



Harmonized Sales Tax: Builders and Recaptured Input Tax Credits

The Government of Ontario and the Government of British Columbia have each introduced a harmonized sales tax (HST) that came into effect on July 1, 2010.

The HST rate in Ontario is 13% of which 5% is the federal part and 8% the provincial part.

The HST rate in British Columbia is 12% of which 5% is the federal part and 7% the provincial part.

This info sheet reflects tax changes included in the *New Harmonized Value-added Tax System Regulations*, and the *New Harmonized Value-added Tax System Regulations, No. 2*.

This info sheet explains how the recapture of input tax credits (RITC) requirement applies to builders in Ontario and British Columbia (B.C.).

Definitions for GST purposes, e.g., builder, commercial activity, consideration, financial service, person, property, qualifying group, specified member, real property, service, supply, and taxable supply, generally apply under the HST, as do the CRA's current policies on the application of the GST to housing. Guide RC4052, *GST/HST Information for the Home Construction Industry*, and GST/HST Info Sheet GI-005, *Sale of a Residence by a Builder Who is an Individual*, explore many of these important terms and concepts.

Builders who are registered for GST purposes are entitled to claim input tax credits (ITCs) to recover the provincial portion of the HST payable on most purchases and operating expenses for use in their commercial activities, in the same way and under the same rules that apply to the recovery of the GST. The GST rules for various types of expenses are explained in Guide RC4052. Builders are not entitled to claim ITCs for any provincial sales tax or retail sales tax paid or owing.

In some cases, however, GST/HST registrant builders may be required to repay the provincial part of certain amounts claimed as ITCs.

Affected builders are not allowed to simply forego claiming ITCs in order to fulfill the RITC requirement (even if the effect on net tax would be the same). Failure to recapture ITCs in the proper manner may result in penalties.

Under the HST framework, the provinces of Ontario and B.C. are allowed to temporarily restrict ITCs for the provincial portion of the HST.

These provinces generally restrict ITCs for the provincial portion of the HST paid on "specified property and services" that a "large business" acquires, or brings into the province, for use by the large business in the province.

Recapture period

For RITC purposes, the recapture period means a one-year period that:

- begins immediately after June 30 of a particular calendar year and ends immediately before July 1 of the following calendar year, and
- occurs during the period that the RITC requirement is in effect (July 1, 2010 to June 30, 2018).

Large business

As a general rule, a person is considered a large business during a particular recapture period if the person is a GST/HST registrant and:

- the person has total taxable revenues (RITC threshold amount) of more than \$10 million in their last fiscal year that ended before the recapture period, or

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- the person is one of the following financial institutions, or a person that is related (for purposes of the GST/HST) to one of the following financial institutions: a bank; a credit union; a corporation that is licensed or otherwise authorized under the laws of Canada or a province to carry on in Canada the business of offering to the public its services as a trustee; an insurer or any other person whose principal business is providing insurance under insurance policies; a segregated fund of an insurer, or an investment plan.

A builder that satisfies either of these criteria is considered to be a large business even if the builder does not have a permanent establishment in Ontario or B.C.

The RITC requirements for selected listed financial institutions are not included in this info sheet.

Public service bodies such as municipalities, hospital authorities, universities, public colleges, school authorities, charities, and non-profit organizations **are not** considered large businesses. If you are a public service body, this info sheet does not apply to you.

RITC threshold amount

When calculating its RITC threshold amount, a GST/HST registrant builder must generally include all consideration for:

- their taxable supplies made in Canada, and
- their taxable supplies made outside Canada through a permanent establishment in Canada,

that became due or was paid without having become due in their last fiscal year that ended before the recapture period.

The builder must also generally include all consideration for such supplies made by any other GST/HST registrant that is associated (for GST/HST purposes) with the builder that became due or was paid without having become due in the associated person's last fiscal year that ended before the recapture period. This includes consideration for supplies made by an associated person that is a GST/HST registrant, but that is not, on its own, considered to be a large business.

