ONTARIO BAR ASSOCIATION
A Branch of the Canadian Bar Association
L'ASSOCIATION DU BARREAU DE L'ONTARIO
Une division de l'Association du Barreau canadien

March 17, 2016

The Hon. Charles Sousa
Minister of Finance
Ministry of Finance
7th Floor, Frost Building South
7 Queen's Park Crescent
Toronto, ON M7A 1Y7

Dear Minister Sousa:

RE: O. Reg 35/16 Changes to the Land Transfer Tax Act Regulation 70/91

As Chair of the Ontario Bar Association ("OBA") Taxation Law Section, I am writing regarding the recent retroactive changes made to the land transfer tax regime by Ontario Regulation 35/16.

Enclosed is a submission prepared by members of our section and the Canadian Bar Association/Chartered Professional Accountants Joint Taxation Committee, in particular:

- Thomas A Bauer – Bennett Jones LLP
- Corrado Cardarelli – Torys LLP
- R. Ian Crosbie – Davies Ward Phillips & Vineberg LLP
- Jarrett Freeman – Goodmans LLP
- Ken Griffin – PWC LLP
- Jane Helmstadter – Bennett Jones LLP
- K. A. Siobhan Monaghan – KPMG Law LLP
- Angelo Nikolakakis – EY Law LLP
- Janice Russell – Deloitte LLP
- Mitchell Sherman – Goodmans LLP
- Antony Schiefer – KPMG LLP
- Lorne Shillinger – KPMG LLP
- Maria Scullion – Deloitte LLP
- Jeffrey Trossman – Blake Cassels & Graydon LLP

Thank you for taking time to consider this submission.

As outlined in the submission, our members are very concerned about this matter and would appreciate the opportunity to meet to discuss the issues and recommendations at your earliest convenience.

Yours respectfully,

John A. Sorensen
Chair, OBA Taxation Law Section

c: His Worship John Tory, Mayor, City of Toronto

We are writing to voice our significant concerns about the recent retroactive changes made to the land transfer tax regime by Ontario Regulation 35/16. In the present circumstances, we believe the approach taken by the Government is unprecedented. The recent changes are not remotely "clarifying" in nature but, instead, are fundamentally inconsistent with the commonly accepted manner in which the prior version of the regulation was interpreted and applied in practice by taxpayers, the tax community and the Government itself. In our view, for the reasons described in detail below, such a significant and clearly adverse change in law should be implemented only on a prospective basis.

We also note that the City of Toronto imposes a land transfer tax on conveyances of beneficial interests in Toronto land. The Toronto legislation essentially incorporates by reference the provincial regime. Thus, Ontario Regulation 35/16 not only retroactively amends the Ontario land transfer tax regime, but also purports to retroactively impose additional municipal land transfer tax.

It is a basic tenet of Canadian tax law that taxation statutes must be administered so as to achieve consistency, predictability and fairness so that taxpayers may manage their affairs intelligently and in compliance with the law.[1] In our view, the same considerations and objectives should apply to the introduction and amendment of taxing legislation and the promulgation of regulations thereunder. The 27-year retroactive nature of the amendment runs counter to any notions of "consistency, predictability and fairness". Taxpayers who acted in accordance with the law as it read at the time they entered into various transactions now find, many years after the fact, that they are potentially liable to significant tax, interest and penalties because of a retroactive change. This result is unacceptable. We urge the Government to reconsider the retroactive nature of the regulation in light of its past practice, which has been to act on a prospective basis in tax matters, and the negative impact that retroactive taxation may have on investment in Ontario and Toronto.

Moreover, the changes in law made by Ontario Regulation 35/16 create numerous taxation anomalies that not only undermine the policy of the *de minimis* exemption, but also are unworkable in practice. Consequently, to the extent that changes are considered by the Government to be desirable or necessary, we believe that a thorough consultation with stakeholders is necessary to address a number of the difficult practical and fairness issues, some of which we have identified below.

Background

Since July 19, 1989, the *Land Transfer Tax Act* (Ontario) (the "**Act**") has provided for land transfer tax on conveyances of beneficial interests in land in Ontario, regardless of whether the conveyance is registered. However, exemptions from section 3 of the Act, which imposes tax on unregistered conveyances of beneficial interests in land, may be and are prescribed. Ontario Regulation 70/91 (the "**Regulation**") has provided a number of prescribed exemptions, each effective July 19, 1989. Subsection 1(2) of the Regulation contained an exemption for an acquisition of an interest in land that is an interest in a partnership where the person acquiring the interest would not be entitled, in

[1] See *Canada Trustco Mortgage Co. v. R.*, 2005 SCC 54, at paragraph 12.

the partnership's fiscal period in which the interest was acquired, to a percentage of the partnership profits that exceeds, by more than 5%, the percentage of the partnership profits to which the acquirer would have been entitled at the beginning of that fiscal period (the "**Exemption**").

