



# GST/HST Memoranda Series

## 19.4.2 Commercial Real Property—Deemed Supplies

August 1999

Notice of Change re 19.4.2 Commercial Real Property – Deemed Supplies.  
Paragraph 56, January 7, 2002

**Overview**

This memorandum examines the GST/HST treatment of capital real property. In particular, it examines the treatment of a deemed supply (a deemed sale or a deemed purchase) that results from a significant change in the extent of a registrant’s use of capital real property in commercial activities.

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**Disclaimer**

The information in this memorandum does not replace the law found in the *Excise Tax 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 a Canada Revenue Agency (CRA) GST/HST Rulings Centre for more information. These centres are listed in GST/HST Memorandum 1.2, *Canada Revenue Agency GST/HST Rulings Centres*. If you wish to make a technical enquiry on the GST/HST by telephone, please call the toll-free number 1-800-959-8287.

If you are located in the Province of Quebec, please contact Revenu Québec by calling the toll-free number 1-800-567-4692 for additional information.

### Capital property

**Definition**  
ss 123(1)

1. For GST/HST purposes, “capital property” in respect of a person, means property that is, or would be if the person were a taxpayer under the *Income Tax Act*, capital property of the person within the meaning of that Act, other than property described in Class 12, 14 or 44 of Schedule II to the *Income Tax Regulations*.

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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*Income Tax Act*

2. Capital property of a taxpayer is defined in section 54 of the *Income Tax Act* as
- “a) any depreciable property of the taxpayer, and
  - b) any property (other than depreciable property), any gain or loss from the disposition of which would, if the property were disposed of, be a capital gain or a capital loss, as the case may be, of the taxpayer.”
3. Of the property excluded from the definition of capital property under the GST/HST, Class 12 and Class 44 of Schedule II to the *Income Tax Regulations* generally would not include real property items. However, under restricted circumstances, rights to use real property supplied by way of licence or concession for a limited period could be included under Class 14 and thus not be considered as capital property for the purposes of the GST/HST.

Exclusions

4. Real property that is inventory (e.g., property acquired or held for the purpose of sale in the course of a business or in an adventure or concern in the nature of trade) is not considered to be capital property.

### Real property appropriated for use as capital property

Deemed sale and repurchases 196.1

5. If a registrant appropriates real property for use as capital property or to improve capital property of the registrant, and if immediately prior to the appropriation, the real property was neither capital property nor an improvement to capital property, the registrant is deemed to have self-supplied the property, i.e., deemed to have sold and repurchased the property. If the property was last acquired for consumption, use or supply in the course of commercial activities, the registrant is deemed to have collected tax calculated on the fair market value of the property at the time of the appropriation and to have paid tax, if the deemed acquisition is not an exempt supply. As a consequence of having been deemed to have paid tax, the registrant is entitled to claim an input tax credit (ITC) to the extent that the capital property or the improvement is for use in commercial activities.

Example

A developer who is a registrant owns several hectares that the developer has divided into lots for a housing development. The developer decides to appropriate three lots for offices of the development company as well as for equipment storage. By removing the three lots from inventory for use as capital property, the developer is deemed to have paid and collected tax calculated on the fair market value of the property at the time of the appropriation. Although in the return for the period the developer must account for the tax deemed collected, since the lots are being used as capital real property in the course of commercial activities of the registrant, the developer may claim an offsetting ITC on the same return in respect of the deemed acquisition to the extent the property is for use in commercial activities which in this case is 100%.

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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- subpara 196.1(b)(ii) 6. Effective April 1, 1997, if the property was not being used in commercial activities of the registrant before the appropriation, or if the supply is an exempt supply, the amount of GST/HST that the registrant is deemed to have paid is equal to the basic tax content of the property at the time of the deemed supply. Calculating the basic tax content of a property is explained in the discussion relating to beginning use in commercial activities. See paragraph 20.
- Before April 1997 7. Before April 1, 1997, if the property was not being used in commercial activities of the registrant before the appropriation, or if the supply was an exempt supply, the registrant was deemed to have paid tax in an amount equal to  $A \times B$ , where:
- A** was the lesser of
- actual tax payable in respect of the last acquisition or importation of the property by the registrant, and
  - tax calculated on the fair market value of the property at the time of the appropriation;
- and
- B** was 100% less the percentage of the rebate which the person was entitled to claim, if any, under section 259 (PSB rebate) in respect of the last acquisition or importation of the property.

### Change-in-use rules

- Capital personal property vs. capital real property 8. The change-in-use rules that affect capital real property are different from those that affect capital personal property. In general, ITC entitlements and the tax status of supplies, including deemed supplies arising from change in use, of capital personal property are dependent on the primary (more than 50%) use of the property. On the other hand, ITC entitlements and the tax status of supplies, including deemed supplies arising from change in use, of capital real property are dependent on the extent of the actual use (usually expressed as a percentage of the total use) of the property in commercial activities. (For a general discussion of ITCs and real property, see Memorandum 19.1, *Real Property and the GST/HST*.)
- General application 9. Generally, a registrant is entitled to claim ITCs for the GST/HST paid or payable on the acquisition of capital real property to the extent that the property is used in commercial activities. Beginning use of capital real property in commercial activities is deemed to be the same as receiving a supply of the property and except where the supply is an exempt supply, the registrant is deemed to have paid GST/HST on the supply. Increasing the extent of commercial use of capital real property by 10% or more is deemed to be the same as receiving a supply of a portion of the real property equal to the extent of the increase. Except where the supply is an exempt supply, the registrant is deemed to have paid GST/HST on the deemed acquisition of the portion of the property that changes from non-commercial to commercial use. The registrant can claim an ITC that is equivalent to the amount of deemed tax.

