a very useful work tool for auditors, but the grid must be adapted to condominium complexes. The first elements considered in this assessment such as core plumbing, insulation, core electricity, core heating, exterior doors and windows, the basement floor and finishing on the heating system are not appropriate to assessing the percentage of renovations of a property that is a condo. These are common parts and a co-owner cannot touch them.\textsuperscript{88}
\end{quote}

For this reason, the court found in favour of the taxpayer’s claim that there was a ‘substantial renovation’ that could give rise to the New Housing Rebate.

The case law reviewed here shows that there are many uncertainties left surrounding the proper understanding, interpretation, and application of the term ‘substantial renovation’ in the GST/HST. Given how frequently residences are renovated, and given the subjectivity and lack of clarity on what constitutes a ‘substantial renovation’, this is an area that is surely to continue to give rise to more litigation in the future.

The third and final cluster of frequently litigated cases concerns issues relating to disputes surrounding the obligation to collect and remit GST/HST on the sale of real property. Unsurprisingly, the tax consequences can be significant for the

\begin{footnotesize}
\begin{itemize}
\item[85.] \textit{Ibid.}, at para. 14.
\item[86.] \textit{Ibid.}, at para. 16.
\item[87.] 2007 GTC 787 (TCC).
\item[88.] \textit{Ibid.}, at para. 12.
\end{itemize}
\end{footnotesize}
parties involved if there has been a mistake or confusion about the status of a particular sale as taxable or exempt; if the parties disagree over which of them has undertaken to remit GST/HST; or if there has been a simple failure to follow through with the payment of GST/HST and no misunderstanding. Because the tax consequences are so significant, such cases frequently result in litigation.

An early example of this arose in Franklin Estates Inc. v. Canada.\(^89\) In this case, both the purchaser and the vendor were GST registrants, and the property was not a residential complex sold to an individual. The vendor was therefore not required under the Excise Tax Act to collect and remit the GST. Instead the purchaser was responsible for remitting the GST directly to the Receiver General. Instead of remitting the GST payable on the transaction directly, the purchaser paid an amount equal to the GST liability to the vendor, with an undertaking from the vendor that the amount paid in respect of GST would be remitted to the Receiver General. The vendor did not in fact remit the GST. The purchaser was found liable for the GST that was not remitted on the basis that the vendor was not acting as an agent for the government when it received the GST, but rather as an agent for the purchaser. Because the purchaser’s agent did not remit the tax, the government could collect the unremitted GST directly from the purchaser. The Tax Court of Canada rejected the argument that this meant that the taxpayer was obligated to pay the GST twice,\(^90\) and suggested that the purchaser and vendor both understood that there was a strong possibility that the vendor would not be in a position to remit the GST in light of its fragile financial position.\(^91\)

In Leowski v. Canada,\(^92\) the purchaser entered into an agreement to buy vacant land from individuals and therefore at the time believed that the sale was an exempt supply. It turned out however that the apparent vendor was acting as a bare trustee for a commercial vendor, which made the sale a taxable supply. The taxpayer purchaser did not pay GST upon the purchase even though it was a taxable supply, and was found liable for the tax on the purchase price.\(^93\)

Similarly, in Rive v. Newtwon,\(^94\) the vendor insisted in negotiating a sale of land with the purchaser that the sale would be an exempt supply. The purchaser disputed this, and insisted on a clause in the agreement of purchase and sale of land that stated that the purchase price of USD 400,000 would include the GST if it turned out that the transaction was taxable. The purchaser did not initially pay GST on the transaction, but claimed ITCs with respect to the cost of the land. The tax authorities then pursued the purchaser for GST on the original purchase of the land. The purchaser paid the GST that was due and successfully sought indemnity from the vendor for the GST in a civil claim for indemnity under the agreement of purchase and sale.\(^95\)

\(^89\) (1994) 2 GTC 1063 (TCC).
\(^90\) Ibid., at paras 10–11.
\(^91\) Ibid., at para. 9.
\(^92\) (1996) 4 GTC 3151 (TCC).
\(^93\) Ibid., at para. 26.
\(^95\) Ibid., at para. 42.
Finally, in *Maloff v. Canada*, the vendor of a commercial real property had previously been a GST registrant but was not one at the time of the sale of the property. The purchaser claimed that it was a GST registrant and that it would self-assess and remit any GST owing. The purchaser, however, had misrepresented its status because it was also not a GST registrant at the time of the sale; it, too, had cancelled its GST registration. The vendor was found to be liable for the GST owing on the sale because it was not entitled to rely on the purchaser’s representation that it was a registrant.

