



Input Tax Credits for Holding Corporations and Corporate Takeovers

This memorandum discusses the provisions of section 186 of the *Excise Tax Act* (the Act), which are special case provisions under Division II, *Imposition of Tax*. If the conditions in section 186 are satisfied, certain inputs acquired, imported or brought into a participating province by a corporation are deemed for purposes of determining input tax credits (ITCs) to have been acquired for use in the course of that corporation's commercial activities.

Note This section of Chapter 8 cancels and replaces GST Memorandum 700-5-6, *Input Tax Credits for Holding Companies, Takeovers and Multi-tiered Corporations* dated December 9, 1991. It also incorporates the information from the following GST/HST policy statements: P-023, *Interpretation of "All or Substantially All"*, P-137, *Availability of ITCs to Holding Corporations on Cost of Acquisition*, P-196, *Whether Administrative Overhead Costs Fall Under Subsection 186(1) of the Excise Tax Act*.

Disclaimer The information in this memorandum does not replace the law found in the *Excise Tax Act* (the Act) and its regulations. It is provided for your reference. As it may not completely address your particular operation, you may wish to refer to the Act or appropriate regulation, or contact any Canada Revenue Agency GST/HST rulings office for additional information. A ruling should be requested for certainty in respect of any particular GST/HST matter. Pamphlet RC4405, *GST/HST Rulings – Experts in GST/HST Legislation* explains how to obtain a ruling and lists the GST/HST rulings offices. If you wish to make a technical enquiry on the GST/HST by telephone, please call 1-800-959-8287.

If you are located in Quebec and wish to make a technical enquiry or request a ruling related to the GST/HST, please contact Revenu Québec at 1-800-567-4692. You may also visit the Revenu Québec Web site to obtain general information.

Note – HST Reference in this publication is made to supplies that are subject to the GST or the HST. The HST applies in the participating provinces at the following rates: 13% in Ontario, New Brunswick and Newfoundland and Labrador, 15% in Nova Scotia, and 12% in British Columbia. The GST applies in the rest of Canada at the rate of 5%. If you are uncertain as to whether a supply is made in a participating province, you may refer to GST/HST Technical Information Bulletin B-103, *Harmonized Sales Tax – Place of Supply Rules for Determining Whether a Supply is Made in a Province*.

ITCs of a holding corporation

ss 186(1) and 186(3) 1. Subsection 186(1) sets out rules for registrant corporations that are resident in Canada and invest in related corporations that are engaged in commercial activities. These rules are designed to enable such corporations to claim input tax credits (ITCs) to the extent their expenses relate to the shares of the capital stock or indebtedness of those related corporations. The deeming provision of subsection 186(3) extends the application of subsection 186(1) to certain related holding corporations. The following discussion examines these two subsections in turn and their interaction.

Deemed for use in commercial activities 2. Subsection 186(1) applies to registered Canadian corporations (referred to as “parent” corporations) that acquire property or services that relate to shares or indebtedness of related corporations where the related corporations acquired, imported or brought into a participating province all or substantially all of their property for consumption, use or supply in the course of their commercial activities. Where the conditions under subsection 186(1) are met and only for purposes of determining an ITC of the parent corporation, to the extent the property or services are acquired, imported or brought into a participating province by the parent corporation for

consumption or use in relation to the shares of the capital stock or indebtedness of a related corporation, the property or services are deemed to have been acquired to that extent for use in the course of commercial activities of the parent corporation. This deeming provision permits the parent corporation to claim ITCs in respect of these inputs if the other requirements for ITCs set out in section 169 are satisfied.

Conditions for subsection 186(1)

– applies to corporations

3. Subsection 186(1) applies to corporations. If the person acquiring the property or service that relates to the shares of the capital stock or debt of a related corporation is not itself a corporation, e.g., it is a partnership, trust or individual, subsection 186(1) does not apply. Similarly, if the related person is an entity that is not a corporation, subsection 186(1) does not apply.

