Underused housing tax – requirements and exemptions

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The federal government's new underused housing tax (UHT) may be aimed primarily at non-residents of Canada, but others may also be caught. Find out more about the UHT and when it applies.

In Budget 2021, the federal government announced plans for an annual one per cent tax on the value of residential real estate that is:

- owned by any non-resident, non-Canadian, and,
- considered vacant or underused.

The UHT Act was enacted on June 9, 2022, with effect from January 1, 2022. While the budget suggested that only non-residents would be affected, the scope of the final legislation is broader, as we explain later in this blog. For example, where a property is held in trust for Canadian resident beneficiaries, there may be a requirement to file a return (form UHT-2900, Underused Housing Tax Return and Election Form) even though no non-residents have an interest in the property and no tax is payable.

In this blog, we highlight the UHT's key elements and answer some top questions you might have about the new tax. See also the Canada Revenue Agency (CRA)'s new UHT webpage, which includes the new UHT return, technical guidance and other information, and which, as we understand, the CRA will update with new information going forward. We will update this tax blog when new information is provided, and we will alert you regarding these updates via our Canadian Tax News page.

Finally, this blog only covers the national UHT. Some provinces and municipalities impose similar vacancy taxes, and you should review these rules also if you or your client has affected properties in these locations.

WHAT IS THE UHT?

The UHT is intended to apply to underused housing in Canada owned directly or indirectly and wholly or partly by non-resident, non-Canadians. UHT obligations apply for calendar years (beginning with 2022) to affected owners of residential property[1] in Canada on December 31 of the relevant year.

The UHT rules have two requirements: an annual reporting requirement and, for some of these filers, a tax liability for UHT. The tax is calculated by multiplying the residential property's value by the 1 per cent tax rate. It must be paid to the CRA by April 30 of the following calendar year, when the annual return is also due.

The UHT rules categorize owners of residential property in three broad groups:

1. owners with no UHT reporting or tax obligation (referred to in the UHT legislation as "excluded owners")
2. owners required file the UHT return and pay tax (referred to by the CRA in their guidance as "affected owners")
3. owners required to file the UHT return but with no tax payable (also "affected owners")

Which owners are excluded?

Excluded owners who are exempt from any UHT obligations include (as of December 31 of a calendar year):

- individual Canadian citizens or permanent residents[2] of Canada ("Canadian individuals"), unless they would be exempt as an owner in their capacity as a trustee or partner (excluding personal representatives of a deceased individual)
- publicly traded Canadian corporations
- persons with title to property in their capacity as a trustee of a mutual fund trust, real estate investment trust or specified investment flow-through trust (SIFT)
- registered charities
- cooperative housing corporations
- municipal organizations and other public institutions and government bodies
- an Indigenous governing body or a corporation
- "prescribed persons" (not yet defined by regulation at the time of writing)

Which owners must file the UHT return and pay the tax?

Affected owners of residential property who must file a return and pay the tax include:

- individuals who are not Canadian citizens or permanent residents who do not qualify for an exemption
- private corporations, including Canadian controlled private corporations (CCPC), partnerships and trusts (other than estates) that own[3] residential property in Canada and are not eligible for an exemption

Which owners must file the UHT return but are exempt from the tax?

This subset of affected owners is generally eligible for one of the available exemptions, but they still need to file the annual return to claim the exemption for a calendar year.

WHAT ARE THE EXEMPTIONS?

Affected owners must first determine whether they qualify for one of the following exemptions from the tax. If they do not, the UHT will be payable.

Exemptions based on qualifying occupancy

An owner of a residential property may be exempt for a calendar year in the following situations.

- **Primary place of residence –** The residential property is the primary place of residence of:
  - the owner or their spouse or common-law partner (referred to as "spouse" in this blog), or
  - a child of the owner or owner's spouse who occupies the residential property for authorized study at an institution designated to host international students.
- **Qualifying** occupants – The residential property is occupied by one or more qualifying occupants in relation to the owner for at least 180 days of the year (counting only the days of the qualifying occupancy period in the year).

A **qualifying occupancy period** means a period of at least one month in the calendar year during which a qualifying occupant continuously occupies a dwelling unit that is part of the residential property.

