



Tips and traps - acquisitions in the oil and gas sector



Outline

- GST/HST - Real property acquisitions
- GST/HST - Transfer of natural resource rights
- GST/HST – Section 167 election and joint ventures
- GST/HST - Transaction Costs – Closure of Business
- GST/HST – Pre-closing GST/HST Debt of Vendor
- BC PST – Taxable Assets
- BC PST – Real property – Affixed Machinery
- BC PST – Production Machinery & Equipment Exemption
- Manitoba PST – Expanded definition of real property and exceptions
- Saskatchewan PST – Oil and gas assets
- PST Transaction Costs – Have you factored PST on the transaction costs?
- PST – Bulk Clearance Certificate
- PST – PST on Legal/Advisory Fees

GST/HST – Real property

GST/HST – Real property

- Real property transfer
 - self-assessment by a registered purchaser of real property
 - *Franklin Estate Inc. v. Canada*, [1994] G.S.T.C. 64 (TCC)
 - RITS 25599
- CRA Administrative policy - administrative concessions if the purchaser does not self-assess under subsection 228(4) and claim full ITCs
 - File No. 11695-7-2, 11685-8
 - File No. 11620-1

Trap: Parties cannot just decide for a vendor to collect the tax



GST/HST – Natural Resources Rights

- Subsection 162(2) of the ETA - deems the following not to be a supply:
 - a supply of a right to explore for or exploit a deposit of minerals
 - A supply of a related right of entry or user,
 - a related right to receive a royalty or profit interest
- What is meant by “explore or exploit”?
 - *Dunbar v. The Queen*, 2005 TCC 769
 - Draft GST/HST Memorandum 3.7, Natural Resources

Trap: 162(2) does not apply to natural resources rights that are part of “fee simple” interest in land”

GST/HST – Natural Resources Rights (con't)

- What is the consequence of 162(2)?
 - Tangible assets – taxable
 - Intangibles (i.e., natural resources rights) – not taxable
 - In most cases, 80% of value attributed to oil and gas rights as “Intangibles” and 20% of value attributed to Tangibles
- Purchaser pay GST on tangible assets only
- Real property v. tangible personal property
 - In practice, the GST is collected from the purchaser on all the “Tangible” portion, unless an election

Tip: If there is a concern with cash flow, and no section 167 election can be made, divide the “tangible” portion between real property and tangible personal property.

GST/HST - Section 167 election and joint ventures

- Most oil and gas assets are explored and exploited as joint ventures
 - GST/HST Policy Statement P-171 – Distinguishing between JV and Partnership
- Parties generally make the election under s. 273 of the ETA
- Section 167 election – may be used for the transfer of undivided interest in JV:
- Does it meet the requirement of transferring a business or part of a business?
 - Is it a JV?
 - CRA in GST/HST Memoranda Series – 14.4: "...to the extent the recipient purchases all of the supplier's undivided interest in all the joint venture property and the rights and obligations attached to this interest, qualify as having acquired a business or part of a business."
- It should also meet the remaining requirements of s. 167 of the ETA
- See GST/HST Memorandum Series -14.4 – Sale of a Business or Part of a Business

Trap: If the assets are not operating assets, there is a risk that s. 167 election would not apply
See - *Low Cost Furniture Ltd v The Queen*, [1997] GSTC 77; 1997 GTC 1171 (TCC)

GST/HST -Recovery

- Does the ITC claimant meet all the requirements of claiming ITCs?
 - Recipient of the supply – 169(1) of ETA and
 - Commercial activity – 169(1) of ETA
 - Tax becoming payable – 169(1) of ETA
 - Information requirements – 169(4) of ETA
- Can a seller claim ITCs if the seller has no commercial activity left after selling operating assets?
 - Yes – 141.1(3) of ETA – “to the extent that a person does anything ... in connection with the ...disposition or termination of a commercial activity of the person, the person shall be deemed to have done that thing in the course of commercial activities of the person.”

