

LAND TRANSFER TAX ACT – PART I

This issue of the Legal Business Report provides current information to the clients of Alpert Law Firm on tax planning strategies, exemptions and deferrals involving transactions, which are currently available under the Land Transfer Tax Act of Ontario (the “Act”). Alpert Law Firm is experienced in providing legal services to its clients in tax and estate planning matters, wealth preservation, tax dispute resolution, tax litigation, corporate-commercial transactions and estate administration.

A. INTRODUCTION

1. IMPOSITION AND RATE OF TAX

The Province of Ontario imposes a land transfer tax on certain conveyances of land in Ontario. This tax is generally payable by the transferee and is levied upon the value of consideration passing to the grantor or transferor pursuant to the conveyance.

Subsection 2(1) of the Land Transfer Tax Act (the “Act”) was amended effective January 1, 2017, changing the rates as follows: the rate is 0.5% for the amount of the purchase price up to \$55,000, plus 1% of the amount between \$55,000 and \$250,000, plus 1.5% of the amount of the purchase price between \$250,000 and \$400,000, plus 2% of the amount of the purchase price over \$400,000. For residential properties including at least one, but not more than two single family residences an additional tax bracket was added increasing the rate to 2.5% on the amount of the purchase price over \$2,000,000.

2. MULTIPLE DEEDS

The use of multiple deeds to minimize land transfer tax has been disallowed. In particular, subsection 2.3(1) of the Act provides that, where land is conveyed by more than one conveyance and the Minister of Finance is of the opinion that one of the reasons for conveying the land by more than one conveyance is to reduce the total amount of land transfer tax payable in respect of the conveyances of the land to an amount less than the amount of tax that would have been payable if the land had been conveyed by one conveyance, then the total amount of land transfer tax payable in respect of the conveyances shall not be less than the amount of tax that would have been payable if the land had been conveyed by one conveyance. A parallel provision prohibits the use of multiple dispositions of beneficial interests in land under similar circumstances.

B. WHEN TAX IS PAYABLE**1. REGISTRATION OF A CONVEYANCE**

Land transfer tax is imposed on persons who tender for registration in Ontario any instrument by which land is conveyed including a final order of foreclosure under a mortgage or charge, or a caution in writing which gives notice of the existence of an instrument by which land is conveyed. The word “convey” is given a broad definition in section 1 of the Act. As a result, tax would be payable in respect of any grant, assignment, release, lease, disposition or agreement to sell any interest in Ontario which is presented for registration.

Therefore, an agreement of purchase and sale or any related notice or caution is a taxable conveyance when tendered for registration. The value of the consideration is the full amount of the consideration set out in the agreement. When the subsequent conveyance of the land to which the agreement relates is tendered for registration, no additional tax is payable where the Affidavit of Residence and Value of the Consideration states that the tax was paid when the agreement of purchase and sale or notice thereof was tendered for registration.

2. UNREGISTERED DISPOSITIONS OF BENEFICIAL INTERESTS

Subsection 3(2) of the Act contains provisions that are designed to eliminate the use of trusts as a scheme to avoid land transfer tax. Subsection 3(2) of the Act extends the application of the tax to certain unregistered conveyances of beneficial interests in land. As a result, tax will be imposed at the same rate and on the same basis as if the disposition had been evidenced by a registered conveyance.

Subject to the exemptions outlined herein, land transfer tax is payable on the 30th day after a disposition of a beneficial interest in land, including a sale, transfer, or assignment, however effected, of any part of a beneficial interest in land occurring after that date as well as any change in entitlement to, or any accretion to, a beneficial interest in land.

Under the Act, every trustee of land must deliver a return to the Minister of Finance within 30 days of becoming aware of any changes in the beneficial ownership of land of which he is the trustee. The Minister of Finance considers a trustee to be any person who holds a legal interest in land in trust for any other person, whether or not there is a formal trust arrangement.