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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10. If a registrant reduces the extent to which the capital real property is used in commercial activities by 10% or more without ceasing commercial use, the registrant is deemed to have sold a portion of the capital real property equal to the extent of the decrease and to have collected GST/HST on that portion of the property no longer in commercial use. When a registrant ceases commercial use of capital real property or reduces the commercial use to less than 10% (this does not apply to financial institutions) and begins to use the property for other purposes, the whole of the property is deemed to have been sold and re-acquired with an accompanying collection/payment of deemed tax. The resulting tax liability has the effect of recapturing previously claimed ITCs and takes into account the current fair market value of the property where it has depreciated in value.

### Insignificant changes in use

Less than 10%  
s 197

11. If the extent to which a registrant changes the use of capital real property in commercial activities is less than 10% of the total use of the property, the registrant is deemed not to have changed the use of the property. However, small changes in the extent of use accumulate from the time of the last acquisition or last significant change of use of the capital real property. For example, a decrease of 5% in the use of capital real property in commercial activities followed by a second decrease of 5% would, taken together, produce a significant change in use. Ceasing to use capital real property in commercial activities is a significant change in use in all cases even if the extent of the change in use is less than 10%.

Rules for capital real  
property

12. Note that this rule regarding insignificant changes in use applies for purposes of subsections 206(2), 206(3), 206(5), 207(2), 208(2) and 208(3). These are the change-in-use rules for capital real property that apply to registrants other than a public sector body that is not a financial institution. Since a change-in-use of capital real property of a PSB<sup>1</sup> is dealt with under the change in use rules for capital personal property, i.e., the primary-use rules, this rule for insignificant changes does not apply to capital real property of a PSB. For example, if a change of 2% in the extent of use means that the primary use of the capital real property of a PSB is no longer in commercial activities, the change is significant for purposes of the change-in-use rules. Similarly, if a change of 25% in the extent of use does not affect the primary use of the property, the change is insignificant for purposes of the change-in-use rules.

ss 204(1)

13. On the other hand, changes in use of capital personal property of financial institutions having a cost to the financial institution of more than \$50,000 are treated as if the capital personal property were capital real property. Thus, the insignificant change-in-use rule under section 197 applies to such property.

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Footnote<sup>1</sup>

A “public sector body” means a government or a public service body. A “public service body” means a non-profit organization, a charity, a municipality, a school authority, a hospital authority, a public college or a university. The initials PSB used in this document refer to a public *service* body.

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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14. If the registrant is an individual and the extent of the change, however small, means that the capital real property of the individual commences to be used primarily for the personal use and enjoyment of the individual or a related individual, the rule in section 197 does not apply. For example, if an individual who is a registrant changes the use of capital real property by 5% and this amount of change means that in the reporting period in which the change occurs, the property begins to be used primarily (greater than 50%) for the personal use and enjoyment of the individual, the individual will be deemed under the provisions of section 207(1) to have ceased use of the property in commercial activities, with an accompanying collection/payment of deemed tax even though the overall change was less than 10%.

### Change-in-use rules for most persons

Change-in-use  
ss 206

15. The provisions that govern changes in the use of capital real property of most persons who are GST/HST registrants are contained in section 206 of the Act. A registrant, who is an individual or a public sector body that is not a financial institution, is not covered by these provisions. For information regarding individuals who are registrants, see paragraphs 41 to 53. For PSBs, see paragraphs 54 to 57. For information on special rules related to financial institutions, see paragraphs 37 to 40.

### • Beginning use in commercial activities

General case  
ss 206(2)

16. If a registrant, other than an individual or a public sector body that is not a financial institution, that last acquired capital real property for use in non-commercial activities begins to use the capital real property in commercial activities, the registrant is deemed under subsection 206(2) to have received a supply of the real property by way of sale. Except where the supply is an exempt supply, the registrant is deemed to have paid tax on the deemed acquisition.

17. Excluded from the operation of subsection 206(2) is a person who, while using capital real property in a commercial activity, becomes a registrant. This situation is dealt with under subsection 171(1) which contains certain rules that apply to persons becoming registrants. Under subsection 171(1), when a small supplier becomes a registrant, the person is deemed to have paid tax on all property the person is holding at that time for consumption, use or supply in the course of commercial activities. This allows the person to claim ITCs for tax that was previously non-recoverable. (ITCs and registration will be covered in Chapter 8, *Input Tax Credits—Eligible ITCs*, in the GST/HST Memoranda Series.)

Use in other activities  
ss 141(3)

18. Subsection 206(2) applies only if more than 10% of the use of the property is in commercial activities. If the use in commercial activities is 10% or less, the registrant is ineligible for an ITC on the property as a result of section 141 which deems that if the property is used 90% or more in activities that are not commercial activities, then none of the use is considered to be in commercial activities. (Note that section 141 does not apply to financial institutions.)

Tax deemed paid

19. Effective April 1, 1997, tax that is deemed to have been paid on the deemed acquisition under 206(2) is equal to the amount of the basic tax content of the property at the time of the deemed acquisition.

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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Definition: basic tax content ss 123(1)

20. The basic tax content of real property is determined by way of a formula. Simply stated, the basic tax content of a property is arrived at by:

- totalling all amounts of tax payable at the time the property was last acquired or imported<sup>2</sup>
- adding any amounts of tax payable at any time on improvements (goods and services) acquired, imported or brought into a participating province after the last acquisition or importation,
- deducting all amounts of tax recoverable by way of rebate, refund or remission (other than ITCs), and
- multiplying the net amount by a factor that takes into account any depreciation in the fair market value of the property since the property was last acquired.

