By FOREST LI

A RENTAL-PROPERTY OWNER? KNOW YOUR TAX

In my previous column, I talked about the tax benefits of purchasing a home as a principal residence. The benefits include first-time home buyer tax credit, property tax credit, GST/HST rebate for new homes, and tax savings from business-use-of-home expenses.

Now let us talk about the tax issues regarding buying a real-estate property to invest and make money. There are at least three tax issues to deal with: the annual income tax, the final capital gain or loss, and the regular GST/HST returns if the property is for commercial use.

If you run a rental business, that is, renting out a property to make money, the income derived from the rent is classified as investment income, which should be reported in your income tax return each year. Unless the business is carried out through a corporation, the rent income and expenses must be reported on your personal tax return using Form T776, or Statement of Real Estate Rental.

Income is the total amount of rents collected for a calendar year, while expenses are amounts spent to run the property, including property tax, insurance, heat, hydro, water/sewer, telephone and Internet, maintenance and repairs, accounting and legal fees, mortgage interest and bank charges, and so on. It is important to correctly claim the mortgage interest and the CCA (Capital Cost Allowance) on your income tax return.

Mortgage payments to the bank consist of two portions: principal and interest. You shall only claim the interest portion as an interest expense, not the whole payment. Total interest payments for a year can be found on the annual mortgage statement from your bank. The banks normally send the mortgage statements to you automatically every year.

CCA is designed by the government to systematically allocate the capital cost to the business life of the property; it can be claimed each year to reduce the net rental income for the year. The amount of the CCA is determined by the purchase price of the property and the total CCA claimed for the property in previous years.

If expenses outpace income, then you have a rental loss, which can be used to reduce your other incomes. You would then get more refund or pay less income tax.

ASSET SALE

If selling a property, you need to deal with capital gain or loss. If the sale price (less selling costs) exceeds the purchase price of the property, then you realize a capital gain, and half of which is taxable. You need to add the taxable amount of the capital gain to your other incomes. In case of a loss, you may use it to offset the current year's capital gain, or carry it back for three years or carry it forward indefinitely for future use to save your income tax.

If the property is for commercial use, you may need to register a GST/HST number, charge HST on the rent, and file GST/HST return regularly. In the GST/HST return, the HST payable is calculated based on HST collected and the HST paid. You may receive an HST refund if the HST collected is less than the HST paid for the reporting period.

Keep all records of income and expenses, in case the government may wish to see them. And keep purchase and sale documents up to six years after the sale transaction. ■

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