C. TAX EXEMPTIONS

1. FOR REGISTERED CONVEYANCES

Transactions exempt from the imposition of tax on registered conveyances include the following:

- (a) under subsection 2(8) of the Act, conveyances to the Crown or a Crown agency;
- (b) under subsection 1(6) of the Act, leases of land, assignments to such leases or notices of leases or assignments of leases, if the lease, at the time that the applicable instrument is tendered for registration, is for an unexpired term which, including renewals or extensions, cannot exceed fifty years;
- (c) certain final orders of foreclosure under any mortgage or charge affecting land only where the final order of foreclosure is made in an action commenced prior to April 10, 1974;
- (d) certain conveyances to or in trust for a pipeline company of easements or right-of-ways over, under or upon land to enable the pipeline company to construct or operate a pipeline;
- (e) certain transfers of land between spouses where the only consideration given for the conveyance apart from natural love and affection is the assumption of any encumbrance registered on the land or that the conveyance is made pursuant to a written separation agreement or a court order. Note that under section 29 of the *Family Law Act* the term "spouse" includes two persons who are not married to each other and have cohabitated (i) continuously for a period of three years or more or (ii) in a relationship of some permanence if they are the natural or adoptive parents of a child. Also exempt are conveyances made to or in trust for a child or dependent of the transferor pursuant to a court order;
- (f) certain conveyances of farm land by an individual, or individuals who are members of the same family to either a family farm corporation, family business corporations, or other family members, which are described in greater detail below;
- (g) certain transfers of life lease interests. The acquisition by an individual or individuals of a life lease interest is exempt from tax where the owner of the property is a non-profit organization or a registered charity; and each transfer

acquired the life lease interest in order to use the unit as his or her principal residence or as the principal residence of each transferee's parent or spouse;

- (h) conveyances of certain mineral rights in the lands; and
- (i) under subsection 2(7) of the Act, where the same conveyance is required to be registered in more than one office under either the Registry or Land Titles System or under both systems, tax is payable only on the first conveyance tendered for registration.

2. CONVEYANCES TO A FAMILY BUSINESS CORPORATION

Certain conveyances of property to a family business corporation are exempt from tax under Regulation 697 of the Act. A "family business corporation" is defined as a corporation in which all issued shares, except for director qualifying shares, are owned by family members of the transferor. To qualify for the exemption, the land must have been in use by an active business that was operated by a member of the family prior to the conveyance. A "member of the family" includes the individual, his or her spouse, children, parents, grandparents, siblings, nieces, nephews and their descendants; in-laws; grandchildren, great-grandchildren and their spouses; and a corporation where all of the issued shares, except for director's qualifying shares, are owned by a member of the family.

Additionally, to qualify for the exemption, the purpose of the conveyance must be to enable the transferee corporation to continue operating the business under the direction of a member of the family. The transferee corporation must qualify for the small business deduction under section 125 of the *Income Tax Act* at the end of their fiscal year following the transfer to be eligible for the exemption.

Prior to the registration of a conveyance of land to a family business corporation, it is necessary to obtain written pre-approval from the Ministry of Finance for the transaction. When the transfer is initiated, the transferee corporation must file a prescribed form indicating that the land has been used predominantly in an active family business and is being transferred to continue the operation of that business. This registered form acts as security for the tax.

Once the transfer is registered, the land must stay in the hands of the transferee corporation for nine months after the end of the fiscal year of the corporation that follows the transfer. At the end of this nine-month period, another prescribed form must be registered with the Ministry of Finance to complete the exemption, indicating that the final requirements have been satisfied (*i.e.* the corporation qualifies for the small

business deduction under section 125 of the *Income Tax Act* and that 75% of its gross income is derived from active business in Canada). Once this form is registered, the security is released and there are no further bars with respect to subsequent transfers of the property.

Upper Valley Dodge Chrysler Ltd. v. Ontario, [2005] O.J. No. 6123

The sole shareholder and officer of a corporation owned land on which the corporate plaintiff operated a business. The sole shareholder conveyed the land to the corporate plaintiff, which claimed an exemption under Regulation 697 of the Act available for a qualifying transfer to a family business corporation.

The Minister assessed land transfer tax on the transaction and the corporate plaintiff appealed the assessment. At issue was the interpretation of section 3 of Regulation 697, which states that the exemption applies to tax payable on the conveyance of land “from an individual or individuals...to a family business corporation” where the business is *operated* by individual family members. The Minister argued that prior to the conveyance the business was not operated by an individual because the corporation did not qualify as an “individual” for the purposes of the exemption.

The Court of Appeal allowed the Minister’s appeal, finding that the conditions required for the exemption were not satisfied. It was the corporate plaintiff who operated the business and not the individual who conveyed the land. Even though the shareholder and officer controlled the corporation, the factor of control is not listed in Regulation 697 as a factor in determining who operated the business. If the Legislature intended control over a corporation to be a factor that could affect the determination of who “operated” a business, the Legislature would have indicated so in clear language. The Court held that the intention of the Legislature was to create an exemption for the conveyance of land from a human being who operates a business to a corporation. Therefore the corporation did not qualify for the land transfer tax exemption.

