

Tax Implications of More Than One Residence

Your tax-free nest (in the form of your home) may be affected by ownership in other residences. If you do own more than one personal residence, the good news is that you can choose which one should be the exempt residence, provided you met the habitation rules - that is, you must have "ordinarily inhabited" each property to choose it as a tax exempt principal residence.

You would of course choose the home that appreciated the most in value as the tax exempt one. Trouble is, you may sell the properties at different times. Here's what you need to know and discuss with your tax advisor.

Residences owned prior to 1982

It has only been since 1972 that gains on the increase in the value of assets have been taxable. And, in the ten year period leading to December 31, 1981, each spouse in the family could own one tax exempt principal residence. In those days, it was not unusual for families to own two properties: one in the city and one at the lake or in the mountains, and then reap the rewards of a tax exempt gain on each property sold in the period.

Where more than one property is owned, and the family uses both at some time during the year, the calculation of the tax exempt capital gain is more difficult. For any gains accrued in the period including 1971 to 1981, the principal residence tax exemption will shelter both properties.

For ownership periods starting in 1982, when only one property per year can be designated as a principal residence for the family, accrued capital gains on one of the properties will be ultimately subject to tax when sold. It is important to have a valuation of the property as of December 31, 1981 to assist with your calculations on a form CRA has devised for those purposes, described below.

Other significant valuation dates for principal residences include the following:

- Pre 1972: no tax on accrued gains on any capital assets.
- 1972 to 1981: one principal residence allowed for each year for each spouse.
- 1982 to date: one principal residence allowed for each year to each family unit in which there was legal married status.
- 1993 to date: one principal residence designation allowed for each year to each conjugal relationship (married or common-law).
- 2001 to date: same-sex couples required to limit themselves to one principal residence designation per year per conjugal relationship.

When these households own more than one personal residence, they must choose one property as the tax exempt property and one as the taxable property.

Form T2091 Designation of a Property as a Principal Residence by an Individual (Other Than a Personal Trust) is used to calculate the exempt portion of a capital gain on a principal residence, in cases where there is a taxable portion. You will be asked to tell your tax advisor the number of years each property you own is to be designated as a principal residence, so that you can calculate the "exempt" portion. It is not necessary to designate the year of sale or transfer, as the computations will add a "grace year" to the formula.

Always get a valuation of all principal residences owned when any of them are sold or transferred so that you can make the right choices on your principal residence designation form. Also be aware that by not reporting the sale of a personal residence you are implicitly designating it as your principal residence for all years that you owned it.

Also, keep all receipts for any repairs to all homes; if any of them are taxable, you'll be able to reduce your tax bill by adding your additional expenditures to the original cost base.

Finally, the cost base of your personal residence may be affected by any Capital Gains Election made on February 22, 1994, the day on which the \$100,000 Capital Gains Deduction was eliminated.

Change in use of principal residence

When a taxpayer starts using a principal residence for income-producing purposes (rental, home office) there are a number of important consequences to consider:

- You must get the property appraised when there is a change of use, as the property is considered to be disposed of at its Fair Market Value (FMV) and then immediately reacquired at the same amount. The gain resulting, if any, would be nil if the home was used in each year before this as a principal residence. However, you may have an immediate tax consequence if you owned another residence that perhaps has appreciated in value more, thereby being your preferred choice for the principal residence exemption.
- If the property is converted back to be used as a principal residence only, there is another deemed disposition and reacquisition of the property to account for. Tax consequences could result.

The good news is that in these cases an election may be made to ignore the deemed dispositions for now and defer any capital gain/loss until the time of actual sale or transfer sometime in the future. In the case of a sale, at least you'll have the money to pay the taxes then. Check this out with your tax advisor and real estate appraiser before you change the use of your property.

Rental property becomes principal residence

It is also possible to make a special election which notifies CRA of your wish to defer taxes when a taxpayer converts a rental property to a principal residence. In that case, there is a deemed disposition at FMV, but the capital gain is deferred to be reported on the actual disposition of the property. This is only allowed, however, if no capital cost allowance was claimed on the property.

Use of principal residence for business purposes

If you use a part of your home for income-producing purposes (for example, child care in the home, boarders in the home or office-in-the-home), your tax exemption will not be affected if you set aside a specific area for the income-producing activity and again do not claim Capital Cost Allowance on the building.

Employer-required moves

There is an important exception to the "inhabitation" rules you should know about if you are a mobile employee. If your employer requires you to relocate to another city, you may not be able to sell your home, or perhaps may want to keep it (choosing to rent in the work location instead). In such a case you can also choose to designate your home as a tax exempt principal residence even though you have not technically inhabited it.

This is possible for up to four years after moving out of the house. You could even choose to rent out your home in the meantime, and then move back into it without losing your principal residence exemption; however you may not designate a different property as your principal residence during this time. You must move back into the home before the end of the calendar year in which your employment is terminated and, of course, you must report the rental income and expenses. Check with your tax advisor about the elections you must file in this case.



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