Some conclusions can be drawn from the foregoing summary of the three clusters of issues that have most frequently given rise to litigation in the GST/HST context. The first is that GST/HST transactions in real property have not, by and large, been overly litigious, outside of a few ‘hot spots’ of concern. The second is that where there has been litigation, it has been driven by issues of valuation or characterization (i.e., what is a ‘substantial renovation’ as compared with a simple renovation), which are heavily fact dependent, or misunderstandings and mistakes (i.e., who must remit). A final conclusion is that it is unlikely that in a reasonably designed VAT it will be possible to entirely avoid these sorts of issues of valuation and characterization, and misunderstandings.

### 3.2.3 GST/HST Administration and Compliance

Although the CRA is not an independent source of tax law, the guides to the GST/HST published by the Agency are expected and intended to reflect the legislation, regulations, and case law. The publications tend be helpful and frequently relied upon by taxpayers, largely because the legislation and the regulations themselves are far too dense and cumbersome to be reasonably navigable by individuals who are not tax law specialists, and the reported case law is not readily accessible to most taxpayers (in substance or in form).

#### 3.2.3.1 Approach of the GST/HST

The GST/HST system in Canada rests on self-assessment. Consistent with the classic invoice-credit VAT method, registered businesses, organizations, and persons act as collection agents for the government. The end consumer (individual or non-registered business) ultimately pays the GST/HST over to suppliers as the agents of the Crown. Taxpayer obligations under the GST/HST system are presented in CRA publications in plain language. These publications strive to be

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96. 2004 GTC 439 (TCC).
97. *Ibid.*, at para. 18. Presumably, the vendor would be able to maintain a civil claim against the purchaser, as in *Rive v. Newton*, for indemnity on the basis of the misrepresentation that the purchaser was a current GST registrant.
reasonably easy to understand.99 Beyond these widely applicable publications intended for the general public, specialized guides, GST/HST Info Sheets, and forms (with instructions) all provide additional information for specific situations should they apply to particular taxpayers. For tax specialists, GST/HST Memoranda100 and several other technical resources or publications provide information about the finer aspects of the system.101 The CRA is a sophisticated organization with significant resources devoted to administrative functions. While the general GST/HST system is regarded by most observers and commentators as complex, it is fair to say – and the above discussion strongly suggests that special sectors such as real property are even more complex than the GST/HST on average.

3.2.3.2 GST/HST Rules, Procedures, and Forms

As mentioned above, businesses or organizations (including partnerships, which are considered taxable entities for GST/HST purposes) that operate in Canada and have sales over CAD 30,000 (CAD 50,000 for public service bodies) must register for GST/HST.102 The registration procedure is straightforward and fast, and can be done online or on the telephone. Any GST registrant becomes automatically a HST registrant. GST/HST registrants are obligated to collect GST/HST on all taxable (other than zero-rated) supplies of goods and services they provide.

Businesses and organizations have further obligations beyond registration and collection of the GST/HST. They must also maintain records, calculate the net GST/HST (tax collected on supplies minus tax paid on purchases) due to the government,103 remit the tax, and file periodic returns at stipulated reporting periods. The frequency of reporting periods (intervals at which tax returns must be filed) range from annual to quarterly, depending on annual taxable supplies thresholds. Other responsibilities include communicating the choice of an accounting period to the CRA; informing customers on whether the GST/HST is included in prices or calculated and shown separately;104 issuing sales invoices to customers;105 claiming input tax credits on goods, services, or capital property; and electing to account and file using simplified methods if applicable.

100. For example, n. 21 supra.
102. For a complete list of seller and purchaser obligations with respect to the GST/HST, see n. 99 supra.
103. Sometimes, tax collected on supplies is called output VAT, while the tax paid on purchases is called input VAT.
104. The vast majority of supplies in Canada are treated by sellers as tax-exclusive, that is, the GST/HST is not included in posted prices and is calculated and shown separately on invoices.
105. Invoices must satisfy certain requirements with respect to information shown. The amount of information increases with the amount of the sale. Sellers must also retain invoices in order to substantiate ITC claims when requested by the Canada Revenue Agency.
Special rules for the home construction industry (broadly defined) clarify administration and compliance. For instance, the imposition of tax depends on the circumstances surrounding the supply. Builders must charge HST at 13% on supplies in participating provinces, and GST at 5% elsewhere. Builders that make a sale of taxable real property have to charge and collect tax on the sale even if they are not registered for GST/HST. In some cases, however, purchasers have to remit the tax directly to the CRA instead of paying it to the builder, such as when the purchaser is registered for GST/HST, or the builder is a non-resident. The compliance effort related to real property transactions is significant relative to other types of transactions. In addition to the publications already referred to in this section, the CRA publishes a number of forms with instructions for specific transactions. Table 3.5 lists the publications and forms, including publication or form numbers, that relate to real property or general compliance obligations attached to such property.