The consideration for taxable supplies by the builder or a GST/HST registrant associated with the builder includes:

- the amount by which the consideration for a supply is reduced because of goods given as a trade-in;
- the value of supplies made between closely related corporations that elected for GST/HST purposes to otherwise treat the supplies as being made for nil consideration; and
- the fair market value of a supply made between persons not dealing at arm's length for less than its fair market value.

The consideration for taxable supplies by the builder or a GST/HST registrant associated with the builder **does not** include:

- the value of GST/HST or certain provincial levies (such as the provincial retail sales tax);
- the value of the sale of capital real property;
- the value of any supplies of financial services; and
- the value of any goodwill supplied as part of the supply of a business.

Example 1

Builder A is a GST/HST registrant that builds houses for sale. The total consideration for Builder A's taxable supplies in its fiscal year ending March 31, 2010 was \$8.5 million. Company B is a GST/HST registrant that is associated with Builder A for GST/HST purposes. Company B manufactures cabinets, the total consideration for the sales of which was \$3 million in its fiscal year ending December 31, 2009. Both Builder A and Company B are considered to be large businesses for RITC purposes during the recapture period of July 1, 2010 to June 30, 2011 because each has an RITC threshold amount equal to \$11.5 million.

If a builder has a fiscal year that is shorter or longer than 365 days, the calculation of the RITC threshold amount must be adjusted to reflect the length of that fiscal year.

If a partnership is a large business and a member of the partnership (other than an individual) acquires, or brings a specified property or service in Ontario or B.C. for use in the province, and that use is in respect of the activities of the partnership, the member will generally be considered to be a large business for that particular acquisition or bringing in.

If a participant in a joint venture is a large business that has made a joint venture election with the operator of the joint venture, and the operator acquires, or brings a specified property or service into Ontario or B.C. on behalf of that participant for use in the province, the operator will generally be considered to be a large business for that particular acquisition or bringing in.

Changes during a recapture period

If a person that is not a large business at the beginning of a recapture period has a fiscal year end during that recapture period and its RITC threshold amount exceeds \$10 million at that point, the person will generally not become a large business until the beginning of the next recapture period.

Example 2

You are a builder with a fiscal year end of December 31. Your RITC threshold amount for the fiscal year ending December 31, 2009 is \$8 million. Therefore, you are not a large business during the recapture period of July 1, 2010 to June 30, 2011. At the end of your fiscal year ending December 31, 2010, your RITC threshold amount is \$11 million. You do not become a large business until July 1, 2011, and are a large business during the recapture period of July 1, 2011 to June 30, 2012.

If a person that is a large business at the beginning of a recapture period has a fiscal year end during that recapture period and its RITC threshold amount is below \$10 million at that point, the person will generally continue to be a large business until the end of that recapture period.

Example 3

You are a builder with a fiscal year end of December 31. Your RITC threshold amount for the fiscal year ending December 31, 2009 is \$12 million. Therefore, you are a large business during the recapture period of July 1, 2010 to June 30, 2011. For your fiscal year ending December 31, 2010, your RITC threshold amount is \$9 million. You continue to be a large business until June 30, 2011, and are not a large business during the recapture period of July 1, 2011 to June 30, 2012.

If the RITC threshold amount of a person is more than \$10 million at the time it becomes a GST/HST registrant, that person (and any associated person) will generally be considered to be a large business and will be required to begin recapturing ITCs at that time.

If a particular corporation that is a large business acquires control of another corporation that is not a large business, the other corporation (and any associated persons) will generally be considered to be a large business when that control is acquired and will be required to begin recapturing ITCs at that time.

If two or more corporations amalgamate and the combined RITC threshold amounts of those corporations is greater than \$10 million at that time, the amalgamated corporation will generally be considered to be a large business upon amalgamation and will be required to begin recapturing ITCs at that time.

If a particular person that is not a large business acquires all or substantially all of the assets of another person that is a large business and continues to carry on the business of that other person, the particular person will generally be considered to be a large business at the earlier of:

- the time that it begins to carry on the business, and
- the time that it acquires substantially all of the assets,

and will be required to begin recapturing ITCs at that earlier time.

