

Chapter 2

RECOVERING GST

There are two mechanisms for recovering the GST an organization pays on any taxable goods and services: claiming input tax credits and claiming rebates.

Input Tax Credits

You will pay GST on most purchases and expenses related to taxable activities. Generally, an organization registered for the GST is entitled to claim an input tax credit for 100% of the GST paid on expenses related to taxable goods and services (including zero-rated). An input tax credit (ITC) is a full refund of this GST, claimed in your GST return.

Rebates

Organizations that provide exempt goods and services cannot claim input tax credits for GST incurred on expenses related to these goods and services. The same applies to non-taxable goods and services, if the organization is a small supplier who has not registered for the GST. However, you may qualify for a rebate of the GST in these situations. A rebate is a full or partial refund of the GST that you claim on a rebate claim form.

The following rebates are available to different types of organizations:

Charities (see page 23)	50%
Qualifying non-profit organizations (see page 24)	50%
Schools	68%
Universities / colleges	67%
Hospital authorities	83%
Municipalities (see page 22)	100%

(The 100% rebate rate for municipalities took effect February 2004; previously the municipal rebate rate was 57.14%).

These types of organizations often provide exempt goods and services, meaning they do not collect GST on their revenues, and cannot claim an input tax credit for any GST they incur related to the exempt revenues. The federal government originally established the rebates to ensure these organizations do not pay more tax under the GST than they did under the previous federal sales tax.



Qualifying for Rebates

Housing providers pay GST on many expenses. To qualify for a rebate for some or all of the GST paid, two criteria must be met:

- Your *development* must qualify for a rebate, and
- Your *organization* must qualify for a rebate.

Qualifying Developments

To claim a partial or full rebate of the GST incurred on social housing-related expenses, at least 10% of the units in the development must be provided to one or more of the following groups:

- Seniors,
- Youth,
- Students,
- Individuals with a disability or otherwise in need of assistance, and /or
- Individuals whose eligibility for occupancy depends on a means or income test.

Most of the social housing developments BC Housing funds meet one of the criteria to qualify for a rebate.

Qualifying Organizations

Your organization's status becomes relevant in determining how much of a GST rebate you can claim.

Three categories of GST rebates can apply to housing providers: designated municipalities, registered charities and qualifying non-profit organizations.

1) Designated Municipality

The Canada Revenue Agency considers certain types of social housing to be a municipal activity. Specifically, the CRA will designate housing providers who deliver rent-g geared-to-income (RGI) housing to be municipalities for GST rebates. Once designated as a municipality, a housing provider can claim a rebate of 100% of the GST incurred in providing RGI housing.

All housing providers who supply RGI units should apply for the municipal designation as soon as possible, because you can claim a rebate for 100% of the GST you incur on expenses related to providing RGI housing, after receiving municipal status.

Please note that the municipal rebate only applies to the GST you pay on expenses related to the RGI housing. For example, if 60% of the units are RGI, and 40% are non-RGI, you can only claim the 100% rebate for the GST on operating expenses for the 60% RGI units.



However, if you are also a charity or a qualifying non-profit organization, you can claim a 50% rebate of the balance of the GST incurred on your expenses. If you are not a charity or a qualifying non-profit, no rebate can be claimed on the balance. (Charities and non-profits are explained in the next two sections.)

Applying for Municipal Designation

You must send a letter to request municipal status to the Canada Revenue Agency to obtain a municipal designation. A sample letter is included on page 67 of the appendix.

The Canada Revenue Agency only approves a municipal designation when proof of subsidy is available, generally in the form of a signed operating agreement. Your operating agreement is usually available when project commitment occurs. Housing providers developing new projects should apply for designation at the project commitment stage to ensure you can claim the highest possible rebate when the project is completed.

Please note that a housing provider does not have to be a registered charity or qualifying non-profit organization (see below) in order to be designated as a municipality.

2) Registered Charities

For GST purposes, registered charities must have a registration number issued by the Canada Revenue Agency, and can issue official income tax receipts for donations. Housing providers who are registered charities are entitled to claim a rebate of 50% of GST that cannot be recovered by claiming input tax credits, or municipal rebates if the charity has been designated as a municipality (see previous section).

If you are not a registered charity, the only other way to claim a 50% GST rebate is as a qualifying non-profit organization (see next section).

To learn more on how to qualify and apply to be a registered charity, refer to CRA guide T4063, *Registering a Charity for Income Tax Purposes*, or visit the CRA website at www.cra-arc.gc.ca.

3) Non-Profit Organizations

Non-profit definition

The GST legislation defines a non-profit organization as:

“...a person (other than an individual, an estate, a trust, a charity, a public institution¹, a municipality or a government) that was organized and is operated solely for a purpose other than profit, no part of the income of which is payable to, or otherwise available for the personal benefit of, any proprietor, member or shareholder thereof.”