– property test
para 186(1)(b)

4. For the deeming provisions of subsection 186(1) to apply to an input of the parent corporation, the other corporation must have acquired its property for use in commercial activity. Specifically, at the time that GST/HST in respect of the acquisition, importation or bringing in of the input of the parent corporation becomes payable, or is paid without having become payable, all or substantially all of the property of the other corporation must be property that was last acquired or imported by the other corporation for consumption, use or supply by the other corporation exclusively in the course of its commercial activities. Note that “exclusively” generally means 90% or more for non-financial institutions and 100% for financial institutions.

Example 1

ParentCo is a GST/HST registrant and a resident in Canada. It is related to MiningCo since it owns all the shares of MiningCo. All of the property of MiningCo is property that it acquired for consumption, use or supply in its commercial activities. ParentCo incurs legal fees that relate to selling 10% of the shares of MiningCo. At the time that GST/HST became payable in respect of the legal fees that ParentCo incurs to sell these shares, all or substantially all of the property of MiningCo is property that was acquired for consumption, use or supply in its commercial activities. Therefore, the provisions of subsection 186(1) apply to deem the legal services related to selling the shares to have been acquired by ParentCo for use in commercial activities.

Example 2

ParentCo has accounting costs that relate to the shares it holds of its wholly owned subsidiary, a manufacturing corporation. In addition to the property that it uses in its own operations, the manufacturing corporation also holds shares of unrelated corporations. The shares of unrelated corporations form 20% of the manufacturing corporation's property. Since only 80% of the property of the manufacturing corporation is property that was acquired for use exclusively in the course of its commercial activities, the provisions of subsection 186(1) cannot apply to the accounting costs incurred by the ParentCo that relate to the shares of its subsidiary that it holds.

– registrant: voluntary
registration to GST/HST
subpara 240(3)(d)(i)

5. For subsection 186(1) to apply, the parent corporation must be a registrant. Where the only activity of a corporation is to hold the shares or debt of another corporation, generally there would be no commercial activity and no eligibility to register for GST/HST purposes. However, where a corporation resident in Canada owns shares of the capital stock of or holds indebtedness of a related corporation and all or substantially all of the property of the related corporation meets the property test described in paragraph 4, the holding corporation is allowed to register under the provisions of subparagraph 240(3)(d)(i). Note that there is no requirement for the corporation whose shares or indebtedness is held by the holding corporation to be a registrant.

– resident	6. The corporation that incurs the expenses in relation to the shares of the capital stock, or indebtedness, of the related corporation must be resident in Canada. There is no requirement for the related corporation to be resident in Canada.
– related corporations	7. The two corporations must be related as determined under subsection 126(2), that is, they are related for the purposes of subsections 251(2) to (6) of the <i>Income Tax Act</i> .
– related at the time	8. For subsection 186(1) to apply, the two corporations must be related at the time the property or service was acquired or imported. Consequently, ITCs for costs relating to the acquisition of shares where the corporations are not related would not be allowed even if the corporations may become related by virtue of such acquisition. However, costs related to the acquisition of additional shares at a time when the two corporations are already related could give rise to ITCs provided the other conditions of subsection 186(1) and subsection 169(1) are satisfied (for information about corporate takeovers, see paragraphs 17 to 25).
– purpose test para 186(1)(a)	9. Subsection 186(1) requires that the property or service acquired by the parent corporation must be such that it can be reasonably regarded as having been acquired, imported or brought into a participating province by the parent corporation for consumption or use in relation to the shares of the capital stock or indebtedness of the other corporation that is related to the parent. 10. The GST/HST is a transaction tax that generally links inputs that are acquired by a person to the first order of supply to which they relate when determining the person's eligibility for ITCs. Generally, the ITC rules would disallow an ITC on inputs related to the acquisition or disposition of shares or indebtedness of a related corporation because the inputs would be related to a supply of a financial service that is generally exempt from GST/HST. Subsection 186(1) provides an exception to the normal ITC rules but only for certain inputs of the parent corporation where the specific conditions are met.
"reasonably be regarded ... in relation to" ss 186(1)	11. Whether a particular property or service can reasonably be regarded as being acquired, imported or brought into a participating province by the parent corporation for consumption or use in relation to the shares or debt of a related corporation, and the extent of this relationship, is a question of fact. Each case must be examined in light of its particular circumstances to determine whether subsection 186(1) would apply.
Example 1	BlueCo, a GST/HST registrant and resident in Canada, owns 55% of the shares of WhiteCo. Thus, it is related to WhiteCo. All or substantially all of the property of WhiteCo is property that it last acquired for consumption, use or supply exclusively in the course of its commercial activities. BlueCo has made a loan to WhiteCo that is secured by WhiteCo's real property assets. In considering whether or not to increase its loan to WhiteCo, BlueCo hires an appraisal service to have the real property appraised. Since these appraisal services relate to the debt of a related corporation that BlueCo holds, these services would be deemed under the provisions of subsection 186(1) to have been acquired for use in the course of commercial activities of BlueCo for the purposes of determining an ITC.