Table 3.5. GST/HST Forms and Publications with Respect to Real Property

<table>
<thead>
<tr>
<th>Forms</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>GST22</td>
<td>Real Property – Election to Make Certain Sales Taxable</td>
</tr>
<tr>
<td>GST26</td>
<td>Election or Revocation of an Election by a Public Service Body</td>
</tr>
<tr>
<td></td>
<td>to Have an Exempt Supply of Real Property Treated as a Taxable Supply</td>
</tr>
<tr>
<td>GST34</td>
<td>Goods and Services Tax/Harmonized Sales Tax Return for Registrants</td>
</tr>
<tr>
<td>GST60</td>
<td>GST/HST Return for Acquisition of Real Property</td>
</tr>
<tr>
<td>GST189</td>
<td>General Application for Rebate of GST/HST</td>
</tr>
<tr>
<td>GST190</td>
<td>GST/HST New Housing Rebate Application for Houses Purchased from a Builder</td>
</tr>
<tr>
<td>GST191</td>
<td>GST/HST New Housing Rebate Application for Owner-Built Houses</td>
</tr>
<tr>
<td>GST191-WS</td>
<td>Construction Summary Worksheet</td>
</tr>
</tbody>
</table>

106. Note 29 supra.

107. A number of criteria must be met in order for the remittance responsibility to switch from seller to buyer. See n. 29 supra, 11–12. It has recently been shown that the remittance responsibility is not economically irrelevant: Joel Slemrod, ‘Does It Matter Who Writes the Check to the Government?’ The Economics of Tax Remittance’, National Tax Journal 61 (2008): 251.

108. Notes: All listed items are available electronically on the Canada Revenue Agency web site which is searchable by form or publication number; see search page <www.cra-arc.gc.ca/formspubs/menu-eng.html>, (accessed 13 Jul. 2009). List in table excludes GST Info Sheets above, and publications related to (1) transitional rules having to do with the reduction in GST and HST rates from 6% and 14% to 5% and 13% on 1 Jan. 2008, and (2) other sectors that are subject to special rules for real property (municipalities, non-profit organizations, charities). Source: Authors’ compilation from a variety of Canada Revenue Agency sources.
3.3 AN INDEPENDENT SUBNATIONAL VAT: QUÉBEC SALES TAX (QST)

3.3.1 PRINCIPLES AND POLICY

3.3.1.1 The QST System

The Province of Québec is the only subnational jurisdiction in the world that successfully operates a destination-based VAT. Québec has done so since July 1992.\(^{109}\) The QST applies to the vast majority of goods and services consumed

\(^{109}\) This general description of the QST system draws on Richard M. Bird & Pierre-Pascal Gendron, n. 6 supra.

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within the province and it is substantially harmonized with the federal GST. The two taxes are imposed on very similar, though not perfectly identical, bases.

The QST is a destination-based credit-invoice VAT that subjects most goods and services consumed in Quebec to tax at a statutory rate of 7.5%. On 19 March 2009, the provincial government announced its intention to raise the QST rate to 8.5% effective 1 January 2011. Unlike most other sales taxes in Canada, the QST applies on the GST-inclusive price of goods and services.\footnote{The only other province in which this is true is the Province of Prince Edward Island, which levies an RST. See Table 3.1 above in the text.} Thus, on a pre-tax retail sale to a final consumer at CAD 1,000 that is a taxable supply under both GST and QST, the GST at a rate of 5% amounts to CAD 50 and the QST at a rate of 7.5% amounts to CAD 78.75 (1,050 \times 0.075), for a total combined tax of CAD 128.75. Both the QST and the GST are collected at the point of sale, and their amounts are shown separately on invoices.\footnote{The obligations of sellers and purchasers are summarized in Revenu Québec, \textit{Renseignements généraux sur la TVQ et la TPS/TVH} (Québec: Gouvernement du Québec, 2008), available online at: \url{<www.revenu.gouv.qc.ca/documents/fr/publications/in/in-203(2009-01).pdf>}, (accessed 17 Jul, 2009). The English language version of this publication has not been updated yet but the 2003 English version is available at \url{<www.revenu.gouv.qc.ca/documents/eng/publications/in/in-203-v282005-04%29.pdf>}, (accessed 17 Jul, 2009).} For the most part, the QST base is identical to that of the GST/HST today. Input tax refunds (ITRs) are the name given under the QST to ITCs under the GST/HST.

