Significant Changes To GST/HST Holding Company Rules

August 14, 2018

The Department of Finance released proposed amendments to the Excise Tax Act that could significantly impact holding companies.

On July 27, 2018, the Department of Finance ("Finance") released a number of proposed amendments to the Excise Tax Act (the "Act"), including section 186, that could significantly impact many businesses that use a holding corporation structure. Section 186 allows a holding corporation to claim input tax credits ("ITCs") to recover GST/HST on expenses incurred with respect to a subsidiary.

Current Rule

The general rule is that a holding corporation cannot claim ITCs for expenses incurred with respect to shares or indebtedness of a subsidiary. In order to claim an ITC, subsection 169(1) requires that property or service is acquired for consumption, use or supply in the course of commercial activities of the company.

Activities related to holding a share or indebtedness of a subsidiary is generally not a commercial activities. Where certain conditions are met, section 186 deems a holding company to be carrying on a commercial activity and allows it to claim ITCs to the extent that expenses are reasonably incurred in relation to a subsidiary.

Proposed Rule – More Targeted

The proposed amendments appear to address the CRA's longstanding concern that the existing rules are too broad as a holding company is only required to prove that the expenses were reasonably incurred "in relation to" a related subsidiary.

The proposed amendments contain more detailed, precise language that aims to more clearly define the scope of activities that would qualify and effectively narrow the type of expenses that would be eligible for ITCs. Moving forward, section 186 will require a more direct link between the holding company expenses and the activities of the subsidiary.

Most holding companies will be affected by these changes.

The draft amendments are open to comment until September 10, 2018.

Consultation Paper – Significant Narrowing of Holding Corporation ITCs

Further to the proposed amendments, Finance also released a consultation paper that proposes to limit the ability of a parent or holding corporation to claim ITCs to "closely related" (i.e., >90 per cent voting control) rather than just a "related" subsidiary. If implemented, this amendment could significantly impact corporate investors and existing ownership structures that use a holding company. The holding company rules would be available only to those arrangements that are effectively wholly-owned parent-subsidiary entities and leave all other corporate structures with unrecoverable GST/HST.

On a positive note, the consultation also proposes to extend the holding corporation rules to include ownership structures that use a trust or partnership, rather than a corporation, to claim ITCs in respect of a subsidiary.

These proposals are open to comment until September 28, 2018.

We Can Help

For assistance in assessing how the draft amendments might affect your business or in preparing a response to the draft amendments and consultation paper, please contact the author or a member of BLG’s Tax Group. We will continue to monitor developments in this area and update you in our bulletins.

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