Calculating basic tax content

21. For many registrants, the basic tax content of a property is calculated under the formula contained in paragraph (a) of the definition of basic tax content in subsection 123(1): (Note: this formula does not apply to selected listed financial institutions—see paragraphs 38 and 39, or to property brought into a participating province, i.e., a province where the HST applies: Nova Scotia, New Brunswick and Newfoundland—see paragraph 22):

$$(A - B) \times C$$

where

A = the total of:

- (i) tax payable on the claimant's last acquisition or importation of the property;
- (ii) tax payable in respect of improvements to the property acquired, imported or brought into a participating province after the property was last acquired or imported;
- (iii) tax that would have been payable in either of the preceding situations but for subsection 153(4)<sup>3</sup> or section 167<sup>4</sup> applying or the fact that the property or improvements were acquired by the claimant for consumption, use or supply exclusively in commercial activities;

and

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Footnote <sup>2</sup>

Importing in this context refers to importing items such as mobile homes or floating homes, or items that will be affixed to real property thus becoming part of it, such as fencing.

Footnote <sup>3</sup>

The provisions of subsection 153(4) apply where a supplier accepts property that is used tangible personal property (or a leasehold interest therein) as full or partial consideration for other tangible personal property.

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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- (iv) tax under section 218 and section 218.1 (tax payable on imported taxable supplies), and Division IV.1 (tax self-assessed on property brought into a participating province from a non-participating province) that the person would have been liable to pay if the property or improvement were not for consumption, use or supply exclusively in the course of commercial activities of the person;

**B** = the total of

- (i) any tax included in **A** (above) that the person was exempt from paying under any other Act or law;
- (ii) all amounts of tax referred to in **A(i)** and **A(ii)** above which the claimant was entitled to recover by way of a rebate, refund, or remission or would have been entitled to recover, if the property or improvement had been acquired for use exclusively in activities that are not commercial activities, other than ITCs and amounts referred to in **B(i)**;
- (iii) the amounts of tax referred to in **A(iii)** and **A(iv)** above which the claimant was entitled to recover by way of a rebate, refund, remission or otherwise under this or any other Act or law or would have been entitled to recover if the tax had been payable and the property or improvement had been acquired for use exclusively in activities that were not commercial activities, other than ITCs and amounts referred to in **B(i)**;

and

**C** = the lesser of 1, and

fair market value at the time the basic tax content is being determined  
consideration payable on the last acquisition + consideration for improvements.

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Footnote <sup>4</sup>

Under the provisions of section 167, an otherwise taxable sale of a business can be made without tax applying if both parties to the transaction so elect (form GST 44). Also under section 167, there can be a tax-free roll-over of the business assets of a deceased individual, if particular conditions are satisfied. For further discussion of section 167, see GST/HST Memorandum 19.4.1, *Commercial Real Property—Sales and Rentals*. When calculating the basic tax content of a property, even though tax had not applied to the last acquisition of the property because of section 167, an amount of tax is included. This amount is based on the fair market value of the property at the time of determining the basic tax content.

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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Example

Property Co. Ltd. bought an office building in Halifax, NS, in 1995 for \$200,000 plus \$14,000 GST. The property was used exclusively in exempt activities until August 1997, when the company spent \$8,000 plus \$1,200 HST to renovate the property for use partly in commercial activities. At the time of beginning use in commercial activities, i.e., at the time of the deemed acquisition, the fair market value of the property had decreased to \$180,000. The building is being used 40% in commercial activities. The company is entitled to an ITC that is equal to the deemed tax paid which is the proportion of the basic tax content of the building that reflects the extent of use in commercial activities at the time of the deemed acquisition:

ITC = deemed tax paid.

Deemed tax paid = basic tax content  $\times$  40%.

The basic tax content of the property at the time of the deemed acquisition is:

$$\begin{aligned} & (A - B) \times C \\ & = ((\$14,000 + \$1,200) - 0) \times \text{the lesser of 1 and } \frac{\$180,000}{\$200,000 + \$8,000} \\ & = \$15,200 \times \text{the lesser of 1 and } .865 \\ & = \$13,148. \end{aligned}$$

Accordingly, the company may claim an ITC of \$5,259.20 (i.e., \$13,148  $\times$  40%).

Basic tax content:  
paragraph (b)  
Brought into a  
participating province

22. The method for calculating basic tax content varies if the property was brought into a participating province from a non-participating province. In this case, paragraph (b) of the definition of basic tax content applies. In all other cases (for example, property that was last acquired in a participating province, or property that was brought into a non-participating province), paragraph (a) applies when determining the basic tax content.

Example

If property is purchased in a non-participating province for \$10,000 and GST of \$700 is payable on the purchase, the basic tax content of the property immediately after the purchase is \$700. Assuming the property is for use exclusively in commercial activities, the registrant would be entitled to an ITC of \$700. If the property is later brought into a participating province for use exclusively in commercial activities at a time when its fair market value is \$5,000, under paragraph (b) of the definition, the basic tax content is the total of

- the basic tax content of the property immediately before the property was brought into the province, which in this example is \$350 ( $(\$5,000/\$10,000) \times \$700$ ), plus
- the tax that is payable on bringing the property into the province which in this example is \$400 ( $8\% \times \$5,000$ ).

The registrant would be entitled to an additional ITC of \$400. Thus, the basic tax content will be \$750. If the registrant ceases using the property in commercial activities soon after it is brought in, the registrant would be required to pay tax under the capital property change-in-use rules equal to the basic tax content of \$750.



## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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Before April 1997

23. Before April 1, 1997, an ITC for a deemed acquisition under subsection 206(2) was calculated as:

$$A \times B$$

where

**A** was the lesser of

(i) actual tax payable by the registrant on the last acquisition and subsequent improvements to the property, and

(ii) 7% of the fair market value of the property at the time of the change-in-use;

**B** was 100% less the prescribed percentage of the rebate available to a PSB under section 259, if any, in respect of tax payable on the last acquisition and subsequent improvements to the property (Note: the PSB must have elected under section 211 to treat an exempt supply of real property as a taxable supply).

