

GST/HST Policy Statement

Please note that the following Policy Statement, although correct at the time of issue, may not have been updated to reflect any subsequent legislative changes.

P-168R	The entitlement of municipalities to claim input tax credits in respect of the GST/HST incurred for infrastructure development relating to sales of serviced lots
Date of Issue	June 29, 2004. This policy statement replaces the draft Policy Statement P-168, dated January 17, 1995.
Subject	The entitlement of municipalities to claim input tax credits in respect of the GST/HST incurred for infrastructure development relating to sales of serviced lots
Legislative Reference(s)	Sections 141.01 and 169 of the <i>Excise Tax Act</i> (the Act) and Part VI of Schedule V to the Act
National Coding System File Number(s)	11895-5 et 11950-5
Effective Date	January 1, 1991 for GST and April 1, 1997 for HST

Issue and Decision

Municipalities may sell developed lots in direct competition with commercial developers. In the case of infrastructure development related to the sale of serviced lots by municipalities, the GST/HST incurred could be considered related to the supply of exempt municipal services, for example under sections 21 and 22 of Part VI of Schedule V, and as such ITCs would not be available. The Canada Revenue Agency (CRA) will permit certain ITCs to be claimed by municipalities for GST/HST incurred on the cost of basic infrastructure within the development, such as streets, curbs and gutters, and sewerage, drainage and water lines, provided it can be clearly established that the infrastructure costs are directly related to activities of the municipality of carrying out a development project in the same manner as a commercial developer.

In addition, the costs incurred must be the same as, or very similar to those that would normally be borne by a commercial developer selling serviced lots under an approved plan of subdivision. In making this determination, the following considerations would apply:

1. The development project is carried out by the municipality in the same manner as a commercial developer, including going through the requisite approval process.
2. To be considered as carrying out the development project in the same manner as a commercial developer, the municipality must not claim any rebate under section 259 of the Act in respect of the development project for which ITCs are otherwise available in accordance with either the Act or this policy. In addition, the consideration that would be

charged by the municipality for the sale of the serviced lots must be based on factors similar to those that a commercial developer would apply under similar circumstances, including recovery of all of the costs of the relevant infrastructures from purchasers of the property and an applicable profit margin based on competitive sale values. In this regard, it is the CRA's view that, at the time of the approval of subdivision, the estimated sale price of the serviced lots based on fair market values must be greater than the land value and estimated infrastructure costs at the start of the development.

3. The full consideration for the sale of all serviced lots within the subdivision must be subject to GST/HST and there is no direct recovery of costs related to the infrastructure through the imposition of tax-exempt lot levies, property taxes and/or special fees by the municipality. This may require the filing of a section 211 election to ensure that the supply is not otherwise exempt under section 25 of Part VI of Schedule V.

Provided these requirements are met, the CRA will allow a municipality to claim ITCs for the GST/HST incurred for basic infrastructure development, but only for those infrastructures within the geographical area of the subdivision development plan during the development stage and only to the extent that would otherwise be allowed in accordance with the Act if the ITCs were claimed by a commercial developer (e.g., the documentary requirements must be met). This policy does not apply to allow ITCs in respect of infrastructures, such as the widening of roads or construction of access roads outside of the subdivision development plan in question.

Where a commercial developer would otherwise receive compensation or reimbursement from a municipality for certain infrastructures, such amount would not normally be included in determining the infrastructure costs to be recovered from purchasers in the sale price of the property. Therefore, no ITCs would be available to a municipality in respect of the GST/HST related to infrastructures to the extent the cost of such infrastructures is normally reimbursed or compensated by the municipality to a commercial developer. For example, where a commercial developer is required by the municipality to provide sewerage lines within its development but is fully reimbursed for the costs by the municipality, the municipality would not be eligible to claim ITCs where it provides sewerage lines within its own development. Similarly, where the infrastructures are considered "oversize" (i.e., in excess of immediate requirements for the development area), the municipality is not eligible to claim ITCs on the GST/HST costs related to the oversize costs under this policy, if the municipality normally pays or reimburses a commercial developer for such oversize costs.

Once the infrastructure installation is complete, the municipality is subject to the normal public sector body rules provided by the Act. As a result, any GST/HST costs for the improvement, repair, maintenance, and other associated costs relating to the infrastructures after such time will not be eligible for ITCs.