Nature of Change: Not Clarifying

On February 18, 2016, amendments to the Regulation were filed that affect the Exemption effective on or after July 19, 1989 (the date on which the Exemption originally became effective). The material released by the Ontario Ministry of Finance (the "**Ministry**") with the amendments (the "**Release**")[2] describes the amendments as "clarifying amendments for certain dispositions".

With respect, the amended Regulation (the "**New Regulation**") can only be described as a fundamental change in law that repeals the Exemption and introduces an entirely different exemption (the "**2016 Exemption**"). The 2016 Exemption is substantially narrower and disqualifies entire classes of transactions that previously fell within the Exemption. The 2016 Exemption cannot reasonably be described as clarifying, as is abundantly clear from the wording of the New Regulation itself and the Release.

Subsection 1(2) of the New Regulation rewrites the Exemption entirely, including the addition of new text that is unclear and confusing (as discussed below). There is no doubt that subsection 1(3) is a new, substantive condition, and to assert that it is clarifying is simply not credible.

Each of a partnership and a trust is a legal relationship, not an entity, and the Act and the Regulation reflect that interpretation – where a partnership acquires an interest in land, it is the partners of that partnership who acquire the beneficial interests in the land. Were that not the case, the Exemption would be unnecessary and irrelevant. Similarly, where a trust acquires an interest in land, it is the beneficiaries of the trust who acquire beneficial interests in the land. Again, if that were not the case, the exemption for the disposition of certain publicly-distributed trust units in subsection 1(1) of the Regulation would be unnecessary.

The Guide[3] published by the Ministry is entirely consistent with this look-through view of trusts and partnerships:

> "A <u>trustee holds the property on behalf of the owners</u> of the units of the mutual fund trust. As a result, if the fund has land…<u>the unit holders will have a beneficial interest in that land</u>."

and

[2] *Land Transfer Tax "De Minimis" Partnership Exemption: Clarifying Amendments for Certain Dispositions* dated February 2016.

[3] 2005-01 – A Guide for Real Estate Practitioners – Land Transfer Tax and the Treatment of Unregistered Dispositions of a Beneficial Interest in Land.

> "In the administration of the Act, the Branch takes the position that a partnership is not a legal entity and therefore a conveyance or disposition of land to a partnership…constitutes a conveyance to the partners of the partnership as tenants-in-common and in proportion to their partnership interest(s)."

The Guide explains the taxing authority's interpretation of the legislation and provides examples. This is typically the purpose of a guide. While it is not a substitute for the legislation, and cannot override the legislation, the expectation is that it will contain guidance about all significant issues. Yet, in the Ministry's ten-part Guide, nothing suggests an interpretation of the Exemption that remotely corresponds to what is now described as being a clarification. In fact, we submit that the Guide suggests an entirely different view, that is only consistent with the look-through view of partnerships and trusts.

Subsection 1(6) of the New Regulation expressly provides that subsection 1(2) as it read before the amendment (i.e., the Exemption) is deemed not to have applied to dispositions of beneficial interests in land on or after July 19, 1989. The very fact that it was considered necessary for the New Regulation to expressly deem the Exemption "as it read immediately before the coming into force of the [New Regulation]" not to apply on or after July 19,1989 substantiates the conclusion that the law is changed; if the New Regulation were merely clarifying, this deeming language would be completely unnecessary.

Typically, when a tax authority publishes new legislation or new guidelines that adversely affect taxpayers, the revisions are applied only on a prospective basis because certainty, predictability and fairness are central tenets of tax law. Taxpayers ought to be able to rely upon the law and the Ministry guidelines in effect at the time they take actions. It is both inappropriate and unreasonable to revoke the Exemption retroactively on the premise that the New Regulation is merely clarifying when it is well known that the Ministry did not interpret the Exemption in that manner. Taxpayers rightfully relied on the Ministry's own interpretation, as reflected in its Guide and rulings. We also are aware of audit experience where this look-through view of partnerships and trusts was applied by the Ministry.

The Release states that where a person received a written ruling from the Ministry on or before February 18, 2016, "the Ministry will generally consider the ruling to continue to apply." If the New Regulation were truly clarifying, then presumably the Ministry should not have issued rulings that are inconsistent with the language of the 2016 Exemption. The purpose of this perspective is not to question whether the Ministry should honour these rulings; obviously, it goes without saying that we believe it should. Honouring rulings given to taxpayers provides them with the appropriate certainty and predictability regarding the tax consequences of transactions undertaken by them. However, the fact that the Ministry issued these rulings is the clearest possible evidence that the New Regulation represents a fundamental change to the Exemption. Moreover, enacting the New Regulation with retroactive effect deprives taxpayers who relied on the law (including the Ministry's interpretation of that law as reflected in the Guide and rulings), but did not obtain a ruling, from that same predictability, certainty and fairness.

