

Land Transfer Tax: Assignments, Flips and Options

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Determining the amount of Land Transfer Tax ("LTT") payable on a routine purchase and sale transaction is not a difficult task. On a more complicated transaction or series of transactions, however, the impact of the *Land Transfer Tax Act* R.S.O. 1990, c.L.6, as amended (the "Act") and the resultant LTT may have surprising and unfavourable results for a purchaser.

In the 1980s, unregistered conveyances of beneficial interests and transactions involving bare trustees were increasingly used to avoid the payment of LTT. As a result, in 1989 the Ontario government chose to tax unregistered transfers of real property. Consequently, the Act now has parallel systems of taxation: Section 2 of the Act imposes LTT on a registered 'conveyance', and Section 3 imposes LTT on an unregistered disposition of a beneficial interest in land. A registered conveyance is one that is tendered for registration, either in the electronic Teranet Land Titles system or paper Polaris Registry system. If land is conveyed but the disposition is unregistered, LTT is payable by whoever acquired the beneficial interest in land within thirty (30) days of the disposition.

Following the 1989 amendments, the Act became increasingly complex as it caught many transactions that were previously not subject to LTT. Assignments, flips and options are three types of transactions where confusion frequently arises about the amount and timing of LTT obligations.

Give me 'Assign'

When is LTT payable on an assignment?

An assignment of a purchase agreement from one purchaser to another is expressly excluded from the definition of a disposition of a beneficial interest in land. Assignments benefit from a temporary sheltering provision in paragraph 3(1)(g) of the Act, which provides that a disposition of a beneficial interest in land does not include a transfer of beneficial interest in land arising out of the execution of a purchase agreement, or a subsequent assignment, provided that the value of the consideration in the purchase agreement has not been paid or the liability for the value of the consideration has not been assumed by the purchaser.

The exclusion in para. 3(1)(g) provides that a purchaser under a purchase agreement is not required to pay LTT on the acquisition of a beneficial interest until the purchaser pays for, or assumes liability for the interest in land, which generally occurs on closing. This exclusion stems from the issue of whether a purchaser obtains an interest in land in the period between the execution of the purchase agreement and the closing of the transaction. Arguably, once all conditions have been waived, the purchaser has an equitable interest in the subject property by virtue of the doctrine of equitable conversion. The effect of the sheltering provision in para. 3(1)(g) is that a purchaser is only required to pay LTT when the transaction contemplated by the agreement is completed.

How much LTT is payable on an assignment?

In the Act, the definition of value of consideration' includes the gross sale price of any consideration, the amount expressed in money

of any consideration, the value expressed in money of any liability assumed or undertaken by or on behalf of the transferee as part of the arrangement relating to the conveyance, and the value of any benefit conferred directly by the transferee on any person as part of the arrangement relating to the conveyance.

In a 1995 Canadian Bar Association conference paper, Maurizio Romanin noted that “the value of consideration should reflect both the purchase price for the land and the consideration for the assignment of the purchase agreement.”[1] No statutory reference or evidence was provided, but his likely source is an interpretation of the definition of ‘value of consideration’ in the Act.

One could argue that “the conveyance” in the last segment of the definition of ‘value of consideration’ relates only to the transfer of the property from the vendor to the assignee purchaser, and does not include the assignment of the purchase agreement. However, the Ontario Ministry of Finance (the “Ministry”) takes the position that LTT is payable on both the purchase price and the consideration for the assignment. Furthermore, Ministry Bulletin 1-2006 ‘Determining the Value of the Consideration for Transfers of New Homes’ provides that in the context of assignments, the true value of consideration includes the “consideration for the assignment, the purchase price in the agreement assigned, and the value of any extras, upgrades, installations, etc.”

The Act also contains a catch-all clause in subsection 2.3(2), which provides that where a disposition of a beneficial interest occurs by a series of dispositions of beneficial interest designed to reduce the amount of LTT payable, the total amount of LTT payable is the amount that would have been payable as if they were one disposition. Interestingly, since an assignment of a purchase agreement is excluded from the definition of a “disposition of beneficial interest in land” by paragraph 3(1)(g), it is therefore arguable that an assignment fee would not be caught by ss. 2.3(2). Nevertheless, paying LTT on the gross value of consideration including any amounts paid to the assignor in connection with the assignment is the safer approach for those seeking to avoid unpleasant inquiries from the Ministry that could potentially lead to penalties and/or litigation.