24. If the fair market value of the property at the time of the change-in-use had increased since the last acquisition of the property, the ITC would be limited to the percentage of actual tax payable in respect of that portion of the property that was used or supplied in commercial activities. In cases where the fair market value of the property at the time of the change-in-use was less than the value on which GST had applied, the ITC would have been restricted to a lesser amount.

- **Increasing use in commercial activities**

General case  
ss 206(3)

25. If a registrant—other than an individual or a public sector body which is not a financial institution—that is currently using capital real property in commercial activities increases by at least 10% the extent to which that property is used in commercial activities, the registrant is deemed to have received a supply of the portion of the property that changes from non-commercial use to commercial use. Except where the deemed supply is an exempt supply, the registrant is deemed to have paid tax in respect of the supply. The registrant may claim an ITC equal to the amount of tax deemed paid on the deemed supply.

26. Effective April 1, 1997, the amount of tax that the registrant is deemed to have paid at the time of the deemed supply is determined by the formula

$$A \times B$$

where

**A** is the basic tax content of the property immediately before the time of the deemed supply, and

**B** is the extent (expressed as a percentage of the total use of the property by the registrant at the time of the deemed supply) to which the registrant increased the use of the property in commercial activities of the registrant.

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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### Example

For example, Property Co. Ltd. cited in the earlier example increases the use of its building from 40% in commercial activities to 75%. The fair market value of the property has increased from \$180,000 to \$225,000 immediately before this change in the extent of use. Accordingly, the company's deemed tax paid arising from the increase in use of the real property in commercial activities is 35% of the basic tax content at the time of the deemed acquisition:

$$\text{basic tax content (using the formula given in paragraph 21)} = (\mathbf{A} - \mathbf{B}) \times \mathbf{C}$$

$$= \$15,200 \times \text{the lesser of 1 and } \frac{\$225,000}{\$200,000 + \$8,000}$$

$$= \$15,200 \times \text{the lesser of 1 and 1.082}$$

$$= \$15,200.$$

$$\text{Deemed tax paid} = \$15,200 \times 35\% = \$5,320.$$

Accordingly, the company may claim an ITC of \$5,320.

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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- Before April 1, 1997
27. Before April 1, 1997, the amount of tax that was deemed to have been paid was equal to the amount determined by the formula  $A \times B \times C$ , where:
- A was the lesser of
    - (i) actual tax payable (or would, but for section 167 have been payable) on the last acquisition and subsequent improvements to the property, or
    - (ii) 7% of the fair market value of the property immediately before the increase in the extent of use;
  - B was the percentage increase in use of the property in commercial activities; and
  - C was 100% less the prescribed percentage of the rebate available to a PSB under section 259, if any, in respect of any tax payable on the property (Note: the PSB must have elected under section 211 to treat an exempt supply of real property as a taxable supply).

- **Ceasing use in commercial activities**

- General case  
ss 206(4)
28. Where a registrant (other than an individual or a public sector body which is not a financial institution) last acquired real property for use as capital property in commercial activities and then begins to use that property exclusively for other purposes, the registrant is deemed to have sold and reacquired the property and, except where the supply is an exempt supply, to have collected and paid GST/HST. For persons other than financial institutions and PSBs which have not made an election under section 211, this deemed sale occurs immediately before the time the registrant begins to use the real property 90% or more for other purposes.
- Amount of deemed tax
29. The amount of GST/HST that the registrant is deemed to have paid and collected at the time of the deemed sale is equal to the basic tax content of the property at the time of the deemed sale.
- Example
- Property Co. Ltd. cited in the earlier examples ceases using its building in commercial activities in June 1998. The fair market value of the property at that time is \$215,000. Accordingly, the amount of tax the company is deemed to have collected when it begins to use the property 90% or more for non-commercial purposes is equal to the basic tax content in June 1998:
- Basic tax content =  $(A - B) \times C$
- =  $(\$15,200 - 0) \times \text{the lesser of 1 and } \frac{\$215,000}{\$200,000 + \$8,000}$
- =  $\$15,200 \times \text{the lesser of 1 and 1.033}$
- = \$15,200.

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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Thus, the company's deemed tax collected at the time of the deemed sale is \$15,200. The company is required to account for this tax on its return for the reporting period when the deemed sale occurs.

Before April 1997

30. Before April 1, 1997, the tax liability was calculated as follows:

$$(A \times B \times C) + (D \times (100\% - B) \times E)$$

where

- A** was 7% of the fair market value of the property at the time that the property began to be used exclusively otherwise than in commercial activities,
- B** was the percentage use of the property in commercial activities immediately before that time,
- C** was 100% less the prescribed percentage of the rebate available to a PSB under section 259, if any, in respect of tax payable on the property before beginning or ceasing use of the property in commercial activities (Note: the PSB must have elected under section 211 to treat an exempt supply of real property as a taxable supply),
- D** was the lesser of actual tax payable (or that would have been payable but for section 167) by the registrant on the last acquisition and subsequent improvements to the property and 7% of the fair market value of the property at that time, and
- E** was 100% less the prescribed percentage of the rebate available to a PSB under section 259, if any, in respect of tax payable on the last acquisition or improvement to the property (Note: the PSB must have elected under section 211 to treat an exempt supply of real property as a taxable supply.)

ITC  
193(1)

31. If the last acquisition of the capital real property was a taxable supply and if the property was not used exclusively as capital property in commercial activities, some tax may remain embedded in the cost of the property. To prevent cascading of tax at the time of the deemed sale, i.e., when the registrant begins to use the property for purposes other than as capital property in commercial activities, the registrant may claim an ITC under subsection 193(1) for the lesser of the previously uncredited or unrebated tax embedded in the cost of the property and the tax paid or payable arising from the deemed sale. (For information on calculating a real property credit, see Memorandum 19.2.3, *Residential Real Property—Deemed Supplies*.)