Dubious Legal Status of New Regulation

Regulations are a form of delegated legislation. They are valid only insofar as they are authorized by an enactment that confers authority to make them. For the reasons discussed below, we believe there is reason to doubt that a court would uphold the New Regulation as legally valid.

While not stated in the text of the New Regulation itself, we presume that the alleged authority for the promulgation of the New Regulation is section 22 of the Act. Only portions of section 22 apply to taxes imposed under the Act in respect of beneficial dispositions.[4] As far as we can tell, the purported authority for promulgating the New Regulation is clause 22(2)(b) of the Act. Clause 22(2)(b) authorizes the Lieutenant Governor in Council to make regulations:

> "exempting from tax arising under section 3 prescribed dispositions or prescribed beneficial interests in land to which it is determined that section 3 was not intended to apply, or exempting from such tax prescribed dispositions of beneficial interests in land to persons prescribed for the purposes of this clause."

Clause 22(2)(b) does not explicitly authorize the Government to restrict previously promulgated regulations that themselves gave effect to exemptions from tax on dispositions of beneficial interests in land. Nor does it explicitly permit the Government to make retroactive regulations that impose tax. While subsection 22(3) of the Act authorizes retroactivity in regulations, this authority must be read in the context of what is permitted by subsection 22(2) and cannot be read as authorizing the retroactive elimination of an exemption, the result of which is taxation that would otherwise not be imposed.

According to Pierre-André Coté, the author of the widely-accepted text, *The Interpretation of Legislation in Canada* (1984), it is a generally accepted principle of statutory interpretation that enabling provisions, such as clause 22(2)(b), "should be interpreted as not permitting the retroactive exercise of a delegated power".[5] In addition, Coté notes:

> "[W]hen [the rule against retroactive operation is] applied to administrative acts, there is also a question of jurisdiction. Administrative agencies possess only those powers authorized by the statute. They cannot enact retroactively unless the statute so provides, either implicitly or explicitly. In the absence of such power, administrative decisions with retroactive effect are void. This rule has been applied to decisions of the government, of ministers, of administrative tribunals and of municipal corporations."[6]

---

[4] See Section 21 of the Act which makes it clear that only clauses 22(2)(b) and (m) apply with respect to beneficial dispositions.

[5] Coté, *Interpretation of Legislation*, at 152.

[6] Coté at 155.

Had the Ontario Legislature intended that the Government be authorized to make retroactive regulations eliminating previously promulgated exemptions, it would have been a simple matter to so provide in the statute. In view of the general presumption against retroactivity, there is doubt that the Lieutenant Governor in Council has jurisdiction to make the New Regulation. While subsection 22(3) of the Act may allow regulations under clause 22(2)(b) to be made on a retroactive basis, that is a power to relieve transactions from taxation. In contrast, the New Regulation has the potential effect of retroactively imposing tax on transactions undertaken over the past quarter century that were not taxable under the then-prevailing law. It amounts to a retroactive charging provision. It is highly debatable that the power to retroactively relieve taxpayers from taxation also grants authority to retroactively impose tax. At a minimum, it seems likely that this matter will come before the courts and, accordingly, will give rise to further uncertainty as to the applicable rules while the matter is considered by various levels of court.

While it is acknowledged that governments generally have the constitutional power to enact retroactive legislation, there is a very strong judicial presumption against reading a legislative measure as having retroactive effect. As stated by the Supreme Court of Canada in the case of *British Columbia* v. *Imperial Tobacco Canada Ltd.*,[7] "there is a presumption of statutory interpretation that a statute should not be given retroactive effect", stating further with respect to observers who perceive legislation that overturns settled expectation as unjust:

> "those who perceive it as such can perhaps take comfort in the rules of statutory interpretation that require the legislature to indicate clearly any desired retroactive or retrospective effects. Such rules ensure that the legislature has turned its mind to such effects and determined that the benefits of retroactivity [or retrospectivity] outweigh the potential for disruption or unfairness".

In the present case, the Ontario Legislature has had no opportunity to "turn its mind" to the disadvantages of disrupting settled expectations. The Government could easily have included the proposed change in its recent Budget, tabled in the Legislature only days after the New Regulation was filed, and yet decided instead to quietly file the New Regulation, thereby insulating it from the scrutiny of the Legislature where the matter could be debated in public. This is in stark contrast to the Government's approach to other changes to the Act.