A holdover from the early days of the tax is that input tax refunds (ITRs) with respect to QST – the equivalent of input tax credits (ITCs) under the GST are denied to registered businesses under particular circumstances. Large businesses, which are defined as having taxable sales (excluding the sales of financial services) over CAD 10 million during a given fiscal year, are denied ITRs with respect to the following types of goods and services: (1) light motor vehicles meant to be driven on public roads (e.g., small service vans), including property and services relating to such vehicles; (2) motor fuels used to supply the engines of the above vehicles; (3) various energy sources, unless used to produce movable property intended for sale; (4) telephone and other telecommunication services, with the exception of the Internet as well as 1-800, 1-888, and similar number services; and (5) food, beverages, and entertainment services not fully deductible under the [Income] \textit{Taxation Act}. The threshold is somewhat low and captures many medium sized businesses. It applies to all business sectors. This provision evidently is intended to protect QST revenues. However, it does so at a cost, both imposing some tax on business inputs and creating some incentive for businesses to inefficiently split operations to avoid the threshold.

\subsection*{3.3.1.2 Treatment of Immovable Property under the QST System}

Immovable property transactions are generally taxable under GST/HST, since ‘immovable property’ is specifically named as one of the constituent elements

QST also applies to transactions involving immovable property in a largely similar way. Indeed, given the high degree of conformity between the treatment accorded to real property under both the GST/HST and QST, this section presents only a brief discussion.

Specific examples of taxable transactions would generally include the following supplies or transactions: (1) sales of new residential buildings; (2) sales of commercial buildings; and (3) leasing of commercial buildings. The key exceptions to the taxable treatment of immovable property under the QST consist in the exempt treatment of: (1) sales of residences or dwellings that are not new at the time of sale; and (2) residential leases that are for a period of one month or longer. Although the documents and publications of Revenu Québec (RQ) do not mention implicit (or imputed) rents to owner-occupied housing, these are also exempt. The QST system features special rules quite similar to those that apply to the GST/HST system with respect to, among other things, registration; self-assessment and remittance of QST to RQ; scope of liability to tax on self-supply of residential dwellings; claiming of ITRs by non-registrants; and QST rebates on new houses.

Businesses and organizations that carry on business in the Province of Québec must register for the QST with RQ. The procedure is distinct from GST/HST registration. Both registrants and non-registrants (persons) that sell taxable immovable property must collect GST and QST on the sale. The exceptions to this rule apply when the person does not reside in Canada or in Québec, or the person is registered and the property sold is neither a residential building nor a cemetery plot. In both cases, the purchaser must self-assess the GST and QST and remit the amount to RQ. A builder who rents or occupies a residential building it built must generally pay GST and QST on the fair market value of the property. A builder who is not registered can claim ITCs and ITRs after having self-supplied the building. Self-supply rules do not apply to (1) persons who use the building as a residence (over 50% residential use); (2) universities, public colleges, and school administrations that build student residences; (3) some religious organizations; and (4) registrants who construct residential buildings in some remote regions.

112. ‘Real’ property under the GST/HST.

113. The distinctive meaning of ‘real property’ in Quebec is necessitated by the reliance in that province upon the Civil Code of Quebec (CCQ) and the differing conception of property that prevails under the CCQ. Outside of Quebec, the common law property concepts determine the boundaries of interests in real property. It is noteworthy in this respect that the definition of ‘real property’ as ‘including’ the specifically named types of property suggests that all property that would at common law (or civil law) constitute ‘real property’ remains ‘real property’ for GST/HST.


The QST features a new housing rebate that applies to new or substantially renovated housing, and new or substantially renovated residential rental property. The QST rebates are less generous than the GST rebates. The maximum rebate (CAD 5,573) is reached for a house valued at CAD 200,000. Any house valued at CAD 225,000 or over does not give rise to a rebate.116 The statutory QST rebate rate is 36% (like the GST) but the effective rate is slightly lower to correct for the fact that the QST is charged on top of the GST. When the purchase price or fair market value exceeds or equals CAD 225,000 but is below CAD 450,000, a QST rebate is provided and calculated on the basis of the GST rebate provided.

In closing, it is important again to note that registrants (both businesses and public service bodies) face restrictions in obtaining ITRs for QST paid on capital immovable property. Those restrictions are based on the portion of the use of the immovable property that is devoted to commercial activities. Table 3.6 summarizes these restrictions. Despite the harmonization of the GST and QST, there are minor differences in those restrictions (compare to Table 3.4).