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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- **Reducing use in commercial activities**

General case  
ss 206(5)

32. Effective April 1, 1997, if a registrant (other than an individual or a public sector body which is not a financial institution) reduces the commercial use of capital real property by 10% or more without ceasing commercial use, the registrant is deemed to have made a supply immediately before the decrease in use of the capital real property to the extent of the decrease in use. Consequently, the registrant is deemed to have collected the GST/HST on the deemed supply at the time of the decrease in commercial use. For purposes of calculating the net tax for the reporting period in which the deemed supply took place, the registrant calculates the amount of deemed tax collected according to the formula:

$$A \times B$$

where

**A** is the basic tax content of the property at the time of the decrease in use in commercial activities; and

**B** is the extent (expressed as a percentage of the total use of the property by the registrant at the time of the decrease in use in commercial activities) to which the registrant reduced the use of the property in commercial activities.

Example

If Property Co. Ltd. cited in the previous examples did not cease using its building in commercial activities in June 1998, but instead reduced the commercial use from 75% to 35%, the tax deemed collected on the deemed supply would have been equal to 40% of the basic tax content of the building. The fair market value of the property at the time was \$215,000.

$$\text{Basic tax content (see paragraph 21)} = (A - B) \times C$$

$$= (\$15,200 - 0) \times \text{the lesser of 1 and } \frac{\$215,000}{\$200,000 + \$8,000}$$

$$= \$15,200 \times \text{the lesser of 1 and 1.033}$$

$$= \$15,200.$$

Thus, Property Co. Ltd.'s deemed tax collected at the time of the deemed sale is  $(\$15,200 \times 40\%) = \$6,080$ . The company is required to account for this tax on its return for the reporting period when the deemed sale occurs.

No ITC

33. Note that an ITC under section 193 (real property credits) is not available in respect of a taxable supply which is deemed to have occurred under subsection 206(5) (reducing use in commercial activities).

Before April 1997  
ss 206(5)

34. Before April 1, 1997, a reduction in the extent to which capital real property was used in commercial activities, without ceasing use, generally resulted in a recapture of ITCs previously claimed unless 7% of the fair market value of the property was less than the GST that had applied on the last acquisition and subsequent improvements to the property.

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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35. Under this earlier version of the change-in-use rules governing reducing use in commercial activities, there was a deemed supply of the property proportional to the extent of the decrease in use of the property in commercial activities immediately before the time of reduced commercial use. The registrant was deemed to have made a supply and, and except where the supply was an exempt supply, to have collected tax in respect of the deemed supply. The formula for determining the amount of tax deemed collected by a registrant in this case was:

$$A \times B \times C$$

where

**A** was the lesser of

- (i) actual tax payable (or that would have been payable by the registrant but for section 167) on the last acquisition and subsequent improvements to the property, or
- (ii) 7% of the fair market value of the property at the time of the decrease in use of the property in commercial activities,

**B** was the percentage decrease in use of the property in commercial activities at that time,

**C** was 100% less the prescribed percentage of the rebate available to a PSB under section 259, if any, in respect of tax payable on the property before reducing use of the property in commercial activities (Note: the PSB must have elected under section 211 to treat an exempt supply of real property as a taxable supply).

No ITC  
para 193(1)(a)

36. Under the provisions of section 193 (real property credits), an ITC could not have been claimed.

### Change-in-use rules for financial institutions

ss 204(2)

37. Financial institutions are subject to the same change-in-use provisions in section 206 as most other registrants. However, there are three differences:

ss 204(1)  
ss 205(1)

- Capital personal property of a financial institution having a cost to the institution of more than \$50,000 is treated as if it were capital real property. Moreover, where a registrant has made an election under subsection 150(1) to have transactions with other members of a closely related group treated as exempt supplies and, as a result of making that election, the registrant ceases to use the property in commercial activities, or reduces the use of the property in commercial activities, the rules for a real property credit in subsection 193(1) and the change-in-use rules contained in subsections 206(4) and (5) apply to all capital personal property without reference to the \$50,000 threshold as if the property were real property.

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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Ceasing use  
ss 206(4)

- A registrant is deemed to have ceased using capital real property in commercial activities when the registrant begins to use the property exclusively for other purposes. For most registrants, “exclusively” means 90% or more; for a financial institution, “exclusively” means 100%.

Basic tax content

- Financial institutions that are selected listed financial institutions have a different formula for calculating “basic tax content”.

Selected listed financial  
institution  
ss 225.2(1)

38. Generally, a selected listed financial institution is a listed financial institution that is required, or would be so required if it had taxable income, to allocate taxable income (or income, in the case of an individual, the estate of a deceased individual or a trust) for income tax purposes between at least one participating province and at least one non-participating province during the current taxation year and the immediately preceding taxation year. (For specific information on how to determine if a person is a selected listed financial institution and the special attribution method that it must use to allocate taxable income, see Technical Information Bulletin B-083R, *Financial Services Under the HST*.)