1211825 Ontario Limited v. Ontario, [2008] O.J. No. 2920

A husband and wife owned all the issued and outstanding shares of a furniture business that was carried on by a corporation, 434999 Ontario Limited (“433999”). The husband and wife also owned all the issued and outstanding shares of a sister corporation, 1211825 Ontario Limited (“1211825”). The husband and wife made two transfers of land to 1211825. Before and after the transfers, the properties were used by 434999 in carrying on the family furniture business.

The Minister assessed 1211825 for land transfer tax on the transfer of both properties and 1211825 appealed the assessment to the Ontario Superior Court of Justice. The Minister alleged that the exemption provided for in Regulation 697 of the Act did not apply to this case. Regulation 697 requires that prior to a conveyance, land must be used in the operation of an active business operated by an individual or individuals. The Minister argued that the family furniture business was operated by 434999, which was a corporation, and not by individuals as required for the exemption under Regulation 697.

The Ontario Superior Court of Justice dismissed the taxpayer's appeal. The Court held that the family furniture business was operated by a corporation and not by individuals. The Court followed the decision of *Upper Valley Dodge Chrysler Ltd. v. Ontario* holding that "operated" did not refer to factual control but rather to *de jure* control. The Court confirmed that the word "prior" in subsection (a) meant immediately prior to the conveyance and did not extend to the period six years earlier when the furniture business was operated by the husband and wife and not by 434999.

3. FOR DISPOSITIONS OF BENEFICIAL INTERESTS

Transactions excluded under section 3 of the Act from the imposition of tax on dispositions of beneficial interest in land include the following:

- (a) the transfer of a beneficial interest which occurs due to the death of the owner of the interest;
- (b) the transfer or assignment of a beneficial interest in the land by a debtor to a creditor for the purpose only of providing security for a debt or loan or the return of security;
- (c) the lease of land or transfer of the interest of a lessee provided that the unexpired term of the lease, including renewals or extensions, does not exceed 50 years;
- (d) the transfer or assignment of a beneficial interest in land which arises upon the execution of an agreement of purchase and sale or by a subsequent assignment of such beneficial interest by a purchaser where the consideration specified in the agreement of purchase and sale has not been paid or the liability for the consideration has not been assumed by or on behalf of the transferee;
- (e) where the disposition of the beneficial interest in land is registered within thirty days after the date of disposition and land transfer tax was paid at the time of registration, no further tax is payable thereon;

- (f) the disposition of a beneficial interest in land pursuant to a written agreement entered into before July 19, 1989, as provided by subsection 21(a) of the Act;
- (g) the disposition of a beneficial interest in land acquired before January 1, 1990 where arrangements in writing for the disposition were substantially advanced before July 19, 1989, as provided by subsection 21(b) of the Act;
- (h) pursuant to subsections 3(9) and 3(11) of the Act, the transfer of a beneficial interest in land from one corporation to another corporation each of which is an “affiliate” of the other immediately before or at the time of disposition. A company shall be deemed to be an “affiliate” of another company if one of them is a subsidiary of the other or if both are subsidiaries of the same company or if each of them is controlled by the same person or company. Control, in this context, is defined as “de jure” control meaning that one corporation holds greater than 50% of the voting shares of the other corporation. In order to obtain this tax relief, the transferring corporation must submit an application to the Minister of Finance, along with security for the tax in the form of a letter of credit, wherein the Applicant undertakes that the underlying control of the corporate group will continue in the same hands and the interest in land will remain within the corporate group for three years following the disposition. The security shall be returned to the corporation which furnished it when the said undertaking has been satisfied, or the conveyance evidencing the disposition of the beneficial interest in land is registered and tax owing upon registration is paid or when the beneficial interest in the land is transferred to a person who is not an affiliate of the corporation and tax is paid on the transfer; and
- (i) sales of units of mutual funds listed on a recognized Canadian stock exchange or units of mutual funds traded pursuant to a prospectus approved by a Canadian securities commission will be exempt from land transfer tax in Regulations to the amended Act.
- (j) dispositions of a beneficial interests in land, involving the transfer or assignment of a partnership interest, which does not exceed more than 5% of the partnership profits, to which the transferor or assignor would have been entitled to receive at the beginning of the fiscal year of the partnership, in which the disposition occurs, (the *de minimis* exemption).