If a person becomes, or becomes related with, one of the financial institutions listed on page 2, the person will generally be considered to become a large business at that time (and continue to be one until it ceases to be one of those financial institution or ceases to be related to one), and will be required to begin recapturing ITCs at that time.

Specified property and services

Generally, from the perspective of the home construction industry, specified property and services include:

- electricity, gas, steam, and fuel (other than fuel used in a propulsion engine) together with incidental delivery charges or regulatory fees;
- telecommunication services, other than Internet access services, Web hosting services or toll-free telephone services such as 1-800 telephone services;

- food, beverages and entertainment, to the extent that they are already subject to the existing ITC repayment requirements (generally 50%);
- road vehicles weighing less than 3,000 kilograms and required to be licensed for use on a public highway (whether purchased or acquired by way of lease, licence or similar arrangement), along with parts and services acquired within 12 months of the vehicle's acquisition (e.g., acquisition and installation of a vehicle anti-theft system), other than parts and service for routine repair and maintenance; and

that is acquired or brought into Ontario or B.C. by a large business for use (in whole or in part) in Ontario or B.C. by that business.

In addition, fuel (other than diesel fuel) that is acquired, or brought into **Ontario** by a large business for use by that business in the engine of a specified road vehicle is subject to the RITC requirement (even if that vehicle was acquired, or brought into Ontario, prior to July 1, 2010).

Motor fuels acquired or brought into **B.C.** are eligible for a point-of-sale rebate of the provincial part of the HST, so are not considered to be specified property for RITC purposes.

A specified service that is acquired in another province or country is considered to be brought into Ontario or B.C., respectively, if it is for use (in whole or in part) in that province.

If a large business brings a specified property or service into Ontario or B.C. for use (in whole or in part) in that province by the large business, the large business will generally be required to account for the provincial part of ITCs that are available (or would be available if the provincial part of the HST were payable) for that acquisition or bringing in of the specified property or service. This rule applies even where the property or service is acquired or brought in for consumption or use exclusively in commercial activities of the large business.

Property and services acquired in Ontario or B.C. for consumption or use outside those provinces are generally not subject to the RITC requirement.

Example 4

Build Co. is a GST/HST registrant in the business of building and selling new houses and condos for sale in Ontario, and had a total of \$15 million in taxable sales in its fiscal year ending June 30, 2011. In September 2012, Build Co. begins construction of a larger administrative office for its expanding operations. As Build Co. is a large business for the recapture period July 1, 2012 to June 30, 2013, it is subject to the RITC requirements for specified property and services it acquires or brings into Ontario, including those acquired to construct the new houses, condos, and administrative office.

Example 5

During its fiscal year ending March 31, 2010, a non-profit organization finished building a 100-unit seniors' residence situated in B.C. When the first resident moved in, the non-profit organization was deemed to have made a taxable self-supply of the residence, and the fair market value of that supply was \$33 million. However, as a non-profit organization is not considered to be a large business for RITC purposes regardless of the value of its taxable sales, the RITC requirement does not extend to any of its expenses.

Example 6

CanCorp, which builds homes in B.C. and Alberta, is a large business for the recapture period July 1, 2011 to June 30, 2012. On August 15, 2011, CanCorp buys a road vehicle (weighing less than 3,000 kilograms) in Alberta and pays GST at 5%. CanCorp intends to use the road vehicle 70% in its business in Alberta and 30% in its business in B.C.

The vehicle is a specified road vehicle for RITC purposes because it was brought into B.C. by a large business for use, in part, by the large business, in B.C. CanCorp is required to account for the ITCs to which it would have been entitled had the provincial part of the HST in B.C. (7%) applied to the purchase of the vehicle. CanCorp is also required to recapture those ITCs for the provincial part of the HST.

If a large business pays an allowance or a reimbursement to an employee or a partner in circumstances where ITCs would be available to the large business in respect of that allowance or reimbursement, the large business will generally be required to recapture the provincial part of those ITCs to the extent that the allowance or reimbursement is attributable to specified property and services.

The rules for claiming ITCs on the **federal** part of the HST paid on these inputs are not affected.