Transaction Costs

- Can they claim ITCs for the assumption of pre-closing liabilities of vendor?
 - Certain Limitations
 - See *Telus Communications (Edmonton) Inc. v. The Queen*, 2008 TCC 5; aff'd, 2009 FCA 49
 - Telus paid for supplies pursuant to assumption of pre-closing liabilities of the supplier
 - Supplies were contracted for by Edmonton Telephone Company ("Ed Tel" or "Vendor") and made by suppliers before acquisition of business but had not been paid for at time of acquisition.
 - Ed Tel was not released of its liability to suppliers.
 - There was no contractual relationship between the suppliers to Ed Tel and Telus.
 - Court found Ed Tel, rather than Telus to be the recipient
 - Telus could not claim ITCs



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Transaction Costs (con't)

- Share Transaction – Financial service and not subject to GST/HST
- Section 185 – Financial service “related” to commercial activity – ITC available
- Section 186 – Holding companies can claim ITCs if you meet certain requirements.
- These sections have a number of requirements.
- You must be made aware of the transaction to allow for ITCs



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GST/HST - GST/HST – Pre-closing GST/HST Debt of Vendor

- Pre-closing GST/HST debt of vendor does not transfer with asset transfer to the purchaser
- Pre-closing GST/HST liabilities do transfer with share transfer or acquiring interest in a partnership
- Section 270 of the ETA – Clearance Certificate to be obtained by a representative when the person distributes property or money as well as winding up
 - Failure – representative may be found liable for any GST/HST debt.
 - Form GST325 - Application for Clearance Certificate

Tip: Purchaser of business assets does not have to do due diligence for GST/HST

BC PST – Taxable Assets

- PST applies to taxable assets – Tangible Personal Property (“TPP”), software
- PST does not apply to oil and gas rights, intangible personal property (“IPP”) (excluding software), real property
- PST would not apply if taxable property was specifically exempt from PST
- One would need to break down the assets to distinguish TPP, real property, IPP, software
- Taxable TPP and Taxable software must be broken down from exempt TPP and exempt software

BC PST – Real Property

- PST does not apply to real property
- Exception – Affixed Machinery – TPP
- What is Affixed Machinery?
 - Machinery, equipment or apparatus that is used directly in the manufacture, production, processing, storage, handling, packaging, display, transportation, transmission or distribution of tangible personal property or the provision of software or a service; and
 - It must be affixed to, or installed in, a building, a structure or land so that it ceases to be personal property at common law

BC PST – Real Property

- What is excluded from Affixed Machinery?
 - heating, air conditioning or lighting a building or structure,
 - sewage disposal for a building or structure, or
 - lifting persons or freight within a building or structure by elevator or escalator; and
 - certain large machinery that must be constructed at the site with some additional requirements

Tip: Portable Buildings are generally TPP (unless installed into realty)

Trap: When equipment runs on rail or track, it could be “affixed machinery,” regardless of size

BC PST – Production Machinery and Equipment Exemption (Oil & Gas Producers)

- Section 95, *Provincial Sales Tax Exemption & Refund Regulations* (“PSTRR”)
- PST Bulletin 113 - Oil and Gas Industry – Producers and Processors
- Machinery or equipment obtained for use in British Columbia primarily and directly in the extraction or processing of qualifying petroleum or natural gas.
 - Only if the machinery or equipment obtained for use primarily at the well site or at the qualifying part of the processing plant or refinery.
- What is primarily?
 - Over 50%
- What is directly?
 - Administrative – “PM&E must be a part of, or an integral component of, the process that transforms the raw material into the marketable product.”
 - *Domtar Inc. v. The Queen*, 2007 BCCA 49

Tip: Most equipment in the gas processing plant would be exempt

Trap: The very last compressor in a plant may not be exempt

BC PST - Production Machinery and Equipment Exemption (Oil & Gas Service Companies)

- Section 94, PSTRR
- PST Bulletin 114 - Oil and Gas Industry – Exploration, Discovery and Development
- Requirement 1:
 - Obtained by a person:
 - who, for commercial purposes, regularly engages in the exploration for, discovery of or development of petroleum or natural gas, and
 - for use substantially in the exploration for, discovery of or development of petroleum or natural gas.
- What is regularly?
 - Person must undertake the activity on a routine basis
- What is substantially?
 - Over 90%

PST - Production Machinery and Equipment Exemption (Oil & Gas Service Companies)

- Requirement 2:
 - Must be on the prescribed list. Examples include:
 - Drilling rigs, including derricks, substructures and foundations; circulating systems, pumps, cement equipment, engine or power plant
 - Truck-mounted service rigs;
 - Portable doghouses, portable winches and portable pickers;
 - Boilers and steamers, required for heating blowout preventers;
 - Parts of pump truck (excluding chassis);
 - Hardware for drilling, including drill bits
 - Machinery and equipment obtained for use in well logging and drill stem testing;
 - Machinery and equipment obtained for hydraulic fracturing
 - Dehydrators, heaters, pressure piping system
 - Shelters substantially for protective covering of PME
 - Support mats
 - Automotive unit is excluded

BC PST - Production Machinery and Equipment Exemption

Other PME exemptions:

- Geophysical Surveying Equipment, s. 98, PSTRR
- Pollution Control, s. 99, PSTRR
- Waste Management, s. 100 PSTRR