Since the exemption was enacted in 1989, it has been used by many pooled investment vehicles, such as real estate investment trust (REITs) to avoid land transfer tax by acquiring minimal interests in partnerships that owned land in

Ontario, despite the fact that the ultimate investors in those situations would normally be considered to be the beneficial owners of the land in Ontario.

On February 18, 2016, the Ontario Ministry of Finance (the “Ministry”) introduced a retroactive amendment to the exemption from land transfer tax with Regulation 35/16. The amendment revoked the *de minimis* exemption from land transfer tax for a trust (such as a REIT) or partnership that acquires a partnership interest. The amendment clarifies that in order to be eligible for the exemption, one of the following must be satisfied by the individual or corporation who acquires the beneficial interest in the land: (i) the person was a partner in the partnership immediately before the disposition and that person’s entitlement as a partner to a percentage of the profits of the partnership increased as a result of the disposition; or (ii) the person became a partner in the partnership as a result of the disposition and became entitled as a partner to a percentage of the profits of the partnership as a result of the disposition.

More importantly, Regulation 35/16 will apply retroactively to transfers that occurred after July 18, 1989, which likely will trigger assessments on trusts and partnerships that previously satisfied the now-defunct *de minimis* exemption. In March 2016, the Ontario government provided a compliance relief update for the amendment. The Ministry stated that they will not target historical transactions relying on the exemption provided that a written ruling in respect of the transaction was obtained from the Ministry of Finance prior to February 18, 2016. For dispositions of a beneficial interest in land through one or more partnerships, the Minister will only assess and/or reassess dispositions that occurred after February 17, 2012, and will not initiate proceedings under the Land Transfer Tax Act for dispositions that occurred prior to February 18, 2016.

2143569 Ontario Inc. v Ontario (Minister of Revenue), 2014 ONSC 4628, 242 ACWS (3d) 970, 2014 CarswellOnt 10931

The taxpayer made an application to the Ontario Superior Court of Justice by way of appeal from the Ministry of Revenue’s decision to refuse the refund of deferred land transfer tax pursuant to subsections 3(9) and 3(11) of the Act.

The taxpayer, Corporation Y, and Corporation M were affiliated corporations of each other. Prior to September 4, 2007, Corporation Y held both the legal and beneficial interest to a land located in Niagara Falls (the “Property”). On September 4, 2007, Corporation Y entered into a trust agreement with Corporation M, wherein Corporation M would hold title to the Property in trust for Corporation Y. After this transfer, Corporation M was the legal owner of the Property and Corporation Y was the beneficial

owner. On September 12, 2007, Corporation Y conveyed its beneficial interest in the Property to the taxpayer by way of an unregistered disposition. On September 14, 2007, the taxpayer submitted an application for the deferral and potential cancellation of land transfer tax pursuant to subsections 3(9) and 3(11) of the Act.

On August 20, 2008, a development agreement (the “Agreement”) was registered on title to the Property by the City of Niagara Falls, dealing with the conditions to be met if the owner was to undertake any construction on the Property or adjacent lands. The Agreement stated the trustee of the Property to be Corporation M and the owner of the Property to be the taxpayer. Corporation Y was not mentioned in the Agreement. The Agreement also did not use the term “beneficial owner” or mention any transfer of beneficial title. On October 20, 2010, the Minister refused to allow a cancellation of the deferred land transfer tax on the Property on the ground that the Agreement is a conveyance or instrument evidencing the disposition has been registered.

The Ontario Superior Court of Justice held that evidence of a specific disposition of beneficial interest would at the very least have to identify both the entity disposing of the beneficial interest (in this case Corporation Y), and the entity acquiring the beneficial interest (in this case the taxpayer). The Agreement made no mention of Corporation Y, and therefore is not a conveyance or instrument evidencing the disposition has been registered. The Court allowed the taxpayer’s appeal, and ordered the Minister to vacate the disallowance and return the land transfer tax to the taxpayer.

4. EXEMPT TRANSFERS BY A REGISTERED CHARITY

Pursuant to the provisions of Ontario Regulation 386/10, certain transfers of land by registered charities occurring after March 25, 2010 have been exempted from land transfer tax. Where there is a transfer of land from trustees to a non-share capital corporation, or from one non-share capital corporation to another non-share capital corporation, the following preconditions must be met in order to qualify for an exemption from land transfer tax: (i) immediately before the transfer, the qualifying trust must own the land and hold it for a charitable purpose; (ii) the transferee non-share capital corporation must continue the same charitable purpose for at least one year after the transfer date; (iii) no consideration must be paid, other than the assumption of any existing liabilities registered on the land; and (iv) tax must have been paid under the Act in respect of a prior transfer of the land to the qualifying trust.