<table>
<thead>
<tr>
<th>Percentage of Use (x) in Commercial Activities</th>
<th>All Other Registrants</th>
<th>Registered Individuals</th>
<th>Public Service Bodies</th>
</tr>
</thead>
<tbody>
<tr>
<td>x ≤ (10%)</td>
<td>None</td>
<td>None</td>
<td>None</td>
</tr>
<tr>
<td>10% &lt; x (50%)</td>
<td>% of use</td>
<td>% of use</td>
<td>None</td>
</tr>
<tr>
<td>50% &lt; x (90%)</td>
<td>% of use</td>
<td>% of use</td>
<td>100%</td>
</tr>
<tr>
<td>x ≥ (90%)</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
</tr>
</tbody>
</table>


117. Notes: Under the GST system, financial institutions claim input tax credits proportional to the percentage of use of capital property in commercial activities. In the QST system, normal rules for all other registrants. Individuals are not entitled to input tax credits or input tax refunds if the percentage of personal use of capital property exceeds 50%. A public service body may elect to submit itself to the rules applicable to all other registrants. Source: Revenu Québec, Renseignements généraux sur la TVQ et la TPS/TVH (Québec: Gouvernement du Québec, 2008), 25, <www.revenu.gouv.qc.ca/documents/fr/publications/in/in-203(2009-01).pdf>, (accessed 17 Jul. 2009).
3.3.2 Frequently Litigated Legal Issues

For the most part the issues raised in the case law originating in Québec relating to the QST closely mirror those that most frequently arise in the GST/HST context (see above review). Indeed, it would be, to some extent, a forced and false dichotomy to insist upon an entirely isolated treatment of the GST and the QST since so many of the issues arise in tandem. Naturally, a number of the cases discussed above arose in the Province of Quebec and therefore also carried with them various QST consequences at the provincial level, in addition to the GST consequences addressed at the federal level.

In addition to the cases discussed above in the GST/HST context, examples arising out of Que´bec can be found arising falling into the same three clusters of cases: (1) disputes surrounding the acceptable methods for arriving at fair market valuations of immovable property for QST purposes – an important issue for determining liability for QST under the self-supply rules;118 (2) disputes surrounding whether a particular renovation of a previously-occupied residential property constitutes a ‘substantial renovation’ – an important question for determining whether the renovations trigger treatment on resale as a new taxable supply of immovable property;119 and, finally, (3) at least one case relating to the coordination of collecting and remitting QST (though not in the context of a transaction involving immovable property).120

With respect to the first cluster of cases, in the valuation context, the QST case law has tended to reach conclusions that appear to be more or less consonant with that in the GST/HST. Probably the best example of a valuation case arising under

118. See, for example, Déziel v. Canada, [2002] T.C.J. No. 639 (QL), in which the valuation of self-supplied residential buildings was addressed.

119. The cases do not reach conclusions that vary from the GST/HST case law discussed above.

120. One important example, though not arising directly in the immovable property context, is the case of Québec (Sous-ministre du revenu) v. Trustee of Consortium Promecan Inc., [2008] S.C.C.A. 78 (S.C.C.), which was heard by the Supreme Court of Canada on 17 Mar. 2009. The case summary prepared by the Supreme Court of Canada provides that:

The Respondent trustee in bankruptcy claimed from a customer of the debtor an amount representing the balance of debts owed, including GST and QST. Upon learning of this, the Applicant Deputy Minister of Revenue of Quebec wrote to the customer to ask it to remit directly to him the amounts corresponding to the GST and QST payable. Faced with these competing claims, the customer paid the trustee and asked it to keep the amount corresponding to the taxes in a trust account until the tax issue was resolved, which the trustee agreed to do. The trustee then decided that it would not pay the Deputy Minister that amount since, in its view, the taxes, which had been invoiced prior to the debtor’s bankruptcy, were an unsecured claim for the Deputy Minister within the meaning of the Bankruptcy and Insolvency Act. The Deputy Minister appealed the trustee’s decision to the Superior Court, which ruled in his favour. The Court of Appeal reversed the decision.

In this case the taxpayer had built a senior’s residence at a cost of in Trois-Rivières, Québec. One of the central issues in the case related to the appropriate method of determining the fair market value of the building. The taxpayer’s expert and the expert retained by the Minister used the same three valuation methods discussed in the GST/HST section, above, namely: (1) the cost method; (2) the comparison method; and (3) the income method. The taxpayer’s expert produced valuations under the three methods ranging from CAD 1.460 million to CAD 1.525 million, whereas the Minister’s expert produced valuations ranging from CAD 1.820 million to CAD 1.905 million. The court held that because the building was new and the issue was valuation upon self-supply, the cost methodology should be preferred over the income or the comparison methods. With respect to choosing between the two expert reports on how to value the property using cost, the court preferred the expert retained by the Minister. The Minister’s expert had reached a fair market valuation under the cost method of CAD 1.820 million after accounting for the construction management services self-supplied by the corporation in addition to the explicit out-of-pocket expenses paid to various contractors for the construction of the senior’s residence.