Calculating basic tax  
content

39. When applying the change-in-use rules in section 206, the selected listed financial institution must determine the basic tax content of the capital real property at the time of the deemed sale or deemed purchase. To calculate the basic tax content, the selected listed financial institution must make an adjustment to the provincial component of the HST that became payable by the institution while it was a selected listed financial institution. In effect, to calculate the basic tax content at the time of a change-in-use, the institution calculates the federal component of the HST and adds an adjusted amount as the provincial component. The adjustment to the provincial component of the HST is determined by the formula:

$$D \times E \times F/G$$

where

**D** is the GST or the federal component of the HST paid or payable for the property;

**E** is the percentage for a participating province determined for the purposes of the special attribution method;

**F** is 8% (the provincial component of the HST); and

**G** is 7% (the federal component of HST).

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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Example

The Dollar Trust Co. Ltd. located in Moncton, NB, acquires an office building for \$2,000,000 plus HST (HST @ 15% = \$300,000) in a taxation year for which its total prescribed percentage (for purposes of the special attribution method) for participating provinces is 10%. The basic tax content of the building is calculated as follows:

HST paid on the acquisition of the building: \$300,000

Basic tax content =

Federal component of HST:  $7\% \times \$2,000,000 = \$140,000$

Plus:

$D \times E \times F/G =$

where:

$D =$  Federal component (\$140,000)

$E = 10\%$

$F = 8\%$

$G = 7\%$

$\$140,000 \times 10\% \times (8\% \div 7\%) =$

$\$14,000 \times 1.143 =$  \$16,000

Basic tax content: \$156,000

Credits  
ss 204(3)

40. The financial institution may be able to claim credits under subsection 193(1) for the disposition or the deemed disposition of capital personal property (other than a passenger vehicle) as if the property were real property if that property has a cost to the institution of more than \$50,000 or if the institution is party to an election under subsection 150(1) (see paragraph 37).

### Change-in-use rules for individuals

Acquisition of capital  
real property by  
individual  
ss 208(1)

41. If an individual who is a registrant acquires real property for use as capital property of the registrant and uses the property primarily (more than 50%) for his or her own personal use and enjoyment or that of a related individual, the individual cannot claim an ITC for tax payable in respect of the acquisition of the property.



## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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- Example  
An individual who is a registrant has purchased a residential complex that is a detached house with four bedrooms. Two bedrooms are used as part of a bed and breakfast operation that takes up 35% of the total area of the home. The individual uses the remaining 65% of the area of the home as the individual's primary place of residence. In this situation, no ITC is available in respect of the acquisition cost of the residential complex or improvements to it. However, ITCs may be available in respect of operating costs related to the commercial activity of the bed and breakfast operation if all the requirements for such ITCs are met.
- Improvement to capital real property ss 208(4)  
42. If an individual acquires, imports, or brings into a participating province an improvement to capital real property, the individual may claim an ITC for tax paid or payable in respect of the improvement if the improvement is used primarily in commercial activities. However, the ITC may not be claimed if the real property at the time tax becomes payable or is paid without having become payable is primarily for the personal use and enjoyment of the individual or a related individual. If the improvement results in a change in the extent of use of the property in commercial activities, the individual may be subject to a tax liability (i.e., for decreasing or ceasing use) or eligible for ITCs (i.e., beginning or increasing use) in respect of the entire property.
- Beginning use ss 208(2)  
43. If an individual registrant begins using real property of the registrant individual as capital property in commercial activities and is no longer using it primarily for the individual's personal use and enjoyment or that of a related individual, the change-in-use provisions apply. The individual is deemed to have received a supply of the entire property by way of sale. Except where the supply is an exempt supply, the individual is deemed to have paid GST/HST on the deemed purchase. An ITC would be available to the registrant to the extent the property is used in commercial activities.
- Basic tax content  
44. Effective April 1, 1997, the amount of GST/HST deemed paid under subsection 208(2) is equal to the basic tax content of the property at the time of the deemed sale. (An example of calculating basic tax content is given in paragraph 21.)
- Example 1  
An individual who is a registrant restores old cars as a hobby. The individual owns a lot and a garage that are used in this hobby. The individual decides to start a business of restoring old cars. The garage and lot are used to store and work on the vehicles. The individual continues to store and work on personal vehicles, however 75% of the property is now being used in commercial activities.
- In this case, the individual is deemed to have received a supply of the entire property by way of sale. The amount of tax deemed paid on the sale is equal to the basic tax content of the property at the time of the deemed sale. The individual is entitled to claim an ITC equal to 75% of the tax deemed paid.
- Note: Even though an individual who begins using capital real property less than 100% in commercial activities is deemed to have paid tax on the entire property, there is no tax remittance with respect to the portion of the property not used in commercial activities. A person is required to remit (or account in net tax) any amount collected as tax. Under this subsection, no amount is deemed collected as tax.

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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Example 2

An individual who is a registrant and proprietor of a construction business decides to locate the office of the construction business in an addition to the individual's home. The home has an area of 200 square metres. The office addition measures 50 square metres. The individual also tears down the existing garage and replaces it with one that has room for a truck used in the business as well as the individual's personal car.

In this instance, because the property is still used primarily (more than 50%) for the personal use and enjoyment of the individual (assuming the number of square metres used for personal use and non-personal use reasonably reflects the extent to which the property is used in commercial activities), there is no change in use. As a result, the individual is not entitled to claim ITCs in respect of the property.

Before April 1, 1997

45. Before April 1, 1997, the amount of tax deemed to have been paid on a deemed sale occurring when a registrant begins using real property of the individual as capital property was equal to the lesser of the actual tax payable by the individual on the last acquisition of the property plus tax payable on subsequent improvements to it, and 7% of the fair market value of the property at the time of the deemed sale.

Increasing use  
ss 208(3)

46. If a registrant individual who is currently using capital real property in commercial activities increases by at least 10% the extent to which that property is used in commercial activities, the individual is deemed, for purposes of determining an ITC, to have received a supply of that portion of the property which changed from non-commercial use to commercial use. The individual is also deemed to have paid tax in respect of the supply. Accordingly, the registrant may claim an ITC equal to the amount of tax deemed paid on the deemed supply.

47. Effective April 1, 1997, the amount of tax that the individual is deemed to have paid at the time of the deemed supply is determined by the formula

$$A \times B$$

where

**A** is the basic tax content of the property at the time of the deemed supply, and

**B** is the extent (expressed as a percentage of the total use of the property by the registrant individual at the time of the deemed supply) to which the registrant increased the use of the property in commercial activities of the registrant.

