ESTATE AND TRUST PLANNING

Understanding the New *Underused Housing Tax Act*

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Summary

Most family trusts and private corporations which own residential properties in Canada are now required to file an annual return under the new federal ***Underused Housing Tax Act***, SC 2022, c 5, s 10 (the "***Act***"). If you are a trustee of a trust or a director of a private corporation, it is important to be aware of, and comply with, this requirement and to understand your obligations under the *Act*.

Overview

The *Act* came into force on June 9, 2022, applying retroactively to applicable property as of January 1, 2022. The *Act* levies a 1% tax on the value of vacant or underused residential property owned, directly or indirectly, by certain non-resident individuals or entities. It also imposes a positive obligation on all owners of residential properties in Canada, other than "excluded owners," to file an annual return with the Canada Revenue Agency.

The annual return must be filed, and any owing tax must be paid, on or before April 30 of the following calendar year. Failing to file the required declaration can result in serious consequences, such as penalties and interest. The annual return must include relevant information about the residential property and the owner, including the address of the property, the legal name and contact information of the property owner, the type of owner, and the specified value of the property and how it was determined. The annual return must be filed even if there is no tax owing.

A "residential property" is defined to include: a detached house, duplex, or triplex containing no more than three dwelling units; a part of a building that is a semi-detached house, a rowhouse unit, or a residential condominium unit; or any other prescribed property.

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Excluded owners

Certain owners are excluded from paying the tax and excluded from the obligation to file the annual return. "Excluded owners" include:

- an individual Canadian citizen or a permanent resident of Canada;
- a publicly traded Canadian corporation;
- a mutual fund trust, a real-estate investment trust, or a SIFT trust;
- a registered charity;
- a cooperative housing corporation; and
- a municipal organization or other public institutions.

By contrast, personal trusts, private corporations, partnerships, and non-resident individuals which own residential property in Canada are not considered excluded owners under the *Act*. This means that these entities and individuals are required to file an annual return; they are also required to pay any applicable tax, unless an exemption applies.

Exemptions

Owners (other than excluded owners) are subject to the underused housing tax unless they qualify for an exemption. The *Act* provides a comprehensive list of owners who qualify for an exemption, including:

- a specified Canadian corporation, where foreign shareholders own less than 10% of the equity value or voting rights in the corporation;
- a specified Canadian trust, where all beneficiaries are excluded owners or specified Canadian corporations;
- a specified Canadian partnership, where all partners are excluded owners or specified Canadian corporations;
- an owner of a property that is the primary place of residence of the owner, their spouse, or child who is an international student;
- an owner that satisfies a qualifying occupancy test in respect of the property (which is, generally, occupancy in periods of at least one month for a total of six months in a calendar year by (i) any of the owner, their spouse, child, or parent who is a citizen or permanent resident of Canada, or (ii) certain renters);
- an owner of a property that is inhabitable or inaccessible for a portion of the year (such as a cottage that is not winterized);
- an owner of a property that is inhabitable due to a disaster or hazardous conditions;
- an owner of a property that is undergoing major renovations;

- an owner of a property that is in its first year of acquisition or is newly constructed; and
- a deceased owner and their estate trustees in the year of death and the following year (the exemption also extends to surviving owners of a property where the deceased's interest in the property was at least 25% percent).

Even if an owner qualifies for an exemption and does not need to pay the tax, the owner is still required to file the annual return.

Consequences for non-compliance

Failing to file the annual return exposes the owner to several significant consequences. For example, such an owner would be liable for a penalty equal to the greater of $5,000 if the owner is an individual ($10,000 if the owner is not an individual) and the amount that is the total of: (i) 5% of the applicable tax in respect of the owner's interest in the property; and (ii) 3% of the applicable tax in respect of the owner's interest for each calendar month the return is overdue.

Other penalties for failing to file a required return include the loss of potential exemptions or interest added on to the unpaid amounts, compounded daily. The Canada Revenue Agency may assess the applicable tax, interest, and penalties at any time after the calendar year for delinquent returns and tax payments.

Other vacant home taxes

Separately, the City of Toronto has enacted a new by-law that imposes a 1% tax on vacant residential homes in Toronto; all residential property owners are required to declare the occupancy status of their residential properties annually, starting in the 2022 calendar year. Other municipalities have implemented their own separate vacancy taxes as well; these are in addition to, and not a substitute for, the federal underused housing tax.

Conclusion

If you are a trustee of a trust or director of a corporation, you may wish to consult with your legal or tax advisors for guidance.