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RENTAL PROPERTIES

Whether you are collecting rent on a portion of your home or a separate property is important to know the tax consequences. Rental properties can be great investments, but they also come with lots of tax risk.

Change in Use (PLEASE, PLEASE, PLEASE READ):

WARNING: We see this a LOT and it can really trip people up. If you are concerned, please reach out.

- A change in use happens when you change all or part of your principal residence into a rental property, or vice versa. An example is when you move out of your condo and into your boyfriend/girlfriend's residence. If you start renting out your condo, it has changed from personal use to income producing.
- A change in use is important because it triggers a 'deemed disposition' for tax purposes. Essentially CRA 'deems' you to have sold your property to yourself, at its fair market value. THIS IS TAXABLE.
- The good news is there are lots of way to plan for this including elections and principal residence exemptions; BUT, timing is crucial. Many of these forms need to be filed in the same tax year that the change in use occurred. Speak with your accountant if this applies to you.

Renting a Portion of your Principal Residence:

There is a risk that capital gains tax could be applied on the income producing portion (i.e. rented portion) of your home when it is sold. The principal residence exemption (PRE) that allows you to sell your home tax free may not cover the rented component.

- CRA does allow 'reasonably small' portion of your home to be used for income production without impacting your PRE. Unfortunately, CRA does not define 'reasonably small'. Conservative estimates generally range from 5% – 15% while more aggressive claims are usually around 20% – 30%.
- The portion of your home used is calculated by either square footage or number of rooms. When calculating your rented portion exclude any personal or common use areas to reduce risk.

Short Term Rental Complexities:

In general, short term rental units are similarly to long term rental units, but with a few important considerations.

- GST (Goods and Services Tax) - if your total collected short term rental income exceeds $30,000 (before deductions) in a 12-month period then you are required to register, collect, and remit GST.
- GST may also apply on the purchase or sale of your property if it has been used for short term rentals. This is a complex area of tax and worth seeking professional advice.
- Depending on location you may also have to pay speculation tax, vacancy tax, or provincial sales (PST).

What you can deduct:

There are lots of deductions available for rental properties with a few extra considerations:

- Property taxes, home insurance, utilities (gas, electric, water / sewer), repair and maintenance, and accounting fees are all deductible. Adjustments may be made for personal / rental use portions.
- Mortgage interest (not the full payment) is deductible.
- Purchase fees (legal fees / property transfer taxes) and renovation costs that significantly improve your property are generally not deductible; BUT, keep all receipts as they may have tax benefits when you sell.

Some final notes:

- Prepare to pay more taxes. Profits from rental properties are quite common. We would recommend saving between 25 – 50% of your rental profits (depending on your income) in anticipation of extra taxes.
- Seek professional accounting advice. Rental properties are complex and hiring a CPA is <u>highly</u> recommended.

Please note the above information is general in nature and should not be taken as professional tax advice.