With respect to the second cluster of cases, there are few (if any) cases surrounding what satisfies the definition of ‘substantial renovation’ for the purposes of the QST. There are, however, a number of examples of such issues arising out of the Province of Québec in the GST context. Many of these cases do not raise questions under the QST because the value at which the QST new housing rebate phases out completely – CAD 225,000 – is only half as high as the value at which the GST New Housing Rebate phases out entirely. This suggests not only that fewer cases would involve disputes over eligibility for the QST new housing rebate, but also that litigation would be correspondingly less attractive due to the transaction costs associated with bringing or defending a claim. Similarly, though for different reasons, it appears that there are few, if any cases involving immovable property and disputes relating to the responsibility to remit or collect QST.

It should probably not be too surprising that the case law arising out of the QST is not as deep or as developed as that relating to GST/HST when one considers that the Province of Québec has a population that is only a fraction of that of Canada as a whole. Nevertheless, it is comforting that the pattern of cases has more or less tracked that of the GST/HST with respect to the first two clusters of cases, and

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121. 2006 QCCQ 7273 (Québec Superior Court).
122. Ibid., at paras 22–26.
123. Ibid., at paras 38–47.
124. Ibid., at para. 125.
125. In addition to the cases referred to above in the GST/HST section, see Schoeb v. Canada, 2008 GTC 143 (TCC). In Schoeb the objection was not based on the how substantial the renovation was, but on whether the residence was the taxpayer’s primary residence or the primary residence of a relative and whether the application for a New Housing Rebate was made within the two year limit set by the legislation.
fewer examples of disputes over the responsibility to remit or collect QST. Perhaps the lower rate of disputes and mistakes over the responsibility to remit or collect is owed to the effectiveness of the administration of the GST/QST in Québec – a topic considered in the next section.

3.3.3 QST Administration and Compliance

3.3.3.1 Harmonization with GST/HST and Approach

RQ administers the GST on behalf of the federal government in Québec’s territory, in addition to the QST. Under the terms of its agreement with the federal government, RQ receives and processes applications for registration under the GST/HST system from all persons carrying on commercial activities in Québec. Businesses registered for the GST are automatically registered for the HST, and GST registration covers the activities of any business in all ten provinces. After registration, all taxable persons continue to deal with RQ for all GST/HST-related matters including returns, remittances, rebate applications, audits, investigations, interpretations of laws and regulations, notices of objection, tax collection, and unfilled returns. This administrative model is unique in the world.

Perhaps reflecting the fact that overall taxation levels in Québec are high in relation to the Canadian average, RQ has over the years become a sophisticated and aggressive tax authority. Indeed, the quality of RQ as a tax administration and its detailed knowledge of its taxpayer population, when added to the economies of scale from collecting two taxes together rather than separately, make the package an attractive one. With good information exchange, hitching the QST to the GST may well have helped both governments protect their revenues.126

3.3.3.2 QST Rules, Procedures, and Forms

Due to the substantial harmonization between the QST and GST, most of the above discussion of GST/HST rules and procedures applies here. Consequently, forms are also harmonized to a large extent, and there is an array of joint (GST-QST) forms with both a GST and QST form number. Differences between the two taxes (e.g., calculations, rates, etc.) are handled right on the forms. Table 3.7 lists the publications and forms, including publication or form numbers, that relate to immovable property or general compliance obligations attached to such property.

The forms under the heading Forms (GST) are GST-related forms to the intention of registrants doing business in Québec. Nevertheless, as in the case of the GST/HST, compliance requirements with respect to immovable property are non-trivial.

126. For an extended discussion of the agreement with the federal government and the administration and enforcement of Revenu Québec in relation to the GST and QST, see Richard M. Bird & Pierre-Pascal Gendron, n. 6 supra.
Table 3.7.  **QST Forms and Publications with Respect to Immovable Property**