¹ A public institution means a school, college, university, hospital or local authority that is also a charity.



Government Funding Test

Only qualifying non-profit organizations are entitled to claim rebates. Qualifying non-profits can claim a rebate of 50% of any GST paid that cannot be claimed as an input tax credit.

To qualify, a non-profit organization must receive at least 40% of its total revenues from government or a qualifying agency, including BC Housing, Canada Mortgage and Housing Corporation (CMHC), or a regional health authority.

Health authorities must supply a completed GST form 322, *Certificate of Government Funding*, certifying that the funding qualifies as government funding.

The following sources qualify as government funding:

- Federal, provincial or municipal governments.
- A corporation controlled by the federal government, a provincial government or a municipality that funds charitable or non-profit endeavors as one of its main purposes.
- A trust, board, commission or other body established by the federal government, a provincial government or a municipality, which also funds charitable or non-profit endeavors.
- An Indian band, as defined by federal legislation.

Government funding does not include payments for other goods and services sold to the government, such as land, consulting services or educational seminars.

Calculating your government funding ratio

The ratio of government to total funding is calculated using the following formula:

$$\text{GF} \div (\text{GF} + \text{A} + \text{B}) \times 100$$

GF = the amount of government funding received or receivable during the year, as reported in the housing provider's annual financial statements.

A = the total of any income from interest or dividends, capital contributions to the housing provider, and loans from parties who are not independent or neutral to your organization.

B = 75% of the revenue from goods or services supplied by the housing provider, including memberships and sponsorships.



The example below illustrates how to apply the 40% funding test to determine if a non-profit organization qualifies for the rebate:

ILLUSTRATION OF 40% FUNDING TEST CALCULATION

1) Government Funding

- BC Housing subsidy	\$50,000	
- CMHC subsidy	<u>\$50,000</u>	
Total subsidies	\$100,000	GF

2) Investment Income

- Interest income	\$1,000	A
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3) Other Revenues

- Rental revenue	\$150,000	
- Commercial leases	\$20,000	
- Commercial parking	\$5,000	
- Laundry	\$3,000	
- Meeting room rental	<u>\$2,000</u>	
Subtotal	\$180,000	
25% Reduction	<u>(\$45,000)</u>	\$135,000 B

Total **\$236,000**

Percentage of government funding **42%** = [GF / (GF + A + B)]
 = \$100,000 / \$236,000 x100



First year of operations

New housing providers usually cannot qualify for the 50% rebate until the end of the first year. If the 40% funding test is met using the first year's financial statements, your organization will be deemed qualified, effective the beginning of that first year. You can then claim the rebate for the first year.

The Canada Revenue Agency may allow a housing provider to qualify during the first year, if you can demonstrate that the 40% government funding threshold will be met, based on funding agreements and operating budgets. Contact the CRA to find out if this condition applies to you.

Second year of operations

If this is your second year of operations, you will qualify for the 50% rebate if you met the 40% government funding test in either the first year or second year of operations.

Three or more years of operations

If you have been operating for more than two years, you will qualify for the 50% rebate if the average of the two preceding years is 40% or more, or the government funding test is met at the end of the current year.

Using these guidelines, housing providers do not necessarily have to meet the 40% government funding test every year in order to qualify for the 50% rebate. For example, a housing provider who met the funding test in each of the first two years, but not the third, would qualify for the rebate in all three years.

The majority of housing providers funded by BC Housing and CMHC do qualify as non-profit organizations under GST legislation, although some larger groups have other sources of funding and donations and may not meet the 40% government funding test. If a non-profit organization does not receive the necessary 40% government funding to qualify, the other option is the municipal or charity rebate, if eligible.

A qualifying non-profit organization may be eligible to claim both the municipal rebate, if you have municipality status (see page 22), and the qualifying non-profit rebate. Some of your units may be eligible for the 100% municipal rebate, and other units for the 50% qualifying non-profit rebate.

Managing Multiple Rebates

Accounting for rebates is relatively straightforward when you are eligible for just one rebate. But the process can be a bit more complicated if you are eligible for two different rebates and file GST returns each month or quarter.

For example, if you have been designated as a municipality, you may supply some rent-gear-to-income units that are eligible for the 100% rebate, while your remaining non-RGI units are eligible for a 50% rebate, as a registered charity or qualifying non-profit.



To reduce paperwork and simplify the accounting process in this situation, you may wish to consider the following alternatives:

Claim 50% and Adjust at Year End

Rather than figuring out the proportion of expenses to claim at 100% and at 50% each month or quarter, an alternative is to claim the 50% rebate on all the rebate claims you file during the year. At the end of the year, you can assess the proportion of rent-geared-to-income housing for the entire year, and submit a municipal rebate claim for the outstanding amount on your final claim.