Transitional measure – Self-assessment

If a builder that is a large business acquires a specified property or service, and the consideration for the supply first becomes due, or is paid without having become due, after October 14, 2009 and before May 2010, then to the extent that:

- the specified property is delivered, and ownership of the property is transferred, to the builder on or after July 1, 2010, or
- part of the specified service (more than 10%) is performed on or after July 1, 2010,

the builder will generally be required to self-assess the provincial part of the HST for that property or part of the service either:

- (i) in the builder's GST/HST return for the reporting period that includes July 1, 2010, if the due date for that return is before November 2010, or
- (ii) in any other case, by completing and filing Form GST489, *Return for Self-Assessment for the Provincial Part of Harmonized Sales Tax (HST)* and paying the amount before November 2010.

The builder will then recapture any ITCs available for the provincial part of the HST on the GST/HST return for the reporting period in which the ITCs first become available.

Non-arm's length transactions

If a builder that is a large business acquires a specified property or service from someone with whom they are not dealing at arm's length for no consideration, or for consideration that is less than fair market value, the builder will generally be required to recapture ITCs as if the transaction had been made at fair market value, **even if** the property or service was acquired, or brought into the province, for consumption or use exclusively in the builder's commercial activities.

ITC recapture rates

The rate of ITC recapture will be 100% for the first five years that the HST is in effect in Ontario and B.C., and then will be phased out by reducing the rate of recapture in equal increments over the following three years. The recapture rates will therefore be:

- 100% for the period from July 1, 2010 to June 30, 2015,
- 75% for the period from July 1, 2015 to June 30, 2016,
- 50% for the period from July 1, 2016 to June 30, 2017,
- 25% for the period from July 1, 2017 to June 30, 2018,
- 0% on or after July 1, 2018.

When to account for recaptured ITCs

A builder that is a large business is generally required to account for recaptured ITCs in its GST/HST return for the reporting period in which the ITCs first become available. This is the first reporting period in which the provincial part of the HST to which the ITC relates becomes payable, or is paid without having become payable.

However, if the builder is currently required to repay ITCs for a particular specified property or service in a reporting period other than the reporting period in which the ITCs first become available, the builder will generally be required, under the RITC requirement, to recapture ITCs for that same specified property or service in that same reporting period.

Example 7

A builder that is a large business is currently required to repay 50% of the ITCs that it claims for certain meal and entertainment expenses in the reporting period immediately following the end of its fiscal year. Some of the meals and entertainment are also specified property or services for RITC purposes. The builder is also generally required to recapture the provincial part of the ITCs for those particular meal and entertainment expenses in the reporting period immediately following the end of its fiscal year, rather than in the reporting period in which the ITCs first became available.

How to account for recaptured ITCs

Restricted ITCs will be "recaptured" rather than denied, so affected builders must separately identify recaptured ITCs in their GST/HST returns. A builder that must recapture ITCs will be required to file electronically using GST/HST NETFILE.

The builder will calculate and report their ITCs as follows:

1. The amount of the “gross” ITCs will be reported in a separate information field on Schedule B to the GST/HST NETFILE return. “Gross” ITCs are the ITCs that a registrant is entitled to claim before taking into account any ITC recapture;
2. The amount of recaptured ITCs will be reported in separate information fields on Schedule B: one field for recaptured ITCs for the provincial part of the HST in Ontario and another field for those in B.C.;
3. The net amount of ITCs (calculated by deducting recaptured ITCs from gross ITCs) will be reported in an information field on the schedule. This net amount can be claimed as an ITC in the GST/HST NETFILE return.

Failure to account for recaptured ITCs in the proper manner will generally result in interest and penalties.

Example 8

A builder that is a large business is a monthly filer that routinely acquires specified property in Ontario. Rather than claim the ITCs for this property in the GST/HST return for the reporting period in which the ITCs first become available, the builder waits until the end of its fiscal year and claims the ITCs at that point. It also recaptures the provincial portion of those ITCs at that point. The builder will generally be subject to interest and penalties in this situation because it should have recaptured the provincial portion of the ITCs in the reporting period when the ITCs first became available.

Generally, if a registrant fails to report recaptured ITCs in the proper reporting period, this is to be corrected through an amended return for that period.