On the ‘Flip’ side

A same day ‘flip’ occurs where A enters into a purchase agreement to sell its property to B, and B then enters into a purchase agreement to sell the same property to C, with both purchase agreements having an identical closing date. In such a situation, the sheltering provision in para. 3(1)(g) of the Act will not apply to B and LTT will be payable once B completes its transaction with A, as the purchase price has been paid or the liabilities will have been assumed by B.

Where the respective purchase transactions are completed at the same time or within moments of one another, the Ministry will not assess B for the LTT incurred under Section 3 of the Act in its purchase from A, as an administrative concession. C will be obligated to pay LTT at the usual rates for its purchase transaction from B. We note that this administrative exemption only deals with unregistered conveyances, and not registered conveyances dealt with by Section 2 of the Act.

Do you have ‘Options’?

Ministry Bulletin 1-2001 confirms that the definition of “convey” in the Act includes the “giving of an option upon or with respect to any land.” There is an important distinction between an option that is registered on title to a property, and an unregistered option.

Registered Options

Notice of an unexercised option may be registered on title to a property. The notice of an option, or the assignment of an option, is a taxable conveyance upon registration. The value of consideration is the amount of the consideration paid by the optionee to acquire the option, and not the option exercise price. Therefore, if an optionee pays the optionor \$1 million dollars for the option to purchase a property for \$10 million dollars, and registers notice of the option on title to the subject property, LTT is payable on consideration of \$1 million dollars at the time of registration of the notice.

If the registered option is never exercised, no refund or rebate for the LTT paid to register the notice of option on title is available. If the option registered on title is exercised, the option effectively becomes an agreement of purchase and sale, and no LTT is payable until registration of the transfer due to the sheltering provision in para. 3(1)(g). Upon registration of the transfer, the value of consideration for calculating LTT is the exercise price, or \$10 million dollars in the above example, as LTT has already been paid on the amount paid by the optionee to acquire the option.

If the option agreement between the parties provides that the \$1 million dollar option fee is to be credited against the final purchase price, the value of consideration for calculating LTT upon registration of the transfer will be \$9 million dollars.

Unregistered Options

While the provisions of the Act relating to registered transactions fall under the broad definition of 'convey', the unregistered provisions require payment of LTT upon a disposition'. A disposition is defined as "a sale, transfer or assignment, however effected, and any change in entitlement to or accretion to a beneficial interest in land."

If the granting of an option does not constitute a change in entitlement to a beneficial interest in land, an optionee should not file a return within thirty (30) days of the granting of an option for LTT on the amount paid for the option. Evidence supporting the view that no return should be filed by an optionee in this situation is that Ministry Bulletin 1-2001 provides that when an unregistered disposition occurs as a result of an option, a return must be filed and LTT paid on the consideration paid by the optionee to acquire the option. If obtaining an unregistered option required a LTT return, the requirement to pay LTT on the gross purchase price including the option payment upon registration would effectively be double taxation on the consideration for the option.

Anti-Avoidance (GAAR)

In 2014 the Act was amended to include a general anti-avoidance rule in Section 12.1, which is applicable to transactions (or part of a series of transactions) completed after May 1, 2014. Section 12.1 defines 'avoidance transactions' as a transaction or series of transactions that, but for this provision, would result, directly or indirectly, in a tax benefit, unless the transaction may reasonably be considered to have been undertaken or arranged primarily for bona fide purposes other than to obtain the tax benefit. Although this amendment was aimed at curbing the abuse of one particular exception in the Act involving partnerships that own land, it is relevant for all transactions structured to reduce or eliminate LTT.

The examples discussed above are indicative of the potential hazards surrounding LTT that may arise in seemingly straightforward transactions involving real property. Our real estate lawyers would be happy to speak with you regarding LTT in real estate transactions and structuring real property transactions.

[1] Maurizio Romanin, "Real Property The Road To Recovery: Real Estate Issues and Concerns Beyond the Recession: Land Transfer Tax" (Paper delivered at the Canadian Bar Association Ontario, Institute of Continuing Legal Education, 1995).

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Bradley McLellan has extensive experience in infrastructure and public projects, including procurement, risk allocation, public-private partnership arrangements, concession agreements, ground leases, design-build agreements and operation and management agreements. He also is a recognized expert in the purchase, sale and financing of commercial real estate.

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