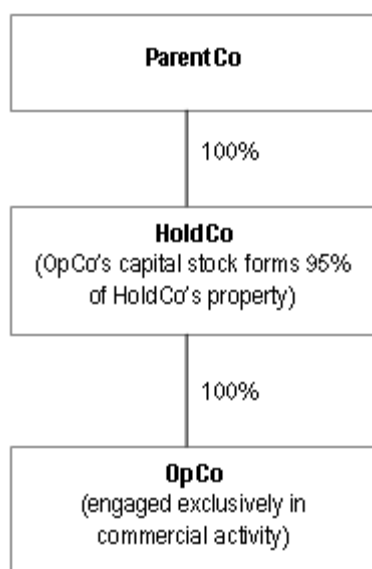
Example 2	<p>BlueCo, a GST/HST registrant and resident in Canada, is related to several subsidiaries and substantially all of its assets are the shares and debt of these subsidiaries. BlueCo acquires properties and services to organize the annual general meeting of its own shareholders. Since these properties and services relate to the corporate entity that is BlueCo and not to the shares or debt of its subsidiaries, subsection 186(1) would not apply to these properties and services.</p>
Example 3	<p>HoldCo is a corporation that is a GST/HST registrant and resident in Canada. It owns 51% of the shares of the capital stock of another corporation, OpCo, which carries on the manufacturing of widgets. All OpCo's property was acquired for consumption, use or supply in that activity. HoldCo is proposing to issue shares of its own in order to finance the purchase of a further 15% of the shares of OpCo. HoldCo will pay GST/HST on legal and accounting services acquired to issue the shares.</p> <p>HoldCo will not be entitled to claim ITCs by virtue of subsection 186(1) in respect of the legal and accounting services because it cannot reasonably be regarded as acquiring the services for consumption or use in relation to the shares of OpCo. Rather, the services will be acquired for consumption or use in relation to HoldCo issuing shares of its capital stock (the first order of supply) and not for consumption or use in relation to the shares of OpCo. As such, the legal and accounting services are not deemed to be for use in commercial activities of HoldCo to any extent under subsection 186(1).</p>
Direct and indirect costs	<p>12. Where the requirements of subsection 186(1) have been met, both direct costs, for example, accounting and legal services on the further acquisition of shares, and indirect costs, such as administrative overhead, can qualify under subsection 186(1), provided the parent corporation can demonstrate that the costs meet the requirements of subsection 186(1).</p>
Allocation of inputs	<p>13. Evaluating whether a particular property or service meets the requirements of the subsection includes examining the nature of the property or service to see if it is reasonable that there is a relationship between the consumption or use of the property or service and the shares of the capital stock, or indebtedness of the related operating corporation. If it is reasonable that there is such a relationship, the extent of the relationship must then be determined—whether it is wholly or partially attributable to the shares or debt of the related corporation. For example, the parent corporation is required to allocate its inputs between the activity of acquiring, holding and disposing of shares and indebtedness of the related operating corporation, and other activities that are not commercial activities such as raising its own capital by issuing shares or borrowing money, and acquiring shares or debt of non-related corporations. For further information and discussion about ITCs, see GST/HST Memorandum 8.3, <i>Calculating Input Tax Credits</i>.</p>
Example	<p>HoldCo is a corporation that is a GST/HST registrant and resident in Canada. It owns 51% of the capital stock in each of OpCo, Aco, Bco, Xco, Yco and Zco (the corporations). The corporations have outstanding loans from HoldCo. HoldCo invests in shares of unrelated corporations. The corporations are engaged exclusively in the manufacturing of widgets. All of the property of each corporation was acquired for consumption, use or supply exclusively in the manufacturing of widgets. HoldCo has employees for whom it provides office space, furniture and equipment. HoldCo pays GST/HST on a monthly basis for the rental of office space and office equipment.</p> <p>In this situation, HoldCo is entitled to ITCs to the extent that the inputs relate to the activity of acquiring, holding or disposing of the shares and indebtedness of the related corporations. To the extent that the rental of office space and equipment relates to either managing the holding corporation and its share structure or buying and holding shares in unrelated corporations, which are not activities to which subsection 186(1) would apply, an allocation must be made.</p>