For example, let's assume:

- A housing provider incurs \$50,000 in taxable expenses during the year.
- 75% of the units are rent-geared-to-income.
- The housing provider has been designated as a municipality and is also a registered charity or a qualifying non-profit organization.

Step 1: GST paid during the year would total (7% of \$50,000) = \$3,500.

Step 2: During the year, the housing provider would claim 50% rebates, as a charity or qualifying non-profit, totaling ($\$3,500 \times 50\%$) = \$1,750.

Step 3: In the last GST return of the year, the housing provider could claim the outstanding amount of the municipal rebate (50% unclaimed) for the 75% RGI units: (75% of 50% of \$3,500) = \$1,312.50.

Claim the 50% Rebate Only

The difference in the rebate rates is important when you develop a new social housing project with RGI units, because a significant amount of GST is payable when the project is completed.

However, if your expenditures for ongoing operations are quite small, making the difference between the 100% and 50% rebate claims insignificant, you may decide to simply claim the 50% rebate to reduce the paperwork required to account for the different rebate rates.

For example, assume a housing provider offers a range of services, and RGI units are a very small part of these services. As the only expense eligible for the 100% municipal rebate is related to the RGI units, it may require more time and effort to account for expenditures on the RGI units separately, than is warranted by the amount of the 100% rebate. It may be easier to simply total all expenses eligible for a rebate, and just claim the 50% rebate.

However, we recommend housing providers claim the 100% municipal rebate whenever feasible, in order to get back most of the GST paid.



GST Status of Social Housing Revenues

Social housing providers receive revenues that can include:

Non-Taxable Revenues

- Grants
- Donations

Exempt Revenues

- Residential unit rentals
- Residential parking
- Residential laundry (user operated)
- Interest or other investment income

Taxable Revenues

The following revenues are potentially taxable:

- Leases of commercial space for offices or retail use.
- Commercial parking rentals (to people who are not residents).
- Meeting room rentals, regardless of whether the room is located in residential or commercial space.

Whether these revenues are taxable depends on your organization's circumstances:

- If your organization is not registered for the GST and is not required to be registered as a small supplier, then these revenues are not taxable.
- If your organization is a registered charity and is registered for the GST, then all of these revenues are exempt, unless you have made an election using GST form 26, *Taxable Real Property Election*. A sample form is included on page 68 in the appendix.
- If your organization is a non-profit and is registered for the GST, then the commercial parking and room rentals are taxable. The commercial leases will also be taxable, if you make an election using GST form 26.

If you elect to make these revenues taxable, you must charge GST on them. You can claim input tax credits to recover the GST you pay for operating expenses to acquire the property or to make improvements, based on the proportion used for taxable commercial purposes.



If you do not elect to make these revenues taxable, you will not be able to claim input tax credits, but you may be entitled to claim a rebate.

You must submit an election form for each property with commercial space, because electing to make the commercial activities of one property taxable does not affect your other properties.

Housing providers may have other sources of revenue; for example, offering courses or running a thrift store. However, the GST status of these revenues is beyond the scope of this guide.

Claiming Input Tax Credits

If you are registered for GST, you can claim input tax credits for the GST you paid on expenses related to providing taxable goods and services, such as commercial leases. There are three methods for claiming input tax credits, depending on the circumstances: the normal method, the special quick method, and the charity method.

1) Normal Method

This method does not apply to charities.

a) Operating Expenses

To claim an input tax credit under the normal method, at least 10% of an operating expense must be used for taxable activities, such as commercial leases. If 90% or more of the expense relates to taxable activities, you can claim the full input tax credit. And you can claim a portion of the input tax credit for expenses when the taxable use is between 10% and 90%. The table below illustrates these three categories:

Taxable Use	ITC Claim
Less than 10%	No ITC
10% - 89%	Claim proportional ITC
90% or more	Claim full ITC

b) Capital Expenses

The above rules do not apply to purchases of capital property, which include equipment and real property such as land and buildings. For these items, you can claim a full input tax credit if more than 50% of the property you acquire is used for taxable activities; otherwise no input tax credit can be claimed. Special rules apply to real property with both housing and commercial space (see page 39).



2) Special Quick Method

The special quick method is a simplified accounting option available to:

- Certain public service bodies
- Some qualifying non-profit organizations
- Certain designated charities whose main purpose is to provide employment or employment-related assistance to people with disabilities
- Non-profit facility operators providing facilities for mentally or physically challenged residents with:
 - Individual nursing and personal care under the direction of qualified medical and nursing staff.
 - Assistance with activities of daily living and social, recreational and other related services to meet residents' psychosocial needs.
 - Meals and accommodation.

The special quick method may not apply to many housing providers. For example, it does not apply to most registered charities, and while designated municipalities can currently opt to use this method, a new formula is being drafted by the Canada Revenue Agency for municipalities. The federal government announced the special quick method will be modified for designated municipalities to accompany the February 2004 change in the municipal rebate, from 57.14% to 100%. But to date, the CRA has not released the changes.