Example

A registrant individual in an earlier example operates a car restoration business. The individual's use of the capital real property is 75% in commercial activities and 25% for personal use and enjoyment. The individual decides to eliminate any personal use of the property and starts to use it 100% in commercial activities. In this case, the individual would be entitled to claim an ITC equal to 25% of the basic tax content of the property at the time of the increase in use. (For an example of calculating basic tax content and the resulting ITC, see paragraph 26.)

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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Ceasing use  
ss 207(1)

48. A registrant who is an individual incurs a tax liability if the individual ceases, or in certain cases, reduces the extent to which capital real property is used in a commercial activity. If the individual ceases to use capital real property in a commercial activity and begins to use the property exclusively (90% or more) for other purposes or begins to use the property primarily (more than 50%) for the individual's or a related individual's personal use and enjoyment, the registrant is deemed to have sold the property immediately before the change in use. Except where the supply is an exempt supply, the individual is deemed to have collected tax on the deemed sale.

49. Effective April 1, 1997, the amount of tax deemed collected is calculated as:

**A - B**

where

**A** is the basic tax content of the property at the time of the deemed sale, and

**B** is the tax, if any, the individual is deemed to have collected under the self-supply provisions in section 190. (For information on the operation of the self-supply rules under section 190, see Memorandum 19.2.3, *Residential Real Property—Deemed Supplies*.)

50. Before April 1, 1997, tax deemed collected under subsection 207(1) was calculated as:

**(A × B) + (C × (100% - B)) - D**

where

**A** was the tax calculated on the fair market value of the property at the time of the deemed sale,

**B** was the extent of use of the property in the commercial activities of the individual immediately before the deemed sale expressed as a percentage of the total use of the property by the individual immediately before the deemed sale,

**C** was the lesser of

(i) the total of the tax that was or would, but for section 167, have been payable by the individual in respect of the last acquisition of the property by the individual and the tax that was payable by the individual in respect of improvements to the property acquired or imported by the individual after the property was last so acquired, and

(ii) tax calculated on the fair market value of the property at the time of the deemed sale, and

**D** was the tax, if any, that the individual is deemed under section 190 to have collected at the time of the deemed sale in respect of the property.

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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Reducing use  
ss 207(2)

51. If the registrant individual reduces the extent to which capital real property is used in commercial activities without ceasing to use it in commercial activities and without beginning to use it primarily for the individual's or a related individual's personal use and enjoyment, a tax liability is incurred. This deemed tax collected must be accounted for when determining the individual's net tax. The individual is deemed to have sold immediately before the change in use that portion of the property that changed from commercial use to non-commercial use. Except where the supply is an exempt supply, the individual is deemed to have collected tax on the sale.

52. Effective April 1, 1997, the amount of tax deemed collected is equal to the amount determined by the formula:

$$(A \times B) - C$$

where

**A** is the basic tax content of the property at the time of the deemed supply,

**B** is the extent of the reduction in use of the property in commercial activities expressed as a percentage of the total use, and

**C** is the tax, if any, that the individual is deemed under section 190 to have collected at the time of the deemed supply.

53. Before April 1, 1997, the amount of tax deemed collected was determined by the formula:

$$(A \times B) - C$$

where

**A** was the lesser of

(i) the total of the tax that was or would, but for section 167, have been payable by the individual in respect of the last acquisition of the property by the individual and the tax that was payable by the individual in respect of improvements to the property acquired or imported by the individual after the property was last so acquired, and

(ii) tax calculated on the fair market value of the property at the time of the deemed supply,

**B** was the extent (expressed as a percentage of the total use of the property by the individual at the time of the deemed supply) to which the individual reduced the use of the property in commercial activities of the individual at the time of the deemed supply, and

**C** was the tax, if any, that the individual is deemed under section 190 to have collected at the time of the deemed supply in respect of the property.

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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### Change-in-use rules for public service bodies (PSBs)

Certain public sector  
bodies  
s 209

54. Under the provisions of section 209, the basic rules for capital real property of
- a PSB which is a registrant other than a financial institution or a government, or
  - a specified Crown agent which is a registrant (see paragraph 55) other than a financial institution

are those of subsections 199(2) to (4) and 200(2) to (4). These are the change-in-use rules for capital personal property. Accordingly, these PSBs and specified Crown agents treat capital real property as though it were capital personal property. This means they may only claim ITCs in respect of the GST/HST paid or payable on acquisitions of capital real property that they use primarily (more than 50%) in commercial activities. If the capital real property is not for use primarily in commercial activities, there is no eligibility for ITCs.

55. Currently, specified Crown agents are the agents of the federal government that are prescribed under the *Crown Agents (GST/HST) Regulations*. To the extent that these agents are engaged in commercial activities, they follow the same rules as do private businesses in relation to the claiming of ITCs to recover tax on purchases. As well, they follow the same rules as other businesses with respect to the treatment of sales of property in respect of which no ITC was claimed. Accordingly, specified Crown agents are excluded from the rule under new subsection 200(4), which provides that all sales of capital property (both real and personal) of governments are taxable. For specified Crown agents, like other registrants, if such property were not used primarily in a commercial activity, it would not be taxable on resale.

56. Effective December 11, 1998, the provisions of the Act that apply to specified Crown agents of the federal government also apply to certain provincial Crown agents. The provincial Crown agents that come under the provisions applying to specified Crown agents are those that pay tax on their purchases without invoking their constitutional immunity from taxation because of an agreement entered into by the government of the province and the federal government under section 32 of the *Federal-Provincial Fiscal Arrangements Act*. There could also be provincial Crown agents that are prescribed as specified Crown agents, however, at the time of issuing this Memorandum, none has been prescribed.

