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The Application of HST to Used Residential Real Estate

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It is often assumed that the Harmonized Sales Tax (HST), which in Ontario is currently 13% does not apply to the sale of a used residential property. In some cases the rules are broader than one might think, whereas in other cases, the rules are more restrictive.

The General Rule

As a general rule, every “supply” of real property in Canada is subject to HST. As always, there are exceptions to this and certain sales of real property can be exempt from HST. In other words, HST will apply to all sales of real property unless the sale falls within an exception to the general rule. Supplies of real property that are considered exempt from HST can be found in Part I of Schedule V to the Excise Tax Act. (the “ETA”)

The Used Residential Complex Exemption

One such exemption is the sale of a used residential complex. This widely-used exemption allows the sale of “used homes” to take place without HST consequences (other than with respect to legal fees and real estate commission which are subject to HST). Plainly speaking, a residential complex will be deemed “used” if a person who is not the builder sold the property in question. The exemption applies to both the resale of an individual’s personal residence and to the resale of rental housing, where the residential complex was held for the purpose of earning rental income.

On the sale of a used residential complex, the seller usually certifies the nature of the property as being exempt from tax under the ETA and therefore no HST is collected on closing. The main objective behind this particular exemption is to ensure that only the first commercial supply of the property, after it is built, is subject to HST.

What is a residential complex?

According to the ETA, a “residential complex” is a part of a building which contains one or more residential units, which includes the common areas, as well as the land that is immediately adjacent to the residential building as a whole. A residential complex includes not only a detached house, but also a semi-detached house, rowhouse, apartment building, a residential condominium unit, a mobile home and a floating home. The sale of this type of residential complex will be exempt from HST so long as it is being occupied as a place of residence by individuals at the time of sale or in the event that the residential complex is vacant at the time of sale, if it was last occupied as a place of residence.

The ETA is silent on whether the definition of “residential complex” is intended to be limited to a particular building size. The Courts have interpreted the phrase “residential complex” as being capable of including more than a single building. Court decisions on



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this particular subject matter focus on the size of the related land, rather than the size of the building.

Input tax credits and the used residential complex exemption

An HST exemption on the sale of a used residential complex is not always available. According to the ETA, in circumstances where the seller of the real property has claimed an input tax credit either for the last acquisition of the property, or for an “improvement” to the capital real property, such sales become taxable. As a result, the used residential exemption is lost and HST must be charged to the Buyer.

An “improvement” means any goods or services used in improving the capital real property, to the extent that the amount paid for the goods or services is included as part of the “adjusted cost base” of the property for income tax purposes. For example, the addition of a central air conditioning unit to a residential complex would likely be considered an improvement and therefore if the seller claimed an input tax credit for the air conditioning unit, the seller would have to collect HST from the buyer when the property is sold.

Buyers and sellers must be alert to the potential HST ramifications that will follow if they have claimed an input tax credit with respect to the property up for sale. The popular used home exemption will not apply to their sale and HST must be charged. Buyers and sellers should keep this in mind in all real estate transactions in order to avoid any unwanted liability in relation to the ETA. Of course, even where HST applies, where the buyer of the property is an HST registrant, the parties can choose to offset the HST if the buyer agrees to self-assess the HST payable on their HST return at a later date.

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