Further, where infrastructure ownership is retained by the municipality and the infrastructure is used in exempt activities of the municipality, the municipality is required to apply change of use rules to the value of the infrastructure at the time the subdivision development is complete. Unlike a commercial developer who does not normally retain ownership of the infrastructure, the municipality is subject to recapture of ITCs when it begins to use the infrastructure it owns in providing exempt municipal services. The amount of ITCs to be recaptured will depend on the scrap value of the infrastructures and whether there are any infrastructure costs that are not recoverable by the municipality in the sale price of the serviced lots (based on fair market value) at the time of the completion of the development.

For purposes of this policy, the fair market value of the infrastructures and related land at the time of the completion of the development will be considered to be the greater of the following amounts:

the scrap value

or

A - B

where

A is the value of the land prior to the development plus the total amounts incurred for the relevant infrastructures, and

B is the fair market value of the lots to be sold by the municipality immediately after the development is complete.

The scrap value is determined by commonly accepted appraisal standards, which are generally based on the fair market value of the infrastructure at the time of the completion of the development.

For example, if the value of the land prior to development and the total amount incurred for infrastructure development in respect of the land amounted to \$500,000, but the fair market value of the lots to be sold by the municipality after development was \$400,000 (perhaps because of an unanticipated decline in market values), the municipality is subject to recapture of ITCs on the greater of \$100,000 or the scrap value. (Note that the estimated sale price of the serviced lots based on fair market value must have originally been expected to exceed the costs of \$500,000 at the start of the development in order for the municipality to be considered as undertaking the development as a commercial developer.)

If the municipality decides not to sell the serviced lots, additional amounts of ITCs may be recaptured at the time such lots are no longer held for the purpose of sale. Failure to account for the applicable amount of ITC recaptured in respect of the change of use at the appropriate time may impact on the initial allowance of the ITCs.

Example

Facts

1. The municipality of XYZ (herein referred to as "XYZ") plans to subdivide land owned by the municipality for the purpose of selling serviced lots.
2. XYZ is registered for GST/HST and has filed an election pursuant to section 211 of the Act in respect of the entire parcel of land described in the plan of Subdivision A.
3. XYZ has followed the requisite approval process for the subdivision in the same manner, as would a commercial developer.

4. In undertaking the development, XYZ has conducted a feasibility study which has determined that the estimated sale price of all serviced lots within the proposed subdivision, based on fair market values, will be greater than the applicable land value and the estimated infrastructure costs of the development of Subdivision A.
5. To date, XYZ has not claimed any rebates under section 259 of the Act in respect of the development of Subdivision A.
6. The consideration charged by XYZ for the sale of all serviced lots is based on factors similar to those of a commercial developer under similar circumstances, including recovery of all the costs of the relevant infrastructure and an applicable profit margin, based on competitive sales values.
7. The full consideration charged for the sale of all serviced lots within the subdivision is subject to GST/HST.

Issue

Is XYZ eligible for ITCs in respect of GST/HST incurred on infrastructure development for the development of Subdivision A?

Comments

XYZ can claim certain ITCs in respect of GST/HST incurred for infrastructure development in Subdivision A, provided that XYZ does not claim any rebate under section 259 of the Act in respect of the development of Subdivision A where ITCs are otherwise available in accordance with either the Act or this policy statement.

XYZ is permitted to claim ITCs only in respect of GST/HST incurred for infrastructures within the geographical area of the subdivision plan during the development stage of the project and only to the extent that would otherwise be allowed in accordance with the Act if the ITCs were claimed by a commercial developer. In addition, the infrastructure costs for which ITCs may be available pursuant to this policy statement must not be recovered through the imposition of tax-exempt lot levies, property taxes and/or special fees.

ITCs are not allowed in respect of the GST/HST incurred for infrastructures to the extent the cost of such infrastructures is normally reimbursed or compensated by the municipality had the infrastructures been provided by a commercial developer. Similarly, no ITCs are available for infrastructures that are considered to be "oversize", that is, in excess of the development requirements for the immediate area, where the municipality normally would pay or reimburse the developer for such oversize.

Once the infrastructure installation is complete, the municipality is subject to the normal public sector body rules provided by the Act. As a result, any GST/HST costs for the improvement, repair, maintenance, and other associated costs relating to the infrastructures after such time will not be eligible for ITCs.

Where infrastructure ownership is retained by XYZ and the infrastructure is used in exempt activities of the municipality, the municipality is required to apply the change of use rules to the fair market value of the infrastructure at the time the subdivision development is complete. (The method of determining the fair market value is set out in this policy statement.)

If XYZ decides not to sell the serviced lots, additional amounts of ITCs may be recaptured at the time such lots are no longer held for the purpose of sale. Failure to account for the applicable amount of ITC recaptured in respect of the change of use at the appropriate time may impact on the initial allowance of the ITCs.