<table>
<thead>
<tr>
<th>Forms (GST)</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>FP-189-V</td>
<td>General GST/HST Rebate Application</td>
</tr>
<tr>
<td>FP-524-V</td>
<td>New Residential Rental Property GST Rebate Application</td>
</tr>
<tr>
<td>FP-525-V</td>
<td>New Residential Rental Property GST Rebate Application Supplement: Multiple Units</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Forms (QST)</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>VD-224.1-V</td>
<td>Election to Defer Payment of the Tax on the Self-Supply of a Residential Complex</td>
</tr>
<tr>
<td>VD-370.67-V</td>
<td>New Residential Rental Property QST Rebate (new residential complex version)</td>
</tr>
<tr>
<td>VD-370.89-V</td>
<td>New Residential Rental Property QST Rebate (co-operative housing corporation version)</td>
</tr>
<tr>
<td>VD-403-V</td>
<td>General Application for a Québec Sales Tax (QST) Rebate</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Forms (GST and QST)</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>FP-505-V</td>
<td>Special Purpose Return</td>
</tr>
<tr>
<td>FP-2022-V</td>
<td>Election to Treat a Sale of Real Property (an Immovable) as a Taxable Sale</td>
</tr>
<tr>
<td>FP-2190.A-V</td>
<td>GST-QST New Housing Rebate Application: Owner of a New Home and Land Purchased from the Same Builder</td>
</tr>
<tr>
<td>FP-2190.C-V</td>
<td>GST-QST New Housing Rebate Application: Rebate Granted by a Builder</td>
</tr>
<tr>
<td>FP-2190.L-V</td>
<td>GST-QST New Housing Rebate Application: Owner of a Home on Leased Land or a Share in a Housing Co-op</td>
</tr>
<tr>
<td>FP-2190.P-V</td>
<td>GST-QST New Housing Rebate Application: Owner of a New or Substantially Modified Home</td>
</tr>
<tr>
<td>FP-2192-V</td>
<td>GST-QST Adjustment Application for Residential Complexes</td>
</tr>
</tbody>
</table>

**Guides**

<table>
<thead>
<tr>
<th>Guides</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>IN-203-V</td>
<td>General Information Concerning the QST and the GST/HST</td>
</tr>
<tr>
<td>IN-205-V</td>
<td>QST and GST/HST Rebates: New or Substantially Renovated Housing and Residential Rental Property</td>
</tr>
</tbody>
</table>

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127. Notes: All listed items are available electronically on the Revenu Québec web site which is searchable by form or publication number; see search page <www.revenu.gouv.qc.ca/eng/pub_form/>, (accessed 13 Jul. 2009). List in table excludes publications related to (1) transitional rules having to do with the reduction in GST and HST rates from 6% and 14% to 5% and 13% on 1 Jan. 2008, and (2) other sectors that are subject to special rules for immovable property (public service bodies, that is, municipalities, non-profit organizations, charities).

*Source:* Authors’ compilation from a variety of Revenu Québec sources.

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3.4 OTHER TAXES ON REAL AND IMMOVABLE PROPERTY IN CANADA

This section presents a brief description of other taxes applicable to real and immovable (henceforth real) property itself, transactions in real property, and services from real property. All the taxes considered below are administered outside the GST/HST and QST regimes, and apply in addition to those two VATs.

Real property taxes are widely used throughout Canada and imposed by both provincial and municipal governments. They constitute the most important source of revenues for the latter. At the top stands the ‘basic’ property tax, an annual charge paid by the owners of real property on a measure of its value. Its base is important for two reasons. Firstly, the case law reviewed earlier suggests that property valuations can be a useful input to GST/HST for compliance and in courts as a number of disputes focus on valuations and the methods used. Secondly, the basic property tax is not inefficient unlike other forms of taxes on real and immovable property.

Real property transfers in particular are subject to various taxes and charges, including land transfer taxes (called stamp duties in some countries), notary fees, and registry charges. Land transfer taxes are quite widespread throughout Canada and come in two versions: provincial and municipal. The provinces of British Columbia, Manitoba, New Brunswick, and Ontario impose provincial land transfer taxes while municipal governments in the Province of Nova Scotia and the City of Toronto (Ontario) impose their own land transfer taxes. The City of Toronto implemented its own Municipal Land Transfer Tax – which applies in conjunction with the province’s land transfer tax on 1 February 2008, after extended discussions, political maneuvering, and much opposition from the public and the real estate industry.

Some jurisdictions also impose taxes on hotel rooms and other types of temporary accommodation. British Columbia is an example of such a jurisdiction, although it is important to note that the harmonization of the province’s sales tax with the GST will see the elimination of that separate hotel room tax.128

Viewed as a whole, these additional taxes connected to real property are important, not only because they undermine efficiency and impose compliance and administrative costs, but because they introduce complex patterns of double- or multiple taxation of real property. A strong case has been made recently in the context of South Africa to eliminate land transfer taxes and to let the VAT be the sole transaction tax to apply to transfers of real property, subject to some exceptions.129 In Canada, proposals to eliminate provincial land transfer taxes in provinces with a VAT (British Columbia, New Brunswick, Ontario) do not appear to have been given serious thought, even during the recent harmonization

discussions for two of those three provinces. The coexistence of VAT (especially with its real property rebate systems) and land transfer taxes will make transaction-based taxation of real and immovable property less neutral than it could have been under a properly designed VAT to be used as a lone tax on such transactions.