Refer to Info Sheet GI-099, *Builders and Electronic Filing Requirements*, for more information on mandatory electronic filing, including other circumstances under which a builder is required to file an electronic return.

Option to use an Estimation/Instalment Approach

To simplify tax compliance, a large business is generally allowed to make an election to use an estimation, instalment and reconciliation approach to accounting for recaptured ITCs, referred to here

as the Estimation/Reconciliation Method. The election is filed with the CRA after the end of a large business’ fiscal year and applies for at least one year.

Under the Estimation/Reconciliation Method, for **each** province that has an RITC requirement, a large business will:

- estimate the amount of ITCs it will be required to recapture during a fiscal year (this amount cannot be less than the actual amount of ITCs it was, or would have been, required to recapture in its previous fiscal year);
- based on this estimate, make equal instalment payments of recaptured ITCs in each reporting period during a one-year period that begins three months **after** the beginning of the fiscal year and ends three months **after** the end of the fiscal year;
- at the end of the fiscal year, determine the actual amount of ITCs it would have been required to recapture during that year for each province with an RITC requirement; and
- report any differences between the estimated and actual amounts in its GST/HST return for a reporting period that includes a date that occurs within three months after the end of its fiscal year.

Example 9

A large business, Builder A, that is a monthly filer with a fiscal year ending on December 31 elects in January 2011 to use the Estimation/Reconciliation Method for its 2011 fiscal year. Builder A has \$8,400 of estimated RITCs for B.C. for that fiscal year, so Builder A divides this Estimated RITC amount by the 12 monthly reporting periods within the April 1, 2011 to March 31, 2012 instalment period, and reports \$700 in the recaptured ITCs field for B.C. in the GST/HST NETFILE return for each of those reporting periods.

Builder A reported \$600 of actual RITCs in its GST/HST returns for January, February and March, before it began using the Estimated/Reconciliation Method. The total amount reported for its 2011 fiscal year was \$8,100 [(\$600 x 3) + (\$700 x 9)].

In March 2012, Builder A determines that its actual RITCs were \$9,000 for its 2011 fiscal year. Builder A would report the additional \$900 (\$9,000 – \$8,100) in its GST/HST NETFILE return for the March 1-31, 2012 reporting period (in addition to the \$700 instalment payment for that same reporting period).

If the HST is only in effect for part of your fiscal year, the actual RITC amount for that fiscal year is to be adjusted to reflect the portion of the fiscal year during which the HST was in effect.

Therefore, under the Estimation/Reconciliation Method, a builder that is a large business must still identify the specified property and services that it acquires or brings into either Ontario or B.C. in such a way that it can determine the actual amount of available ITCs that are subject to the RITC requirement. However, this approach allows the builder to account for these recaptured ITCs on an annual basis and on the basis of complete financial information.

A builder that is a large business was generally able to elect to use the Estimation/Reconciliation Method before the introduction of the HST in Ontario and B.C. on July 1, 2010.

However, to simplify administration, no reconciliation can take place before April 2011. If a builder using the Estimation/Reconciliation Method has a fiscal year that ends after the implementation of the HST in July 2010 and before January 2011, it will be required to account for its reconciliation in the reporting period that includes April 1, 2011.

This info sheet does not replace the law found in *the Excise Tax Act* (the Act) and its regulations. It is provided for your reference. As it may not completely address your particular operation, you may wish to refer to the Act or appropriate regulation, or contact any CRA GST/HST Rulings Centre for additional information. A ruling should be requested for certainty in respect of any particular GST/HST matter. Pamphlet RC4405, *GST/HST Rulings – Experts in GST/HST Legislation*, explains how to obtain a ruling and lists the GST/HST Rulings Centres. If you wish to make a technical enquiry on the GST/HST by telephone, please call 1-800-959-8287.

If you are located in Quebec and wish to make a technical enquiry or request a ruling related to the GST/HST, please contact Revenu Québec by calling 1-800-567-4692. You may also visit their Web site at www.revenu.gouv.qc.ca to obtain general information.

All technical publications related to GST/HST are available on the CRA Web site at www.cra.gc.ca/gsthstech.