Election  
s 211

57. Most supplies by way of sale, lease, licence or similar arrangement of real property by PSBs other than charities are exempt under section 25 of Part VI of Schedule V. Most supplies by way of sale, lease, licence or similar arrangement of real property by charities are exempt under section 1 of Part V.1 of Schedule V. A PSB (including a charity) may elect on a property by property basis to have supplies of real property not be exempt. If this election, *Real Property of a Public Service Body* (form GST 26), is in effect, such supplies in most cases are taxable and, as such, ITCs may be available. Also, the general change-in-use rules, i.e., those in section 206, apply for the real property of the PSB for which this election has been made, rather than the change-in-use rules for capital personal property under section 209 (see paragraph 54). This election will be discussed in greater detail in Memorandum 19.6, *Supplies by Public Sector Bodies*.

Summary chart of change-in-use provisions

“Change-in-use” provisions

Type of registrant	Use of capital property in commercial activity	Section or subsection
<ul style="list-style-type: none"> <li>• a registrant, other than an individual or a public sector body (PSB) that is not a financial institution, or</li> <li>• a registrant financial institution as well as its capital personal property whose cost is more than \$50,000, or</li> <li>• a registrant PSB (including a charity) that has elected under section 211 in respect of a property</li> </ul>	begins use	ss 206(2)
	increases use	ss 206(3)
	ceases use	ss 206(4)
	reduces use	ss 206(5)
<ul style="list-style-type: none"> <li>• a registrant individual</li> </ul>	acquires capital property, begins use or increases use	s 208
	ceases use or reduces use	s 207
<ul style="list-style-type: none"> <li>• a registrant PSB which is not a financial institution or a government and which has not elected under section 211, or</li> <li>• a registrant, specified Crown agent which is not a financial institution</li> </ul>	change-in-use	s 209

**Self-supply vs. change-in-use**

58. Both the self-supply rules and the change-in-use rules give rise to a tax liability on the part of the registrant. However, there are important differences between these sets of rules. The following table illustrates the differences between the self-supply rules and the change-in-use rules:

Summary comparison

<b>Self-supply rules apply</b>	<b>Change-in-use rules apply</b>
to real property transactions of builders and developers of residential-use real property (e.g., newly developed residential trailer parks, newly constructed or substantially renovated housing)	to transactions involving all capital real property
to all such builders and developers whether or not they are registrants or non-registrants for GST/HST	to GST/HST registrants only
generally only once to a property	any number of times to capital real property
generally only to residential-use real property	to any commercial-use capital real property

Exclusive events  
s 195.1

59. Under the self-supply rules<sup>5</sup> in section 191, builders of a residential complex or an addition to a multiple-unit residential complex are deemed to have sold and reacquired a newly constructed or substantially renovated residential complex at the time the complex is first rented or otherwise occupied as a place of residence (e.g., the first apartment is first rented in a newly constructed or substantially renovated apartment building). In the absence of any provision to the contrary, a registrant builder could be liable in such circumstances to pay tax twice—once under the self-supply rules and once under the change-in-use rules.

60. Section 195.1 ensures that the change-in-use rules do not apply at the same time as the self-supply rules by giving, in effect, priority to the self-supply rules. The residential complex, or the addition to the multiple-unit residential complex, is deemed under section 195.1 not to be capital property until the builder has self-supplied under section 191 or until the builder has received an exempt supply by way of sale of the property. In essence, the property is treated as inventory for supply in a commercial activity until it is deemed to be sold under section 191. The effect of this is to remove the possibility of tax applying twice on the same supply under these provisions.

Footnote<sup>5</sup>

For a discussion of the self-supply provisions, see Memorandum 19.2.3, *Residential Real Property—Deemed Supplies*.

## 19.4.2 Commercial Real Property: Deemed Supplies (continued)

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### Example 1

A builder constructs a multiple-unit residential complex. The builder decides to rent the units temporarily as places of lodging once they are completed for periods of occupancy of less than 30 days. The builder subsequently decides to rent the units as places of residence and is uncertain whether to self-assess tax under the provisions of subsection 191(3) (self supply of a multiple unit residential complex) or under the change-in-use provisions (beginning use in commercial activities).

In this case, until such time as the first unit is first rented as a place of residence, the provisions of section 195.1 deem the newly constructed multiple-unit residential complex not to be capital property of the builder. Once the first unit is rented as a place of residence, the builder is deemed under subsection 191(3) to have sold and reacquired the complex and to have collected and paid GST/HST on the deemed sale and re-acquisition.

### Example 2

A person converts a hotel that is not a residential complex into a rooming house. As a result of this conversion, the property becomes a residential complex. The residential units in the rooming house are leased for periods of continuous possession or use of more than one month. The renovations undertaken for the conversion are not extensive enough to be classed as a substantial renovation of the building. When leasing the first unit of the rooming house, the person is uncertain whether he/she is required to self-assess tax under subsection 191(3) (self supply of a multiple unit residential complex) or under the change-in-use provisions (ceasing use in commercial activities).

Because the rooming house is neither newly constructed nor substantially renovated, an analysis of this situation might first suggest that the person is not required to self-supply under subsection 191(3). It could also suggest that the change-in-use provisions governing ceasing use in commercial activities apply.

However, subsection 190(1) (conversion to residential complex) applies in this case and under paragraph 190(1)(d) deems the person to have substantially renovated the residential complex. The person is also deemed to be the builder of the complex under paragraph 190(1)(f). Consequently, subsection 191(3) applies. Since the provisions of section 195.1 deem the property not to be capital property of the builder from the time of the conversion until after the deemed builder either receives a taxable supply under 191 or receives an exempt supply of the complex, the change-in-use provisions governing ceasing use in commercial activities do not apply.

All GST/HST memoranda and other Revenue Canada publications are available on Internet at the Revenue Canada site <http://www.rc.gc.ca/> under the heading "Technical Information" in "General Information".



**19.4.2 Commercial Real Property: Deemed Supplies (continued)**

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