In the context of the 2014 Ontario Budget, the then Minister of Finance expressed concern over perceived land transfer tax avoidance transactions and introduced a general anti-avoidance rule ("**GAAR**") in section 9.3 of the Act, with prospective effect, to address those concerns. Introducing targeted legislation with prospective effect would be a fair and balanced approach to addressing any perceived anomalies in the Exemption. The New Regulation, which has broad-reaching, adverse implications retroactive to 1989, has not had the benefit of public consultation or debate. In our view, this approach undermines transparency, trust and the rule of law.

In this context, we are of the view that a court may well determine that the statutory language in the Act authorizing the making of retroactive regulations to exempt certain classes of transactions

[7] [2005] S.C.R. 473.

cannot properly be construed to authorize the New Regulation, which amounts to an extremely unusual retroactive measure that functions as a charging provision. In view of the strong judicial presumption against retroactivity, a properly directed court could well find that the Legislature plainly did not intend to authorize retroactive taxation by way of regulation. It would follow from such a finding that the New Regulation would be invalid.

We believe that in the interests of certainty, predictability and fairness, the New Regulation should be rescinded, and any proposed modifications to the Exemption should be brought forward in a consultative and open manner. Years of uncertainty while the status of the New Regulation is considered by the courts would not be in the best interests of any stakeholders.

<u>Administrative Concerns</u>

The retroactive nature of the 2016 Exemption gives rise to a number of administrative concerns. Taxpayers who acted in compliance with the law at the time they undertook transactions may now find themselves in non-compliance, potentially for transactions that occurred as long as 27 years ago. This retroactive “non-compliance” raises a number of administrative concerns that go to the very heart of the Canadian legal system and the rule of law.

Pursuant to the Regulation, transactions that qualified for the Exemption were exempted from section 3 of the Act, and hence the obligation to pay the tax otherwise payable under subsection 3(2) of the Act. The retroactive nature of the 2016 Exemption means that taxpayers who were not liable to pay tax on transfers of partnership interests at the time of such transfers, now find themselves potentially non-compliant with respect to the obligation to pay the land transfer tax. Moreover, we note that a failure to pay the tax that is owing within 30 days of a taxable acquisition transfer results in the taxpayer being subject to the imposition of a penalty under subsection 7.1(4) of the Act.

A related administrative concern arises in connection with the obligation to deliver returns under subsection 5(7) of the Act. The Exemption not only exempted qualifying acquisitions of beneficial interests in land from tax payable under subsection 3(2) of the Act, but also exempted them from the requirement under subsection 5(7) to deliver a return to the Ministry reporting such transfer within 30 days of the acquisition of the beneficial interest in land. The retroactive amendment to the Exemption means that taxpayers who were not required to deliver a return at the time they entered into a transaction now find themselves potentially non-compliant with respect to the obligation to deliver a return. Once again, a failure to deliver a return within the 30-day period results in the taxpayer being subject to the imposition of a penalty, under subsection 7.1(3) of the Act.

The fact that taxpayers may, as a result of the retroactive nature of the 2016 Exemption, now find themselves subject to tax that was not otherwise payable at the time they entered into the applicable transaction is, by itself, deeply troubling. Furthermore, any such unpaid tax would normally be subject to arrears interest,[8] which, given the lengthy retroactive period covered by the New Regulation, could end up being well in excess of the tax payable. However, as written, the retroactive nature of the 2016 Exemption means that taxpayers, who were exempt from land transfer tax and related reporting obligations at the time they undertook certain transactions, also may potentially be subject to multiple penalties - one for failure to deliver a return within 30 days and a second for failure to pay the tax within the 30-day period - in respect of obligations that did not exist at the time they entered into the relevant transactions.[9] In our view, this would be unconscionable and simply cannot be supported. However, there is significant uncertainty about what approach the Ministry will take and, accordingly, we strongly encourage the Ministry to promptly provide clarity on these and a number of related issues as described in this letter.

As a practical matter, we expect that, due to the passage of time, in many cases it will be exceedingly difficult, perhaps impossible, for taxpayers to determine whether they were compliant with the 2016 Exemption in the past. As a starting point, the 2016 Exemption could require taxpayers to review all transactions undertaken in the past 27 years to determine whether the Exemption was relied on and, if so, whether it is possible to rely on the 2016 Exemption. We expect that in many cases the relevant documentation to enable parties to make this determination will no longer be available. (The Act provides for a seven-year document retention period following the filing of a return or the registration of a conveyance but those provisions would not have applied to transactions that qualified for the Exemption as a return was not required to be filed. Accordingly, taxpayers would not have been legally required to maintain records for the 27-year period to which the New Regulation is stated to apply.[10]) Furthermore, we expect that in many cases the identity of the relevant taxpayers – former partners or trust beneficiaries – will no longer be known and that many will have died, moved, been dissolved. etc., so that it may not be possible to determine who bears the ultimate liability for the tax or to locate them.

