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Canadian Sales Tax Update

Holding Companies May Face New Rules for GST/HST



The Department of Finance has proposed new “holding corporation rules” for GST/HST* that, if enacted, would be effective as of July 28, 2018. The following is intended solely to provide an overview of the current and proposed new rules including why these rules exist and how they apply.

What are the Holding Corporation Rules?

In simple terms, the rules generally allow for a GST/HST registered parent corporation (“Holdco”) to claim input tax credits (“ITCs”) to recover GST/HST paid by Holdco with respect to expenses that relate to another corporation (“Opco”) that carries on GST/HST taxable activities.

Without these rules, a Holdco would generally not be able to claim any ITCs given that such corporations commonly only own shares of Opco’s and/or other financial instruments, that generate GST/HST exempt income (such as dividends and interest). To claim ITCs, an essential requirement is that the property or service on which GST/HST is payable must be acquired for use, consumption or supply in the course of the “commercial activities” of the claimant. These rules, when applicable, effectively deem Holdco to have acquired property or service that relates to the Opco in the course of Holdco’s commercial activities and, therefore, allows Holdco to claim ITCs to recover the tax, subject to the usual restrictions and requirements.

Under the Current Rules

If the following five conditions are satisfied, a Holdco would generally be able to claim an ITC with respect to the GST/HST payable on the particular expense.

- 1) Holdco is a GST/HST registrant (meaning either registered or required to be registered for GST/HST purposes)
- 2) Holdco is a resident of Canada
- 3) The expense incurred by Holdco can reasonably be regarded as relating to shares or indebtedness of Opco
- 4) At the time GST/HST becomes payable on the expense incurred by Holdco, 90 per cent or more of the properties held by Opco were properties that were acquired for use in GST/HST taxable activities of Opco
- 5) Holdco is related to Opco

Note that special look-through rules may apply if the shares of Opco are not held directly by Holdco.

**Under Section 186 of the Excise Tax Act*

Under the Proposed Rules

Essentially (ignoring special rules that may otherwise take precedence with respect to takeover fees), a Holdco would be able to claim ITCs if all of the following conditions are satisfied:

- 1) Holdco is a GST/HST registrant (as before)
- 2) Holdco is a resident of Canada (as before)
- 3) NEW: The particular expense must be one of the following:
 - a. An expense incurred by Holdco for the purpose of selling or otherwise disposing of, purchasing or otherwise obtaining, or holding shares or Opco debt
 - b. An expense incurred by Holdco for the purpose of redeeming, issuing, converting or otherwise modifying shares, or debt, of Opco by Holdco
 - c. An expense incurred by Holdco for the purpose of issuing or selling its own shares or debt to the extent the proceeds from the issuance or sale are transferred to Opco for use by Opco in the course of its GST/HST taxable activities
 - d. An expense incurred by Holdco at a time when 90 per cent or more of the properties held by Holdco are shares or debt of one or more Opcos (each meeting the conditions in item 4 below) for a purpose of carrying on an activity other than:
 - An activity that is primarily (more than 50 per cent) with respect to the shares or debt, of a person that is neither Holdco nor an Opco (that meets the conditions in item 4 below)
 - A Holdco activity that is GST/HST exempt unless the activity is a financial service that meets certain conditions
- 4) At the time GST/HST becomes payable on the expense incurred by Holdco, 90 per cent or more of the properties held by Opco were properties that were acquired for use in the GST/HST taxable activities of Opco (essentially as before)
- 5) Holdco is related to Opco (as before)

Again, special look-through rules may still apply if the shares of Opco are not held directly by Holdco.



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The Takeaway

If the legislative proposals are enacted, a Canadian-resident holding corporation's ability to claim ITCs may be significantly reduced. If you believe that you may be impacted by these new rules, your Crowe Soberman Tax team is here to help assess the impact and offer guidance of the proposed changes on your processes and transactions.

Connect with the Author

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