A **qualifying occupant** in relation to the owner includes:

- an arm's length tenant, under a written agreement
- a non-arm's length tenant who is given continuous occupancy of the dwelling unit under a written agreement for a fair amount of rent[4]
- an individual owner or their spouse who is in Canada to pursue authorized work under a Canadian work permit and who occupies the dwelling unit for that purpose
- a spouse, parent or child of the owner who is a citizen or permanent resident

If the owner and their spouse jointly own multiple residential properties, their ownership may not qualify for the exemptions for either primary place of residence or qualifying occupancy unless they file an election with the CRA to designate only one property for the exemption. The election must be filed as part of the UHT return by the April 30 of the following year. Where the owners own the property jointly, they must also make the election jointly.

Where an owner or their spouse elect to designate one of the multiple properties as a primary residence, they cannot be qualifying occupants of any other properties they may own.

Exemptions based on a property's limited availability

An exemption may be allowed if the residential property's availability is limited for any of the following reasons.

- **Limited seasonal access –** The property is not a suitable residence year-round or not accessible during part of the year.
- **Disaster or hazardous condition –** The property is uninhabitable for at least 60 consecutive days in the calendar year due to as disaster or hazard caused by circumstances beyond the owner's reasonable control, and the property was not exempt in a previous year for the same reasons.
- **Renovation –** The property qualifies for the exemption for residential properties that are uninhabitable for at least 120 consecutive days in the calendar year due to a renovation done without unreasonable delay, and the property was not exempt in a previous year for the same reasons.
- **Under construction –** The property was not substantially completed (generally, 90 per cent or more) before April of the calendar year, or it was substantially completed in January, February or March, offered for sale to the public during the year, but never occupied by an individual.
- **Year of acquisition –** The owner first acquired the residential property during the year and did not own the same property during any of the nine preceding years.

Exemption based on type of owner

The following types of owners are exempt from UHT:

- ***deceased owners*** and their personal representatives (exempt in the year of owner's death of the owner or the following year)
- ***surviving joint owners*** with at least 25 per cent interest in the property (exempt in the year of the deceased owner's death)

- ***specified Canadian corporations***, which are generally Canadian corporations having less than 10 per cent of their votes or equity value owned by foreign individuals or corporations
- persons who own the property solely in their capacity as a ***partner of a specified Canadian partnership***, which is one that has, on December 31, only excluded owners or specified Canadian corporation as partners
- a person who owns residential property solely in their capacity as a ***trustee of a specified Canadian trust***, which is a trust that owns a residential property where each beneficiary with an interest in the property is, on December 31, an excluded owner or specified Canadian corporation.

Exemption based on prescribed area and condition or person

Recreational and other properties in less densely populated areas may be exempt from the UHT if the residential property is:

- located in a prescribed area of Canada, and
- used personally by the owner, the owner's spouse or both for at least 28 days during the calendar year.

You can find out whether a residential property is in a prescribed area of Canada using the CRA's Underused housing tax vacation property designation tool. The determination is based on periodically updated census data, so you should check whether an area qualifies as a prescribed area for UHT purposes each year.

Finally, "prescribed persons" are also exempt under the UHT legislation, but no regulatory definition of this term has been released to date.

HOW IS THE UHT CALCULATED?

The UHT formula is one per cent of the property's value multiplied by that person's ownership percentage. Where property is held jointly (i.e. no percentage is listed in the land registry), the ownership percentage is based on the number of owners.

There are two ways to determine the value of a residential property:

- **Taxable value,** which is the greater of:
  - the assessed tax value for the year under the related property tax assessment, and

    - the most recent sale price on or before December 31 of the calendar year, or
- **Fair market value,** which can be used if the owner files an election with the CRA to use that method for the property (the election will be included on form UHT-2900).

To elect to use fair market value, the CRA states that the owner must get an appraisal report for the property prepared by an accredited, arm's length real estate appraiser.

When are UHT returns and payments due?

Every affected owner must file an annual return with the CRA for each residential property they owned on December 31 of a calendar year. The return and any UHT payable are due by April 30 of the following calendar year, with the first annual filings and payments due by May 1, 2023 (since April 30 falls on Sunday) for applicable properties owned on December 31, 2022.

Affected owners who own two or more residential properties in Canada on December 31, must file separate UHT returns for each property. Where ownership is shared, each affected owner must file separate UHT returns for the property and either claim an exemption or pay the tax based on their share of value.

At the time of publishing, the CRA has not yet provided details on how to file the return. We understand that the filing can be done electronically, through My Account, My Business Account or Represent a Client, or directly on the CRA's website. The UHT return can also be filed by paper.