These concerns are particularly acute in the case of publicly-traded partnerships and trusts whose ownership interests have changed over the years. As a practical matter, it may be impossible to identify the beneficial owners of the real property at the time the beneficial ownership was acquired. Conversely, members and beneficiaries of closely-held partnerships and trusts that continue to operate may be readily identifiable. The result may be to unfairly impose tax on some taxpayers on a retroactive basis, while others escape liability.

<u>Retroactivity</u>

While we are generally not supportive of retroactive amendments, we understand that in some cases they may be necessary as a measure of last resort; for example, where a court has found a

---

8 Subsection 17(1) of the Act. The interest is levied at a prescribed rate (currently 6%) compounded daily.

9 It goes without saying that the Ministry cannot impose penalties on the basis an offence has been committed as contemplated in sections 6, 6.1 or 7 of the Act.

10 Consistent with this, the Ministry's guidance on document retention indicates that the Ministry will typically consent to destruction of documents seven years after the taxation year to which they relate. See Ontario's *"Retention/Destruction of Books and Records*".

statutory provision which has been relied on by taxpayers and the government for many years to be unconstitutional (as in the *Re Eurig Estate*[11] decision). However, we are deeply troubled by the use of a retroactive amendment in this case, which serves to re-write the rules after the fact to the detriment of taxpayers who arranged their affairs in reliance on the law as it was written at the time they entered into various transactions. The rule of law is a fundamental aspect of our society and a cornerstone of our democracy. Retroactive rule-making should be limited to the rarest of circumstances in order to promote the essential tenets of our tax system – certainty, predictability and fairness. As noted above, consistent with this principle, when the GAAR was added to the Act "to maintain the integrity of the land transfer tax system," it was made applicable only to transactions completed after the announcement date (May 1, 2014) or prior to the announcement date if the transaction was part of a series of transactions that was completed after the announcement date that meet the relevant conditions of the provision. This approach is far more consistent with the principles of certainty, predictability and fairness.

We also have a technical concern regarding the retroactive nature of the 2016 Exemption and its interaction with the limitation period provisions in the Act. As a general rule, subsection 12(4) of the Act prevents the Ministry from reassessing any person more than four years after the transaction giving rise to the obligation to pay land transfer tax was entered into. That general limitation does not, however, apply where the failure to report or pay the tax is due to neglect, carelessness or wilful default. Moreover, the four-year limitation period does not apply in circumstances where "the person has failed to deliver any return required by this Act". In such cases, the Ministry may assess or reassess the tax at any time the Ministry considers reasonable.

As noted above, subject to the New Regulation, taxpayers who fell within the Exemption were not required to deliver a return, because the transaction was exempted from section 3 of the Act, and thus from the corresponding requirement to deliver a return under subsection 5(7) of the Act. Based on the fact that the 2016 Exemption is made retroactive for a period of 27 years, we wonder whether the Ministry's intention, with respect to transactions that were previously exempted under the Exemption but are no longer exempted under the 2016 Exemption, is that the normal four-year limitation period in subsection 12(4) will not apply. If so, in addition to the concerns raised above regarding retroactivity, we are concerned that the retroactive nature of the 2016 Exemption effectively amounts to an indirect amendment of the normal four-year reassessment period in subsection 12(4) of the Act. As you will appreciate, any amendment to subsection 12(4) clearly falls outside the authority delegated to the Lieutenant Governor in Council to prescribe regulations, and falls within the exclusive purview of the Legislature. On this basis, we question whether the retroactive nature of the 2016 Exemption is authorized by subsection 22(2) or might amount to an improper exercise of delegated legislative authority. We urge the Ministry to clarify that the 4-year limitation period continues to apply.

[11] [1998] 2 S.C.R. 565.

Collateral Damage: Financial Reporting and Commercial Concerns

The impact that the retroactive land transfer tax has on financial reporting implications is significant. First, it must be determined whether the entity (such as a publicly-traded trust (a "**REIT**") or publicly-traded partnership) has any liability and, if so, how to quantify the liability. Clearly, given the change is stated to be retroactive to 1989, the Ministry must provide further guidance on how it intends to apply the New Regulation (including its position regarding the application of the limitation period in subsection 12(4) of the Act, and the requirement to file returns in respect of transactions that occurred prior to the announcement of the New Regulation, and whether it intends to offer administrative relief).