Tolko Industries Ltd. v. The King, 2024 BCSC 599

- Section 8 of the Interpretation Act (BC):
 - Every enactment must be construed as being remedial, and must be given such fair, large and liberal construction and interpretation as best ensures the attainment of its objects.
- How to claim PME Exemption?
 - Form FIN492

BC PST – Production Machinery and Equipment Exemption

Examples of Exclusions:

- Buildings
- Transportation equipment (some exceptions)
- Portable generators, with some specific exemptions
- Bases and foundation that become part of real property
- Scaffolding, walkways, catwalks (some exceptions),
- Office furniture



Manitoba – Expanded Definition of Tangible Personal Property

- In Manitoba, RST does not apply to real property
- TPP is expanded to include the following:
 - machinery, equipment, an apparatus or a storage structure — other than a warehouse, grain elevator or other storage building prescribed by regulation — that is installed on, under or in, or attached to, buildings or land and used in manufacturing, producing, processing, storing, handling, packaging, displaying, measuring, monitoring, transporting, transmitting or distributing tangible personal property, or in providing a service,
 - plumbing, heating, cooling, vacuum, electrical, electronic and telecommunication systems and components installed on, under or in, or attached to, buildings or land
- All mechanical and electrical equipment become TPP, including equipment used in production, processing, refining or transportation of oil and gas.
- Sale of Oil and Gas Wells – Taxable but not the intangible interest.
- From Bulletin No. 045 Oil Producers, Oil Well Drilling and Service Contractors – “machinery, equipment, apparatus and storage structures that may be installed on, under or in, or attached to buildings or land such as down hole tubing, underground tanks, pipes, pumps and related equipment”.

Manitoba – Expanded Definition of Tangible Persona Property (con't)

- Exemption – 3(22) of Retail Sales Tax Act
 - Manufacturing or processing plant is sold or leased;
 - Equipment at the plant is used to manufacture or process “tangible property”;
 - For 6 months after the sale or lease, plant is owned or leased by the purchaser or a closely related person of the purchaser and used in manufacturing or processing; and
 - The equipment must be PST-paid.
- What is “tangible property”?
 - “property having physical substance apparent to the senses.”
- Does 3(22) apply to natural gas processing plant?
- Exemption - 3(22.1) of Retail Sales Tax Act
 - Building – mechanical and electrical become exempt

Manitoba – RST Exemption – Oil and Gas Service Companies

Exemptions for Drilling and Servicing Companies:

- Drilling rigs or well servicing rigs designed and used solely (greater than 90%) for oil and gas exploration or development, or for servicing oil or gas wells
- Mobile equipment used for seismic exploration, formation testing, cementing, fracturing, acidizing, including trucks and trailers
- Oil and gas testing equipment
- Geophysical survey and exploration equipment used in oil and gas exploration

Saskatchewan – PST Exemption – Oil and Gas Producers

- PST does not apply to real property
- PST does apply to tangible personal property
- In practice, PST would apply to certain mobile tanks, mobile generators, and other TPP

Tip: No expanded definition of TPP

Trap: No Exemption



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Saskatchewan – PST Exemption – Oil and Gas Service Companies

- Certain oil and gas drilling and service rigs and related capital equipment are exempt from PST – s. 18.61 and Table 1 of Schedule of the Provincial Sales Tax Regulations.
- The specified equipment must be used substantially in the oil and gas industry or other qualifying activities and must be capitalized or recorded as a long-term lease receivable (capital lease) in the company's records.
- The equipment should be capitalized as well.
- Geophysical survey and exploration equipment
- Well servicing equipment, including the following (some example):
 - coiled tubing
 - Blowout preventer
 - Cement pump trucks
 - Acid Pumping unit, frac pumping unit, CO2 pumping unit, nitrogen pumping unit.

PST – Bulk Clearance Certificate

- Pre-closing PST liabilities of a vendor can transfer to a purchaser of assets.
- Exception – bulk clearance certificate

Tip: If it is not possible to obtain bulk clearance certificate as a buyer, obtain an indemnity if possible

Tip: If you are the seller, stay silent first. If the purchaser asks for a clearance certificate, add a best effort clause

Trap: It may not be easy to get a bulk clearance certificate easily

PST – Transaction Costs

- The parties may have to do self-assessment on the following costs related to the transaction:
 - Legal Fees
 - Accounting Fees
 - Other fees??

- After the PSA is closed and prior to the effective date, please do the following:
 - Get access to GST/HST, QST, PST account as needed

Trap: CRA Account could be difficult if directors are not readily available

Questions?

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