The analogue of property taxes on commercial real property (often referred to as local business taxes) is levied on business occupiers as opposed to owners under the residential property tax. Business taxes are levied in all ten provinces by a combination of provincial or municipal authorities. All ten provinces also authorize municipalities to impose special assessments and charges to recover local improvement costs. Québec imposes a special 'tax on lodging' that is calculated on the accommodation price inclusive of GST and QST and collected separately. Revenues from this tax are allocated to a tourism partnership fund which is used to fund expenses to promote the tourism industry. Revenue source and expenditures are matched on a regional basis. Finally, the Province of British Columbia shares RST revenue with its municipalities. For instance, municipalities may request that the hotel room tax be levied at 8% rather than 7% (the current RST rate in the province), with the additional percentage point to be transferred to local governments.

This section is not meant to be exhaustive, so to simplify and illustrate, we present in Table 3.8 an incomplete summary of all government-imposed charges on new housing in Canada. New housing is the most politically-sensitive area of real property taxation.

<table>
<thead>
<tr>
<th>Charges/level</th>
<th>Components</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Municipal/regional</strong></td>
<td></td>
</tr>
<tr>
<td>Building permit fees</td>
<td>Building permits, plumbing, and mechanical or electrical permit fees</td>
</tr>
<tr>
<td>Development application and processing fees</td>
<td>Subdivision application fees, condominium application fees, site plan approval, administration fees</td>
</tr>
<tr>
<td>Infrastructure charges</td>
<td>Hard (sewer, water, road) and soft (parks, libraries, police) off-site infrastructure (subdivision agreements)</td>
</tr>
</tbody>
</table>

or development charges), and water and sewer connection fees; engineering review fees; sewer connection and other inspection fees

<table>
<thead>
<tr>
<th>Charges/level</th>
<th>Components</th>
</tr>
</thead>
<tbody>
<tr>
<td>Land dedications</td>
<td>Land dedications (and cash in lieu thereof)</td>
</tr>
<tr>
<td>Registry/land transfer fees</td>
<td>City of Toronto’s Municipal Land Transfer Tax; the Province of Nova Scotia allows municipalities (e.g., Halifax) to levy their own municipal land transfer tax</td>
</tr>
<tr>
<td>Property taxes</td>
<td>Property taxes (the ‘basic’ property tax), garbage collection surcharges, police surcharges, fire surcharges, education surcharges, etc.; all ten Canadian provinces and three territories allow municipalities to levy (real) property taxes</td>
</tr>
</tbody>
</table>

Provincial

<table>
<thead>
<tr>
<th>Charges/level</th>
<th>Components</th>
</tr>
</thead>
<tbody>
<tr>
<td>Home warranty fees</td>
<td>New home warranty programmes (both required and optional)</td>
</tr>
<tr>
<td>Provincial sales taxes (RSTs)</td>
<td>Retail Sales Tax on construction materials</td>
</tr>
<tr>
<td>Provincial (other)</td>
<td>Provincial plumbing and electrical inspection fees, provincial engineering review fees, home warranty licensing fees</td>
</tr>
<tr>
<td>Registry/land transfer fees</td>
<td>Land transfer taxes and title registration fees are levied by the provinces of British Columbia, Manitoba, New Brunswick, and Ontario</td>
</tr>
</tbody>
</table>

3.5 CONCLUSION

Despite its complexity and the harsh reception the GST was greeted with at its inception, the story emerging from Canada’s VAT experience is mostly a happy one. Indeed, it now appears that a majority of the provinces will soon have replaced their RSTs with harmonized VAT systems – a positive sign of acceptance and the recognition that VATs are economically superior to RSTs and that having parallel but incompatible – in practice, that is – sales tax systems makes little sense from the perspective of economic efficiency and compliance and administrative costs.

As this chapter has explained, the tax treatment of real property under Canada’s VAT systems – the GST/HST and QST is far from being straightforward.
Nevertheless, this chapter has attempted to summarize the most important features of the design of the systems and their administration, as well as identify the legal issues that most frequently land in the Tax Court of Canada. If nothing else, the complexity of the relevant Canadian law demonstrates and underscores that the value of a comparative volume such as this one is inestimable, particularly to policymakers in jurisdictions considering imposed on VAT on real property.