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TAX MATTERS

The Underused Housing Tax affects more people than expected

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My wife Carolyn and I visited some good friends recently. Our friend Karen shared that she's been suffering from insomnia. "The good news, Karen, is that you're married to Dan – who's an accountant. Next time you have trouble sleeping, just roll over and ask him to tell you about his day," I suggested. (I'm allowed to say that since I'm also a CPA.) I said that another good way to fall asleep is to read the rules about the Underused Housing Tax (UHT), which became effective Jan. 1, 2022.

The UHT was originally billed by the government as a tax on foreign investors in residential real estate in Canada, but it can apply to some Canadian citizens and permanent residents as well. It's a 1-per-cent tax levied on the value of residential property owned on Dec. 31 each year, and that is vacant or considered underused. But when you look closely at the rules, you'll see the requirement to file applies to more people and entities than you might expect.

Filing Returns

Who has to file? Everyone who owns residential real estate in Canada unless they're an "excluded owner." If you're not an excluded owner, and therefore must file a UHT return, you might still be exempt from paying the tax if you meet one of several exemptions.

The deadline for UHT returns – Form UHT-2900, Underused Housing Tax Return and Election Form – is April 30 each year for the prior year. This year, since April 30 is a Sunday, the taxman will accept 2022 returns filed by May 1, 2023. Sound pretty clear? Let's look at it closer.

Excluded Owners

Excluded owners generally include Canadian citizens and permanent residents, but partners of a partnership and trustees of a trust (other than Canadian executors of estates) are not considered to be excluded owners, so they may have to file.

Private corporations that hold residential real estate also are not excluded owners and are required to file a return. Individuals and entities who are not excluded owners – who the taxman refers to as "affected owners" – have to file but may not owe UHT taxes if they are "exempt owners."

Exempt Owners

So, you've figured out that you have to file Form UHT-2900. Sorry about that. The good news? You might not have to pay the tax if you meet one or more of the exemptions, which can fall into four categories: (1) the type of owner, (2) the availability of the property, (3) the occupant of the property or (4) the location and use of the property.

There's an exemption, for example, for properties that are a primary residence or meet "qualifying occupancy" criteria. And vacation properties located in an eligible area of Canada and used for at least 28 days a year by the owner, or their spouse or common-law partner, can also be exempt. Properties that are seasonably inaccessible or uninhabitable for part of a year may also escape the UHT tax.

A corporation can be exempt if foreign owners own or control less than 10 per cent of the shares or voting rights, and Canadian partnerships or trusts can be exempt if all the partners or beneficiaries, respectively, are excluded owners or corporations that are exempt.

I've simplified the list of exemptions here, so speak to a tax pro for more details.

Penalties Apply

You don't want to miss filing a UHT return if you're required to file. The minimum penalty is $5,000 for any individual and $10,000 for a corporation, for each property. Ouch. Also, additional penalties can apply depending on how late the return is filed, and there's no time limit for the taxman to assess a UHT liability, along with penalties and interest, if you fail to file.

Nuances Abound

The UHT is levied on the value of the property – but what value is used exactly? The general rule is that the taxable value (on your property tax assessment) should be used, although you can use the fair-market value instead if you file an election to do so. And the 1-per-cent tax is the total tax paid by all owners together on the property, so you may need to prorate the tax for your percentage of ownership to calculate how much you owe. But each owner must file their own UHT return for each property.

Here's the thing: There are other nuances, the rules are complex and it's reasonable to expect that in this first year of filing UHT returns, many taxpayers will not understand who is excluded or exempt. People are going to fail to file as a result. Let's hope the Canada Revenue Agency is lenient in this first year.

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