D. REDUCTIONS IN LAND TRANSFER TAX**1. TRANSACTIONS FOR WHICH CONSIDERATION IS DEEMED NIL**

As noted earlier, land transfer tax is exigible, at whatever rate is applicable, upon the “value of the consideration” for the conveyance. This term is defined very broadly to include the gross cash value of the lands given for the conveyance, any liability assumed or undertaken by the transferee, or any benefit conferred on any person by the transferee of the lands.

The Minister of Finance has issued several bulletins outlining certain transactions for which the consideration given is deemed to be nil. The result in these cases, is that no land transfer tax is payable on such transfers of land. The transactions where the value of the consideration is deemed to be nil include the following:

- (a) conveyances to a corporation which constitute a contribution of capital to the corporation and in respect of which no consideration has been given by the corporation for the land;
- (b) where, by virtue of the statutory amalgamation of corporations, the land of two or more companies becomes vested in the company resulting from the amalgamation;
- (c) where tax is paid upon registration of an agreement of purchase and sale, no further tax is payable when the subsequent conveyance of the land is tendered for registration. If the agreement of purchase and sale is registered and the tax is paid at that time and the transaction is not completed, the proposed purchaser may apply for a refund of the tax paid plus interest currently calculated at the rate of 6% per annum compounded daily;
- (d) conveyances for which the only value of consideration given is natural love and affection, regardless of the relationship between the parties to the conveyance. However, under the Act, consideration includes the assumption of any liabilities. Therefore, if there is an outstanding encumbrance on the property, land transfer tax will be payable on this amount regardless of the relationship between the parties, except on certain transfers between spouses;
- (e) where the sole purpose of the registration is to effect a simple change in the form of legal tenure of land between the parties from tenancy in common to joint tenancy or vice versa;

- (f) conveyances from the personal representative of a deceased person to a beneficiary of the deceased's estate;
- (g) where land is partitioned and each, or any, of the co-tenants receives property equal in value to the co-tenant's original interest in the whole property;
- (h) where a dissolution of a partnership that owns land occurs, and each or any of the partners receives land equal in value to the partner's original interest in the whole property, the Minister of Finance has previously taken the position that no land transfer tax is payable on the basis that partners are treated as tenants in common for the purposes of the Act; and
- (i) where there is an unregistered disposition of land from an employee to his or her employer, no tax is payable if the disposition is made pursuant to a relocation program. In practice, an employee being relocated is paid for his or her home by the employer in return for which the employer receives a transfer signed with no transferee named. The employer then has 180 days to sell the house to a third party.

2. STATUTORY REDUCTIONS OF "VALUE OF THE CONSIDERATION"

In addition to the transactions outlined above where the value of the consideration is deemed to be nil, there are certain types of conveyances where less tax is payable because the value of consideration is reduced or declared to be nil. These include the following transactions:

- (a) if the sole purpose of registration of a notice of a purchaser's lien is the protection of the purchaser's rights of repayment of consideration paid toward the purchase price under an agreement of purchase and sale which the purchaser does not intend to complete and which he or she considers to have been breached by the vendor, the value of consideration may be declared as nil;
- (b) where land is being acquired to replace land that was expropriated by a statutory authority, the value of consideration of the replacement property is reduced by the compensation or proceeds of sale of the expropriated lands;
- (c) where a person leasing land has paid tax on the acquisition of that lease and later wishes to purchase the leased land, the value of consideration for the conveyance is reduced by the value of consideration for the prior lease of land in respect of which tax has already been paid;

- (d) where the conveyance of land contains a single-family residence for a value of consideration in excess of \$400,000, the transferee is liable to pay tax at the higher rate only upon that amount by which the portion of the value of consideration allocated to the lands used in connection with the single-family residence exceeds \$400,000. Such an allocation will only be permitted when the portion of land not used in connection with the single-family residence is the subject of a use other than residential. If the remaining lands are merely vacant, such an allocation will not be allowed; and
- (e) when HST applies to the purchase of land or an interest in land, the value of the consideration does not include the amount of HST paid on the purchase price. Accordingly, land transfer tax is not exigible on the HST paid.

This issue of the Legal Business Report is designed to provide information of a general nature only and is not intended to provide professional legal advice. The information contained in this Legal Business Report should not be acted upon without further consultation with professional advisers.

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