Deemed acquired for use in commercial activity: subsection 186(3)

14. Subsection 186(3) provides that where all or substantially all (generally 90% or more) of the property that a particular corporation acquired or imported for consumption, use or supply exclusively in the course of its commercial activities, shares of its capital stock held by a related corporation or indebtedness of the particular corporation owed to the related corporation are deemed, for purposes of section 186, to be property acquired by the related corporation for use exclusively in the course of the related corporation's commercial activities. Note that subsection 186(3) does not impose residency or registration requirements for its deeming provisions to apply.

Example 1

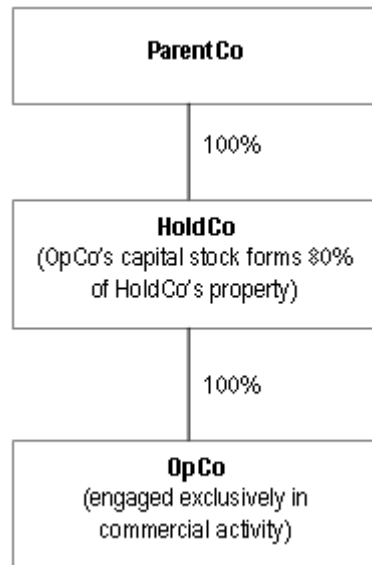
ParentCo owns 100% of the capital stock of HoldCo, which owns 100% of the capital stock of OpCo. OpCo is engaged exclusively in commercial activities. All of OpCo's property was acquired for consumption, use or supply in commercial activities. The capital stock of OpCo forms 95% of HoldCo's property.



ParentCo engages accounting services to evaluate the advantages and disadvantages of long-term holding of the capital stock of HoldCo. Under the provisions of subsection 186(1), the accounting services that ParentCo acquires in relation to HoldCo's capital stock would be deemed to have been acquired in the course of the commercial activities of ParentCo if all or substantially all of the property of HoldCo had been acquired for consumption, use or supply exclusively in HoldCo's commercial activity. Since OpCo satisfies the property test of subsection 186(3) (i.e., all or substantially all of OpCo's property is property that was acquired or imported for consumption, use or supply exclusively in the course of OpCo's commercial activities), subsection 186(3) deems the capital stock of OpCo that is owned by HoldCo to be property that HoldCo acquired for consumption, use or supply exclusively in its commercial activity. Also, since OpCo's capital stock forms all or substantially all of HoldCo's property, then HoldCo's property satisfies the property test of subsection 186(1). Thus if ParentCo is a GST/HST registrant and resident in Canada as required under subsection 186(1), it could claim ITCs for these accounting services provided the other requirements for ITCs under section 169 are met.

