

Investment limited partnerships: Federal Budget 2018

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- The Liberal government's third budget confirmed plans to go forward with amendments to the *Excise Tax Act* (Canada), similar to draft legislation published last September (the Revised Legislation)
- Overview of the Revised Legislation and the implications for investment limited partnerships
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On February 27, 2018, the Liberal government's [third budget](#) announced that the government would be going forward with amendments (the Revised Legislation) to the *Excise Tax Act* (Canada) (ETA) that are intended to levy GST/HST on management and administrative services provided by a general partner to its investment limited partnership (ILP). The Revised Legislation largely mirrors similar proposed amendments released by the Department of Finance (Finance) on September 8, 2017 (the Initial Legislation), which was discussed in our [update](#) published last September. Although some helpful changes were included in the Revised Legislation, many of the concerns raised by taxpayers with respect to the Initial Legislation still exist.

The following reviews the changes made in the Revised Legislation and spells out the GST/HST payment and reporting obligations that affected general partners and investment limited partnerships will imminently have to comply with.

Overview of the Revised Legislation

In essence, the Revised Legislation causes GST/HST to apply to the provision of management or administrative services by the general partner of an investment limited partnership to the ILP. An ILP is broadly defined to include limited partnerships whose primary purpose is investing in property that is primarily financial instruments, which would generally include among other things debt or equity interests in corporations, trusts or other partnerships. Furthermore, the ILP will be considered to have acquired the management or administrative service in question for the fair market value of these services. The general partner must then remit to the Canada Revenue Agency (CRA) the GST/HST payable on the fair market value of the services rendered. If enacted, these measures would represent a significant change relative to current law, under which GST/HST is generally not payable on these services.

Issues addressed by the Department of Finance

The Initial Legislation provoked numerous taxpayers and advisors to raise a number of concerns with the proposals. Finance did address some of these concerns in the Revised Legislation. In particular, Finance amended the Initial Legislation's wording to clarify issues relating to collecting and reporting, and as to when the rules come into force.

Collecting and reporting

One problem with the Initial Legislation was that it had the effect of deeming consideration for the supply of services to become due when the services were rendered. For ongoing services, this could potentially have caused GST/HST to become payable on a daily basis.

Finance has redrafted paragraph 272.1(3)(b) of the ETA to clarify when GST/HST must be collected and reported in the ILP context. Generally, if payment for the management and administrative services is split into billing periods, then the GST/HST payable should become due on that last day of the applicable billing period. Otherwise, the GST/HST should become due on the first day of the general partner's reporting period, which could be as often as monthly for those general partners earning in excess of \$6 million annually.

Coming into force

Another issue with the Initial Legislation was that in certain circumstances, the fair market value of some services rendered prior to the announcement date of September 8, 2017 (Announcement Day) could have been considered to be subject to tax. Finance has now created a bright line test between services rendered before Announcement Day, and those rendered on or after Announcement Day. Under the Revised Legislation, services rendered on or after Announcement Day will generally be subject to the new rules regardless of when consideration for the services is paid.

Areas of continuing concern

A number of concerns were raised with the Initial Legislation that were not addressed in the Revised Legislation.

Valuation issues

Pursuant to the Revised Legislation, general partners of an ILP must collect GST/HST on the fair market value of management and administrative services provided to the partnership. While the ETA does use the concept of fair market value in other contexts, determining the fair market value of management and administrative services in the context of services rendered by a general partner will be particularly difficult. In order to determine the fair market value of the services being provided to the ILP, a general partner will need to first unbundle its management and administrative services from any other services or activities it performs. It will then have to determine what an arm's length party would pay for these services. If the general partner is not providing similar services for a fee to arm's length third parties (which they generally won't be), determining the fair market value of the general partner's services will likely be both problematic and administratively inconvenient.

Primary purpose definition and tiered partnerships

A limited partnership will come within the definition of ILP set out in subsection 123(1) if its primary purpose is to invest funds in property consisting primarily of financial instruments. The Revised Legislation does not provide guidance on how to determine a partnership's "primary purpose." This raises the question as to what criteria this determination is based on: Do you look solely to the partnership's stated objectives? The time spent by the partnership on various activities? The make-up of the partnership's assets? The partnership's income as calculated for income tax purposes?

As drafted, there is a concern that the Revised Legislation will capture tiered partnerships where the bottom partnership is engaged in commercial activities. For instance, a limited partnership set up for the purpose of investing directly or indirectly in real estate will often make its acquisitions of real property through another partnership. As a result, it may only own partnership interests in the partnerships that actually own and operate the real property. Arguably the primary purpose of such a limited partnership should not be "investing funds in property consisting primarily of financial instruments," which includes partnership interests, even though 100% of the limited partnership's assets are invested in financial instruments. However, at this time, it is not clear whether the CRA would agree with this analysis. We understand that the CRA plans to issue guidelines to clarify the application of the primary purpose test, but until it does so, there will be uncertainty as to which entities will be considered ILPs.

Next steps if the Revised Legislation applies to you

The first step is determining if you have an ILP. If you do, then based on the Revised Legislation, the general partner of the ILP will likely have to register for GST/HST. If the ILP existed prior to February 27, 2018 (Budget Day), the general partner will have to determine the fair market value of the management and administrative services it performed during the period from Announcement Day to Budget Day. The general partner will then have to calculate the GST/HST owing on this amount, less any amount actually collected on the services. These amounts are deemed payable on Budget Day.

In other words, the general partner will be required to remit GST/HST payable on the fair market value of administrative or management services it made for the period from September 8, 2017 to February 27, 2018 (less any amount actually collected) with its GST return for the period including February 27, 2018. Thus, if a general partner becomes a monthly registrant, it should have to remit the GST/HST payable to the CRA with its GST return covering the February 27, 2018 period. For monthly filers, should be due by March 31, 2018. If the general partner is a quarterly filer, the deadline for remittance, April 30, 2018, is quickly approaching. General partners should ensure they are registered for GST as soon as possible, so that they can remit the GST/HST payable on the fair market value of their services by the due date.

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