How is the UHT paid and what if it is paid late?

At the time of publishing, the CRA has yet to provide details on how UHT payments can be made.

Daily compound interest will accrue on unpaid amounts at the CRA's prescribed rate. A deadline extension for filing and payment to the CRA can be made in writing although the CRA has not explained in what circumstances an extension will actually be allowed as it appears the CRA has the power to allow extensions on a discretionary basis.

What happens if a required UHT return isn't filed?

Every person who does not file a UHT return as required is liable to a penalty equal to the greater of:

a. $5,000 for individuals, or $10,000 otherwise, and

b. the total of
    - five per cent of the UHT tax payable by the person in respect of the residential property for the calendar year, and
    - three per cent of the tax payable times the number of complete months after the due date that the balance is unpaid

Where a return is not filed by December 31 of the following calendar year:

- the penalty is determined as if the exemptions were not available, and
- the penalty in (b) above will be determined as if a tax amount was payable for the property.

Where no return is filed for a calendar year at all, that year will never become statute barred.

Finally, a recent change enacted as part of Bill C-32 allows the CRA to decline a request for a section 116 certificate of compliance where a non-resident vendor has not fully complied with its UHT tax and reporting obligations for all periods up to the date of sale.

IMPACT OF UHT RULES ON COMMON OWNERSHIP SCENARIOS AND PROPERTY USES

Private corporations owning residential property

Private corporations, including Canadian-controlled private corporations (CCPCs), are affected owners that are required to file the annual UHT return. Specified Canadian corporations are exempt from UHT tax. However, as the threshold for foreign ownership is quite low, any level of foreign ownership should be closely monitored.

Affected corporations should also keep in mind that the UHT return and liability are due on April 30. If this is out of line with the corporation's corporate tax filing deadlines, a separate process should be implemented to ensure the UHT requirements are met.

Trusts holding residential property

Trusts can be set up to hold residential property. For residential property held in trust, the trustee is generally the affected owner who is required to file the annual UHT return (trustees of mutual fund trust, real estate investment trust or SIFTs are excepted from this rule). Additionally, unless the trust is a specified Canadian trust (i.e., all the beneficiaries are excluded owners), the property may be subject to the UHT. The UHT legislation appears to assume that the trustees legally own the property, so they – and not the trust – are required to file the return and pay any taxes. While this is in line with the CRA's processes for filing UHT returns and remitting the taxes, it is out of step with how T3 tax returns are filed. We have suggested to the CRA that a more consistent approach would reduce confusion.

Non-resident owners who own Canadian residential rental property

Non-resident owners who receive rental income from residential property in Canada are affected owners who will have to file the UHT return and potentially pay UHT (depending on whether they qualify for an exemption).

Affected owners who have elected (under section 216 of the Income Tax Act) to file a Canadian tax return should keep the different filing deadlines in mind – that is, UHT returns and payments are due on April 30 of each year while section 216 tax returns may be due on June 30. We have suggested to the CRA that consolidating these filing requirements could reduce compliance costs.

THINGS TO WATCH FOR

Although the UHT legislation took effect from January 1, 2022, some details are still unclear. As currently written, the UHT is overly broad and certain resident Canadians may have UHT filing and payment obligation. Additional regulations may be introduced in the future to prescribe special treatment for certain persons, properties or areas.

We understand from the CRA that owners can start filing UHT returns and paying UHT for the 2022 calendar year as early as February 6, 2023. The CRA has yet to publish the annual return and election forms, however, and guidance on the CRA's website is limited.

WE'LL KEEP YOU POSTED

Be sure check back on this Tax blog for updates as we continue to monitor legislative and administrative developments and the CRA continues to enhance their UHT resources.

[1]In general, residential property is defined as property that includes a detached house (or similar building), or a semi-detached house, rowhouse unit, residential condominium unit (or other similar premises), along with any common areas, appurtenances, and the related land.

[2] Permanent resident" for UHT purposes has the same meaning as provided under the Immigration and Refugee Protection Act, rather than under income tax concepts of residency.

[3] A residential property's owner is the title holder under the relevant land registration system.

[4] Fair rent is currently defined as five per cent of the residential property's taxable value.

Disclaimer

The views and opinions expressed in this article are those of the author and do not necessarily reflect that of CPA Canada.

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