Example 2

ParentCo owns 100% of the capital stock of HoldCo, which owns 100% of the capital stock of OpCo. OpCo is engaged exclusively in commercial activities. All of OpCo's property was acquired for consumption, use or supply in commercial activities. However, even though subsection 186(3) deems all the capital stock of OpCo that is owned by HoldCo to be property that HoldCo acquired for consumption, use or supply exclusively in its commercial activity, OpCo's capital stock forms only 80% of HoldCo's property. The remaining property of HoldCo is capital stock of unrelated corporations. Consequently, since HoldCo's property does not satisfy the property test of subsection 186(1) (i.e., all or substantially all of its property is to be acquired or imported for consumption, use or supply exclusively in the course of commercial activities), ParentCo cannot claim ITCs for any property or service it may acquire that relates to the shares of HoldCo.



More than two levels

15. While the preceding examples show only one holding corporation between the parent corporation and the operating corporation, there could be additional holding corporations in the ownership structure with each holding capital stock or indebtedness of the corporation one layer down. Where the corporation seeking to claim ITCs for expenses that it incurred in relation to shares or indebtedness of a related corporation satisfies the conditions of subsection 186(1) and where the requirements of subsection 186(3) are met at each level of an ownership structure, the provisions of section 186 can apply to deem the expenses to have been acquired for use in the course of commercial activities of the corporation that incurred the expenses.

16. Since section 186 applies only to corporations, the effect of the interaction of subsections 186(1) and 186(3) ends where a partnership, trust or other non-corporate person is used as an entity in the ownership structure.

ITCs for takeovers

17. As indicated in paragraph 10, a person is generally not able to claim ITCs for GST/HST paid or payable in relation to the acquisition of shares of the capital stock of a corporation since a share is a financial instrument. For GST/HST purposes, expenses incurred to acquire a financial instrument are not usually expenses incurred in the course of commercial activity. Subsection 186(2) provides an exception to this general rule.

Required conditions under subsection 186(2)

Expenses related to takeovers ss 186(2)	<p>18. Under subsection 186(2), if a corporation (the purchasing corporation) acquires or proposes to acquire all or substantially all of the issued and outstanding shares, having full voting rights under all circumstances, of the capital stock of another corporation (the target corporation), any property or service that the purchasing corporation acquires in the course of the takeover or attempted takeover are deemed to have been acquired in the course of commercial activities, if certain conditions are met.</p>
Voluntary registration subpara 240(3)(d)(ii)	<p>19. For subsection 186(2) to apply, the purchasing corporation must be resident in Canada and a registrant. Under the provisions of subparagraph 240(3)(d)(ii), a particular corporation that is resident in Canada may register voluntarily if it is acquiring, or proposes to acquire, all or substantially all of the issued and outstanding shares of the capital stock of another corporation, having full voting rights under all circumstances where all or substantially all of the property of the other corporation is, for the purposes of section 186, property that was last acquired or imported by the other corporation for consumption, use or supply exclusively in the course of its commercial activities.</p>
Property test for target corporation para 186(2)(b)	<p>20. For subsection 186(2) to apply, all or substantially all of the property of the target corporation must be property that was acquired or imported for consumption, use or supply exclusively in the course of commercial activities. This requirement that applies to the property of the target corporation must be met during the period:</p> <ul style="list-style-type: none">• beginning when the performance of the service being acquired by the purchasing corporation began, or when the purchasing corporation acquired, imported or brought in to a participating province, as the case may be, the particular property, and• ending the later of the day the purchasing corporation acquired all or substantially all of the shares of the target corporation or the day the intention to acquire the shares was abandoned. <p>21. In addition, to be subject to the deeming provisions of subsection 186(2), the properties or services acquired by the purchasing corporation must relate to the acquisition or proposed acquisition of the required shares of the target corporation.</p>
Example 1	<p>PurchasingCo, a resident in Canada and a GST/HST registrant, prepared a takeover bid for TargetCo. It incurred expenses for legal and financial advisory services. The legal services provided by LegalCo relate to the undertaking of due diligence concerning the current financial position of TargetCo. The financial advisory services provided by AdvisorCo involved its undertaking of a study to enable the rendering of an opinion as to the fairness of the financial consideration to be paid by PurchasingCo for the shares of TargetCo. During the period beginning with the start of the performance of the legal and financial advisory services and ending with the purchase of the shares, all or substantially all of the property of TargetCo was property that was acquired or imported for consumption, use or supply exclusively in the course of commercial activities. Therefore, these particular services provided by LegalCo and AdvisorCo to Purchasing Co are deemed under the provisions of subsection 186(2) to be acquired by PurchasingCo for use exclusively in the course of commercial activities.</p>