For housing providers who qualify, this method eliminates the need to separate purchases that are for taxable activities and GST exempt activities.

When you use the special quick method, you continue to charge the 7% GST on any taxable goods and services you supply. You multiply the amount of GST you collected by 76.4% to calculate how much to remit to the Canada Revenue Agency, rather than submit the 7% you charged.

Using this approach means you remit only a part of the tax you collected. You can not claim input tax credits on most of your purchases using this method. Instead, you keep the rest of the tax you collected ($100\% - 76.4\% = 23.6\%$). The 23.6% represents the approximate value of the input tax credit you would normally have claimed.

GST on taxable revenues (e.g., commercial rents) – Collect 7%

GST reported as collectible on GST return – 76.4% of GST collected

GST retained in lieu of input tax credits – 23.6%



Certain goods and services are not included in the special quick method calculation including:

- Sales of land and buildings.
- Zero-rated goods and services (see page 18 for details).
- New developments on which you had to assess the amount of GST owing at completion, using self-supply rules. The self-supply rules apply to new construction and substantial renovations only, and are explained on page 36.

Because you keep part of the tax you collect using the special quick method, you do not claim input tax credits on most of your purchases and expenses. However, you can claim an input tax credit for the following items:

- Purchases of and improvements to capital real property used primarily in taxable activities.
- Purchases of or improvements to capital personal property, such as computers and vehicles used primarily in taxable activities, where the cost of the property exceeds \$10,000.

If you want to use this special quick method, you must submit GST form 287, *Election for Special Quick Method*, to Canada Revenue Agency. A sample form is included in the appendix on page 70.

3) Charity Method

Most registered charities that provide taxable goods and services are required to use the charity method of accounting for GST input tax credits. However, you can opt to use the normal method if you:

- Provide zero-rated goods or services,
- Provide goods or services outside Canada, or
- Have at least 90% taxable revenues.

Using the charity method, registered charities do not claim any input tax credits for GST paid on operating costs. To compensate for the unclaimed input tax credits, you keep 40% of the GST you collected on taxable revenues such as commercial rentals. Please note that you must still charge 7% GST to the recipient of these goods and services, but you report only 60% of that amount as collectible GST to the Canada Revenue Agency.



Claiming Both Input Tax Credits and Rebates

Some housing providers may provide both taxable and exempt goods and services. In this case, you may be able to claim input tax credits for the portion of GST related to your taxable activities, and rebates for the portion of GST related to your exempt activities.

For example, a housing provider operates a facility with 25% commercial space and 75% social housing units.

Rental income from the commercial space will usually be taxable, so the housing provider can claim a full input tax credit for the GST incurred on utility costs for the commercial space.

Rental income from the social housing will be exempt, so the housing provider cannot claim an input tax credit for the GST incurred on utility costs for these units. But if you qualify, you can claim a partial or full rebate of this GST.

As this example illustrates, overall facility expenditures must be allocated to the taxable and exempt components. For instance, an input tax credit may be claimed for the commercial portion of repair and maintenance work (25%) done for the entire facility, and if eligible, a partial or full rebate on the balance.

The *GST Return* and *Rebate Application* forms are the same for charities and qualifying non-profit organizations. However, you can not combine the rebate claims or returns for a charity and a qualifying non-profit onto a single rebate claim or return form; each organization must file separately.

ITC Example

The example on the next page illustrates the three methods for calculating input tax credits, as well as rebates.



FACTS

- Housing provider operates a facility with:
 - 25% taxable commercial rentals
 - 75% exempt residential units
- Housing provider does not have municipality status
- Housing provider is eligible for a 50% rebate

Taxable revenues

Commercial rental revenue	\$50,000
GST collected (\$50,000 x 7%)	\$3,500

Taxable Purchases

Taxable operating costs - eg: utilities	\$20,000
GST paid on purchases (\$20,000 x 7%)	\$1,400

	Normal	Special Quick	Charity
GST collectible to report	all GST collected	76.4% of GST collected	60% of GST collected
Input tax credit to claim	all GST relating to taxable activities	none	none
Rebate	50% of GST relating to exempt activities	50% of all GST incurred	50% of all GST incurred
Using the information above:			
a) GST collectible to report on return	\$3,500	\$2,674 (\$3,500 x 76.4%)	\$2,100 (\$3,500 x 60%)
b) ITC claimable	\$350 (\$1,400 x 25%)	-	-
c) Rebate	\$525 50% x (\$1,400 - \$350)	\$700 (50% x \$1,400)	\$700 (50% x \$1,400)
Net amount to remit to CRA (a-b-c)	\$2,625	\$1,974	\$1,400