The Ministry should also advise whether assessments of the tax liability for the acquisition by trusts and partnerships of partnership interests will be issued to the beneficiaries and the partners, consistent with its past administration of the Act. In this respect, in addition to the difficulty in finding the appropriate beneficiaries and partners, it will be extremely difficult, perhaps impossible, to accurately compute the relevant land transfer tax liability. Consistent with the tax being payable by the beneficiaries and partners, it would be necessary to know the value of each beneficiary's and each partner's interest in the real property. In publicly-listed trusts and partnerships, the beneficiaries and partners may change daily. Some may be non-residents of Canada or tax-exempt entities. It seems obvious to us, and we assume to the Ministry, that it is highly unrealistic to expect such partners and beneficiaries to re-trace 27 years of transactions to determine whether they may be liable for land transfer tax by virtue of the changes implemented by the New Regulation.

Moreover, depending on the terms of the constating documents for the REIT (or partnership), the 27-year retroactive application of the New Regulation may potentially create a liability for the REIT (or partnership), with the result that it will be borne by the current beneficiaries (or partners) notwithstanding that the property may no longer be owned by the REIT (or partnership). This is expected to lead to a significant, unanticipated, and unreasonable financial burden on the affected trusts and partnerships. In some cases, the financial burden may be devastating.

The following examples illustrate the potential negative financial consequences in circumstances in which the Exemption was relied upon and it is retroactively no longer available:

1. A Canadian REIT must adhere to stringent leverage criteria, and typically a REIT intends to deliver steady and increasing distributions to its unitholders. These unitholders, particularly our senior citizens, necessarily rely on such distributions to fund their annual living costs.

   1.1. The maximum total indebtedness of a REIT is normally "hard wired" into its constating document. If significant unbudgeted borrowings are required to fund the land transfer tax payable by past unitholders as a consequence of the retroactive effect of the New Regulation, a REIT may be unable to borrow such funds without violating its constating documents.

   1.2. The immediate payment of a significant unbudgeted land transfer tax liability will create a significant financial drain on a REIT, and may make it difficult, particularly in the case of a smaller REIT, to maintain its distributions to its unitholders. Given the potentially significant tax, interest and penalties, no lender may be willing to advance funds to enable the REIT to pay the tax.

2. Syndicated special purpose trusts or partnerships may have sold their real property holdings and been dissolved long ago. There may be no remaining party or property to satisfy the land transfer tax payable as a consequence of the New Regulation.

3. Syndicated special purpose trusts or partnerships must determine their net asset value ("**NAV**") on a daily, monthly or quarterly basis. NAV is used to determine the price at which units are redeemed, purchased and issued in satisfaction of distributions. Because of the concerns raised in this submission, the potential land transfer tax liability, if any, resulting from the retroactive application of the New Regulation may not be determined until greater clarity is provided by the Ministry. Until such time, the NAV for units of such trusts and partnerships may be subject to material misstatement.

4. If a partnership interest was acquired and no land transfer tax was paid, on the basis the Exemption applied, the cost of that interest for income tax purposes will not have included any land transfer tax so that the gain (or loss) on a subsequent disposition of the partnership interest will have been overstated (or understated). This will potentially have significant income tax implications for partners and the trust unitholders. Given the retroactive application of the New Regulation, the relevant (income) taxation years of the partners and unitholders may well be statute-barred.

Additional Scope and Drafting Concerns

The discussion above sets out numerous reasons why we believe that it is inappropriate to apply the 2016 Exemption on a retroactive basis. In addition, we have identified several important concerns with how the 2016 Exemption will apply to transactions undertaken after the filing of the New Regulation.

Changes in drafting

The Exemption applies if the person seeking to rely on it would not be entitled to a percentage of profits of the partnership in the year of acquisition that exceeds, by more than 5%, the percentage of profits that the person was entitled to at the beginning of the fiscal period. The 2016 Exemption now distinguishes between a person who was previously a partner in the partnership and a person who became a partner in the partnership as a result of the disposition in question. Because the operative provision of the exemption continues to require that the increase in the profit percentage not exceed 5%, we do not understand the purpose of distinguishing between these two situations. If the Ministry intends that these two situations are to be treated differently in any respect, we suggest that the Ministry advise taxpayers of the intended difference. If there is no distinction, we believe that the separation into two distinct clauses is unnecessary.

The 2016 Exemption uses the words "as a partner" in certain clauses in subsection 1(2) of the New Regulation. The Exemption did not contain this requirement. We believe the Ministry should explain the reason for this addition. As noted above, if this is another attempt to ensure that the 2016 Exemption does not apply to a tiered structure (on the basis that a participant in an upper tier trust or partnership is not a "partner" in the acquired partnership), we believe that, whatever decision the Ministry makes on retroactivity, this addition should not apply on a retroactive basis. Jurisprudence supports the position that a partner in a partnership (upper tier partnership) is a partner in any partnership of which the first partnership is a partner (lower tier partnership).[12] Furthermore, we ask that the Ministry confirm that the *de minimis* exception would apply to the acquisition of a *de minimis* interest in a top-tier partnership (or trust) in a tiered partnership (or trust on partnership) structure.