Example 2

Corporation A, having full voting rights under all circumstances, proposes to acquire all or substantially all of the issued and outstanding shares of target Corporation B. All or substantially all of the property of target Corporation B is property that was acquired or imported for consumption, use or supply exclusively in the course of commercial activities. Corporation A incurs costs relating to an offering of its own shares that it undertakes to raise capital to purchase the required shares of target Corporation B. Subsection 186(2) does not apply to these costs since they relate to the offering of Corporation A's shares. They do not relate to the acquisition or attempted acquisition of the shares of target Corporation B.

22. The takeover bid must result in, or, if it were successful, would have resulted in the purchaser owning all or substantially all of the issued and outstanding shares, having full voting rights under all circumstances of the target corporation. For example, if a registrant corporation holds 40% of the issued and outstanding shares and then acquires or attempts to acquire sufficient shares that, when added to the shares already held, would give it all or substantially all of the issued and outstanding shares having full voting rights under all circumstances of the target corporation, it could be eligible to claim ITCs for property or services acquired that relate to acquiring any of the required shares, provided the other requirements for claiming ITCs under section 169 are met. However, it is important to note that subsection 186(2) would not apply to the initial acquisition unless it can be shown that the subsequent purchase was part of the initial proposal.

23. If the takeover bid is for all or substantially all of the issued and outstanding shares, but less than that amount is tendered and accepted, subsection 186(2) of the Act may still apply.

When tax deemed payable or paid para 186(2)(c) and (d)

24. For the purpose of claiming an ITC, the GST/HST in respect of the property or service is deemed to have become payable and been paid by the purchaser on the later of:

- the later of the day all of substantially all of the shares of the target corporation were acquired and the day the intention to acquire the shares is abandoned; and
- the day the tax became payable or was paid by the purchaser.

25. The purchasing corporation must also meet all other requirements with respect to claiming ITCs, such as documentary requirements and claiming the credit within the specified time limits.

26. For more information relating to the entitlement to claim ITCs, refer to the other memoranda in Chapter 8, *Input Tax Credits: Eligible ITCs*, of the GST/HST Memoranda Series. For additional information relating to financial institutions claiming ITCs, see the following Technical Information Bulletins: B-097, *Determining Whether a Financial Institution is a Qualifying Institution for Purposes of Section 141.02*, B-098, *Application of Section 141.02 to Financial Institutions That Are Qualifying Institutions*, B-099, *Application of Section 141.02 to Financial Institutions That Are Not Qualifying Institutions* and B-106, *Input Tax Credit Allocation Methods for Financial Institutions for Purposes of Section 141.02 of the Excise Tax Act*.

Enquiries by telephone

Technical enquiries on the GST/HST: 1-800-959-8287

General enquiries on the GST/HST: 1-800-959-5525 (Business Enquiries)

If you are located in Quebec: 1-800-567-4692 (Revenu Québec)

All technical publications on GST/HST are available on the CRA Web site at www.cra.gc.ca/gsthsttech.