

Tax memo

Canadian tax updates



Joint ventures and partnerships: GST/HST and issues for real estate industry

Discusses issues relevant to real estate developers, builders and lessors.

November 2, 2012

This *Tax memo* highlights certain Goods and Services Tax/Harmonized Sales Tax (GST/HST) and Workplace Safety and Insurance Board (WSIB) issues relevant to those in the real estate and construction industries:

- some GST/HST issues real estate joint ventures and partnerships encounter;
- issues related to the use of bare trustees in the real estate sector; and
- an Ontario WSIB coverage change, effective January 1, 2013, relevant to employers in the construction industry.

GST/HST issues

Joint ventures

Under the general GST/HST rules, a joint venture is not a “person.” Therefore, unless a joint venture election is in place, all participants in a joint venture must account separately for their prorated share of the GST/HST collectible on any sales, as well as the GST/HST paid on the joint venture purchases.

The joint venture election under the *Excise Tax Act* provides flexibility in the reporting of the GST/HST for certain prescribed joint ventures. For GST/HST purposes, the participants in a joint venture may elect one of the following to be the “operator” of the joint venture:

- a member that contributed resources and takes a share of revenue or losses; or
- a manager of the joint venture.

The election is particularly helpful when there is a single operator and the other participants are not directly involved in day-to-day operations.

The elected joint venture operator is responsible for accounting for the GST/HST on all sales made by participants through the joint venture and will claim allowable input tax credits for tax paid on expenses and other outlays made through the joint venture. However, the operator and the participants remain jointly and severally liable for the collection and remittance of GST/HST for the joint venture operations.

Participants will still be permitted to claim input tax credits for tax paid on expenses related to the joint venture that they incur directly (that is, not through the joint venture), to the extent that they would be entitled to do so if the election had not been made.

The joint venture operator election is available in various prescribed cases, including for joint ventures:

- undertaking the construction of real property; or
- whose purpose is to derive revenue from real property by way of sale, lease, licence or similar arrangement.

The election must be made using the prescribed form, but the form does not have to be filed with the Canada Revenue Agency (CRA).

The CRA takes the position that the joint venture operator election applies only to post-acquisition conduct and, in the case of real property, does not apply to the acquisition of that property.

Consequently, each participant should:

- register for GST/HST on or before the acquisition date of real property acquired in connection with a commercial activity; and
- claim any available input tax credit for its share of the GST/HST upon the acquisition.

For real estate transactions in which the purchaser is required to self-assess GST/HST on the purchase, each participant of the joint venture:

- should provide its GST/HST registration number to the vendor, so GST/HST is not charged on the sale; and
- must self-assess its respective share of the GST/HST and claim any available corresponding input tax credit.

Subsequently, the joint venture participants can elect an operator to account for the GST/HST on post-acquisition activities related to the real property.

Partnerships

A partnership is considered a separate “person” for GST/HST purposes. If carrying on a commercial activity, the partnership must be registered for and report the GST/HST on its activities. A partnership cannot designate a partner, in an equivalent manner to the operator under a joint venture election, to handle all the GST/HST accounting for the partnership.

If someone other than the partnership has reported the GST/HST transactions on behalf of the partnership, interest and penalties could be assessed against the partnership for the non-reporting of GST/HST collected on revenue.

There may also be an issue with respect to the partnership’s eligibility for input tax credits for GST/HST paid, whether because the partnership was not GST/HST registered when the GST/HST was incurred or because the time to claim the input tax credit has lapsed. Finally, the person reporting the GST/HST on behalf of the partnership can be assessed for claiming input tax credits if they were not theirs to claim.

Nominees or bare trustees

In some cases, legal title to real property may be held in the name of a corporation acting as nominee or bare trustee for the beneficial owner(s). This nominee corporation may take all actions necessary to facilitate the acquisition, financing, leasing and sale of the particular property as agent for, and under the instructions of, the beneficial owner(s).

As a result of this arrangement, the nominee corporation is typically shown as the mortgagor, lessor and/or purchaser/vendor on all agreements pertaining to the property.

To determine whether agency principles or trust principles apply, the provisions of the bare trustee agreement must be reviewed to see who has discretionary decision-making powers.

The CRA will consider a corporation to be a bare trustee if the corporation has no independent or discretionary powers in the decision-making related to the properties held in trust.

On the other hand, if the bare trustee has no discretionary powers and all powers or responsibilities to manage the trust property are retained by the beneficial owner, the CRA generally will consider the beneficial owner, rather than the bare trustee, to be involved in commercial activities

relating to the trust property. In this case the beneficial owner generally would:

- be required to register for GST/HST;
- collect and remit the GST/HST payable; and
- be eligible to claim any related input tax credits under the normal rules.

The bare trustee would not be considered to be engaged in a commercial activity in respect of the trust property, and therefore would not be allowed to account for the GST/HST in respect of the trust property.

If the bare trustee has reported the GST/HST transactions on behalf of the beneficial owner, interest and penalties could be assessed against the beneficial owner for the non-reporting of GST/HST collected on revenue.

There may also be an issue with respect to the beneficial owner's eligibility for input tax credits for GST/HST paid, whether because the beneficial owner was not GST/HST registered when the GST/HST was incurred or because the time to claim the input tax credit has lapsed. Finally, the bare trustee reporting the GST/HST on behalf of the beneficial owner can be assessed for claiming input tax credits that were not theirs to claim and were not incurred in a commercial activity of the bare trustee.

Ontario Workplace Safety and Insurance Board (WSIB) coverage

Until January 1, 2013, owners and executive officers of a company are not required to have coverage under the Ontario WSIB, although the company may elect to obtain coverage for them.

Consequently, companies may have many owners and executive officers who are not required to have WSIB coverage. If the company chooses not to obtain coverage for the owners and executive officers, these individuals are not eligible for WSIB benefits.

To qualify as an executive officer, an individual must be an executive officer who controls the direction of

an entire company (as opposed to a division, branch or department), and his or her appointment must be recorded in the company's minute books.

The executive officers of a company generally include the president, vice president, chief executive officer, chief financial officer, chief operating officer, and secretary/treasurer.

Effective January 1, 2013, an employer who is in the construction industry may select only one owner or executive officer to be exempt from WSIB coverage. The selected individual must not perform any construction work, although periodic site visits are permitted. To qualify for this exemption, a prescribed form (*Declaration for Exemption from Compulsory Coverage*) must be completed and submitted to WSIB for approval.

Owners or executive officers who do not qualify for the exemption must have WSIB coverage, but may be eligible for a special premium rate. It is anticipated that the special rate will be \$0.21 per \$100 of payroll.

Example

Suppose Constructco Limited has as executive officers the president and five vice-presidents, all of whom are listed in the company's minute book as executive officers. Under the current rules all six are not required to have WSIB coverage.

Effective January 1, 2013, only one of the six executives can apply to be exempt from coverage, and then only if he or she does not perform any construction work and visits construction sites only periodically.

For more help

For more information, please contact your local PwC adviser or the individuals listed on the next page.

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