Subsection 1(4) of the New Regulation provides that a partner means a limited partner or a general partner as determined under the *Limited Partnerships Act* (Ontario) where such a partnership has, or was required to, file a declaration under that act. We do not understand the need for this provision. We would have thought that the relationship of "partner" and "partnership" should be determined under the applicable governing law of the partnership. Furthermore, this provision does not address general partnerships or partnerships established in other jurisdictions (except, perhaps, to the extent that a limited partnership is required to file a declaration under the *Limited Partnerships Act* (Ontario) as an extra-provincial limited partnership because it owns real property situated in Ontario). We believe that the Ministry should elaborate on the rationale for this deeming provision.

De Minimis (Less than 5%) Acquisition by a Trust/Partnership

Subsection 1(3) of the New Regulation provides that subsection 1(2) does not apply if the partner who acquires the interest in the partnership is a trust or another partnership. Limiting the *de minimis* exception in this manner produces inappropriate and anomalous results. We have identified below a number of specific situations which demonstrate these concerns. We have no doubt that countless more examples of unfair and inconsistent taxation will be uncovered in the coming months as taxpayers begin to consider how the 2016 Exemption should be applied to their many varied structures.

<u>Private Trust</u>

Consider the example of a trust with a single beneficiary. If the beneficiary of the trust were to directly acquire a *de minimis* partnership interest (less than 5%), the *de minimis* exception would apply. However, if the trust acquires a *de minimis* partnership interest, the exception is not available pursuant to subsection 1(3) of the New Regulation. In both cases, the same person obtains the same beneficial interest in land as a result of the acquisition of the same *de minimis* partnership interest. We cannot think of any policy rationale or substantive basis to distinguish the land transfer tax consequences of these transactions. Our view would be the same if the trust

[12] See, for example, *Devon Canada Corporation v. The Queen* 2013 T.C.C. 415; *Major (Inspector of Taxes)* v. *Brodie* [1998] BTC 141 (Ch D); and *Green* v *R*. 2016 T.C.C. 10.

in our example had multiple beneficiaries. This is particularly egregious in the context of the retroactive application of the 2016 Exemption.

As drafted, we believe that the changes made by the New Regulation go well beyond any concerns that the Ministry could have had with the acquisition of *de minimis* partnership interests. We recommend that the scope and purpose of subsection 1(3) of the New Regulation be reconsidered. At a minimum, beneficiaries of a trust should not be liable to the tax where, had a single beneficiary directly acquired the partnership interest, the *de minimis* exemption would have been available.

Tiered Structures

We are concerned that the restriction in subsection 1(3) of the New Regulation (and possibly the change in wording in subsection 1(2) of the New Regulation, discussed below) will not apply properly to tiered structures. Trusts and partnerships (including multiple tiers of trusts and partnerships) may be used as investment vehicles for various reasons (including limiting liability, control rights, commercial/business considerations, financing requirements, family/succession planning, etc.). Creating a blanket restriction in the *de minimis* exception for trusts and partnerships not only creates anomalous land transfer tax results, but also may inappropriately influence investment decisions and structures.

Consider a real estate partnership fund with 50 equal individual partners. The fund is formed as a limited partnership (the "**Master Partnership**"). The Master Partnership has an interest in numerous real estate projects which are held in separate subsidiary limited partnerships for various commercial reasons. Assume the Master Partnership acquires a 50% interest in another existing real estate partnership. Historically, we would expect the *de minimis* exception to apply because each of the 50 partners would be treated as acquiring a 1% co-tenancy interest in the underlying real property by virtue of the acquisition of an interest in that other partnership. The New Regulation now precludes this result. In contrast, if each of the partners of the Master Partnership had instead directly acquired a 1% interest in that other partnership, the exemption would clearly apply in respect of the acquisition.

There is no supportable basis for the land transfer tax consequences of the two transactions described above to differ. In our view, any exemption from land transfer tax should apply equally regardless of whether the acquisition of a partnership interest is acquired at the top-tier or any other tier in an investment structure. We again ask that you reconsider subsection 1(3) of the New Regulation.

Trust Investments in Private Real Estate Funds

Private real estate funds are commonly structured as limited partnerships. Frequently, various types of trusts invest in such private real estate fund partnerships as limited partners. These include trusts governed by registered pension plans, First Nations trusts, charitable trusts and family trusts. Assuming that the trust has a less than 5% partnership interest in the limited partnership at all times, it is unfair that the trust would have to pay land transfer tax when it acquires limited partnership interests, or when its percentage interest in the fund is increased as a result of another investor's limited partnership interests being redeemed. Investors that are not trusts or partnerships would not be subject to land transfer tax in the same circumstances.

