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Home Sweet Home – Tax Tips For Homeowners

by Jamie Golombek

With spring in the air, house-hunting season is in full bloom. Whether you're looking to buy your first home, you're already a homeowner or you sold your home in 2010, here are some tax tips to keep in mind.

1. TAX FILING TIPS (2010 RETURNS)

Home Buyers' Tax Credit (line 369)

If you purchased a new home in 2010, don't forget to claim the Home Buyers' Tax Credit. Introduced in 2009, this new non-refundable tax credit is worth $750 to "first-time home buyers," who acquired a home after January 27, 2009, the date of the 2009 budget.

For the purposes of this credit, you are considered a first-time home buyer if neither you, nor your spouse or partner, owned and lived in another home in the calendar year of purchase, or any of the four preceding calendar years.

The credit is also available for the purchase of a home either by, or on behalf of, an individual eligible for the disability tax credit if the home enables the disabled individual to live "in a more accessible dwelling or in an environment better suited to the personal needs and care of that person."

Any unused Home Buyers' Tax Credit can be claimed by your spouse or partner. Note, however, that even if each spouse or partner uses his or her own funds to jointly purchase a new home, the Home Buyers' Tax Credit is still limited to one credit of $750 (as opposed to $750 for each spouse or partner).

Home Buyers' Plan Repayments (Schedule 7)

The federal Home Buyers' Plan (HBP) currently allows a first-time home buyer to withdraw up to $25,000 from his or her RRSP to purchase, or construct, a new home without having to pay tax on that withdrawal.

Under the HBP, any funds withdrawn must be used to acquire a home before October 1st of the following year. Amounts withdrawn under the HBP must be repaid over a maximum of 15 years, or the amount not repaid in a year is added to the participant's income for that year.

If you participated in the HBP previously and were required to make a repayment for 2010, be sure to designate a portion of your RRSP contributions as a HBP repayment on Schedule 7 of your personal tax return, under "PART B – Repayments under the HBP…"

Provincial Property Tax Credits

If you're a resident of Quebec, Ontario or Manitoba, you may get some additional tax relief on your property taxes. Quebec provides a refund for property tax paid during the year (line 460 of the Quebec Provincial tax return), while both Ontario (Form ON 479) and Manitoba (Form MB 479) provide a tax credit for property tax or rent paid during the year.

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2. MAKE YOUR MORTGAGE INTEREST TAX DEDUCTIBLE

If you've got a mortgage and also have non-registered investments, you may wish to consider making your interest expense tax-deductible by paying off non-deductible debt (the mortgage) with your non-registered funds and then borrowing back for investment purposes.

This strategy has often be referred to as the "Singleton Shuffle" because it was named after Vancouver lawyer John Singleton's 2001 Supreme Court victory, which upheld the notion that you can rearrange your financial affairs in a tax-efficient manner so as to make your interest on investment loans tax-deductible.

This technique has been employed by many Canadians who own non-registered investments and are advised to liquidate these investments and use the proceeds to pay off their mortgage. The investor would then obtain a loan secured by the newly replenished equity in their home and use the loan for earning investment income, thus making the interest on the loan fully tax-deductible.

Before doing so, be sure to speak with an advisor to discuss any tax consequences of selling your non-registered investments, along with any prepayment fees for paying off your mortgage early.

3. CLAIMING THE PRINCIPAL RESIDENCE EXEMPTION

Finally, if you sold your home in 2010, the good news is that the gain is likely tax-free, provided you didn't also own a second home.

The principal residence exemption ("PRE"), if available, can shelter the gain on a principal residence from capital gains tax. A principal residence can include either your main home, or a vacation property, even if it's not where you primarily live during the year, as long as you "ordinarily inhabit" it at some point during the year.

A cottage is considered to be ordinarily inhabited by someone, even if that person lives in that property for only a short period of time during the year (for example, during the summer months), as long as the main reason for owning the property is not for the purpose of earning income. Even if you rent it out occasionally, the CRA has stated that incidental rental income won't prevent a cottage from still qualifying as a principal residence.

Prior to 1982, it was possible for each spouse to own a property and designate it as his or her principal residence, with the resulting capital gains tax-free upon disposition. The change in rules means that for years of ownership after 1981, a couple can only designate one property between them as their principal residence for any particular calendar year.

This becomes a challenge when a couple owns more than one principal residence and is forced to choose, upon ultimate sale of the first one, which property will be designated the principal residence for each year during the period of multi-home ownership.

Technically, the calculation of the PRE is done on Form T2091-(IND), "Designation of a Property as a Principal Residence by an Individual." The CRA, however, assumes that if the Form isn't filed, and no gain is reported on your return for the year of sale, the PRE has been used to eliminate the gain, and therefore, no other property (such as the vacation property) can be designated for the years in which the PRE was presumed to be claimed on the sold property.

As a result, if you sold a home in 2010, a conscious decision should be made as to whether the gain should be reported since failure to report will result in the assumption that the "sold property" has been designated as your principal residence for the years you owned it, precluding you from using the PRE in the future on the sale of your other property, at least during the overlapping years.

Generally, the decision to claim the PRE when you sell your vacation property, as opposed to "saving it" for the disposition of your other property, will depend upon a number of factors, including: the average annual gain on each property (that is the gain on each property divided by the number of years each was held), the potential for future increases (or decreases) in value of the unsold property, and the anticipated holding period of the unsold property.

Non-economic factors may also come into play if you are more concerned about an immediate tax liability versus a tax liability payable later (possibly upon death) on the sale of your other property.

For more information on planning for the sale of a second home, see our report "What's up dock: Tax & estate planning for your vacation property" which can be found at http://www.cibc.com/ca/features/tax-tips/tax-planning/income-tax-plan.html

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