Private Real Estate Feeder Funds (Tiered Partnerships)

As noted above, private real estate funds are commonly structured as limited partnerships. Sometimes there are "feeder" funds that pool investments from different types of investors and in turn invest in the main fund limited partnership ("**Fund LP**").

To take a simple example, suppose that there are two feeder funds that invest in Fund LP, which directly acquires Ontario real estate. The first feeder fund ("**Feeder LP**") is structured as a limited partnership, and the second feeder fund ("**Feeder Ltd.**") is structured as a corporation. The Fund LP has monthly closings of new investments, and also permits redemptions by investors. The percentage interest that each of Feeder LP and Feeder Ltd. has in Fund LP accordingly fluctuates monthly as a result of additional investments and redemptions.

For example, consider a small investment in Fund LP made through Feeder LP which results in the new investor (which is not itself a trust or partnership) acquiring a 1% interest in Feeder LP. Assume no investment is made through Feeder Ltd. at the same time (and there are no redemptions at the same time), and that Feeder LP's percentage interest in Fund LP increases by 0.5%. The 2016 Exemption would not be available to the new investor (even though it is not a trust or a partnership), because the acquisition of the additional 0.5% interest in Fund LP (the partnership that owns the real estate) is an acquisition by another partnership, Feeder LP, of an interest in a partnership.

To take another example, consider that a small investor in Feeder Ltd. that redeems its shares of Feeder Ltd., and as a result Feeder Ltd. redeems some of its interests in Fund LP to fund its obligation to pay the share redemption price, resulting in Feeder LP's interest in Fund LP increasing by 0.1%.None of the investors in Feeder LP would be entitled to the 2016 Exemption because Feeder LP's "acquisition" of the additional percentage interest in Fund LP is an acquisition by another partnership.

Full land transfer tax will have been paid when Fund LP acquired the Ontario real estate, and so this is truly a case of small changes in the percentage interests in an existing partnership that already owns "tax paid" real estate, the very situation the *de minimis* Exemption was intended to cover. It may not be feasible or desirable for commercial reasons for existing funds and feeder funds to be restructured to eliminate the tiers, so the loss of the *de minimis* Exemption would put them in an untenable situation.

Distribution Reinvestment Plans

Many REITs have distribution reinvestment plans ("**DRIPs**"), which allow unitholders to reinvest the distributions in additional units of the REIT. In some cases, the REIT is a partner of a "subsidiary" partnership in which there are also third party limited partners whose limited partnership units are "exchangeable" for units of the REIT. Often the DRIP is structured so that where a unitholder "reinvests" in REIT units, the REIT correspondingly "reinvests" in limited partnership units (to increase the number of limited partnership units the REIT holds to align with the number of outstanding REIT units). The reinvestment at the partnership level increases the interest of the REIT in the partnership, usually by modest amounts (typically much less than 5% on an annual basis). This increase in interest was normally exempt from land transfer tax under the Exemption by looking through the REIT to its unitholders as partners. Under the 2016 Exemption, a DRIP structured in this manner will give rise to land transfer tax and administrative filing burdens every time the REIT reinvests in limited partnership units under the DRIP (even in circumstances where the increase in the interest of the REIT is much less than 5%). It may not be possible to restructure or cancel existing DRIPs to avoid these burdens.

Conclusion

In our view, the Government should reconsider the effective date and scope of the New Regulation. As expressed above, we are doubtful that there is authority to retroactively revoke an existing exemption under the power to make regulations. However, more importantly, consistent with the Government's past practice and with the fundamental principles of fairness, certainty and predictability in tax matters, we believe it is imperative that the change in law effected by the New Regulation apply only on a prospective basis (i.e., to transactions that occur after February 18, 2016) and that a change of this nature should be passed in the Legislature. This is critically important, not only for the reasons described above, but because we are concerned that a retroactive change of this nature may have an impact on the confidence that investors may have in investing in Ontario.

For the reasons described above, we also believe a number of circumstances are inappropriately falling outside the scope of the 2016 Exemption as drafted. The uncertainty surrounding the scope of the New Regulation creates a disincentive for REITs and private real estate funds to invest in Ontario and Toronto. In our view, the Ministry should immediately provide guidance concerning its intentions regarding taxpayers' obligations to file returns and to pay tax, interest, or penalties in respect of past transactions, the scope of the limitation period, and administrative relief. The prevailing uncertainty is causing significant confusion and anxiety.

We would like to engage in a consultation process with the Ministry with the objectives of addressing these anomalies in a fair and practical way while recognizing the Ministry's objective to levy land transfer tax in circumstances that it believes to be appropriate. We remain ready and willing to participate in such a dialogue.