

# Thinking of selling your cottage? Pay close attention to the new rules on principal residence exemptions



**JAMIE GOLOMBEK** | October 7, 2016 1:50 PM ET  
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PostmediaA seasonal residence, such as a cottage, cabin, lake house or even ski chalet can be considered to be "ordinarily inhabited in the year" even if you only use it during vacation periods "provided that the main reason for owning the property is not to gain or produce income."

As part of the new measures introduced by Finance Minister Bill Morneau this week to, among other things, "improve tax fairness for Canadian homeowners," the government announced its intention to close "loopholes surrounding the capital gains tax exemption on the sale of a principal residence."

The principal residence exemption (PRE) provides Canadians with an exemption from tax on the capital gain realized when you sell the property that you have designated as your principal residence.

Under the Income Tax Act, in order for a property to qualify as your principal residence for a particular tax year, four criteria must be satisfied: The property must be a housing unit; you must own the property (either alone or jointly with someone else); you or your spouse or kids must "ordinarily inhabit" the property; and you must "designate" the property as a principal residence. Note that a seasonal residence, such as a cottage, cabin, lake house or even ski chalet can be considered to be "ordinarily inhabited in the year" even if you only use it during vacation periods "provided that the main reason for owning the property is not to gain or produce income."

Since 1982, you can only have one principal residence per family unit in a particular year. So if you own more than one residence that qualifies as "ordinarily inhabited," you will need to do some analysis to determine which property should be designated for each tax year in which you own both properties. Fortunately, you need only make the decision when you sell the first one. Factors to be considered before coming to a decision would include the accrued gain to date (if any) on each property along with the anticipated holding period and future anticipated appreciation of each property.

In the past, it was the Canada Revenue Agency's published administrative policy that when you disposed of your principal residence, you didn't have to report the sale on your tax return if you were eligible for the full PRE.

But starting this year, applicable for the sale of a principal residence in 2016 or later tax years, the CRA has announced that it will only allow the PRE if you report the sale and designation of principal residence on Schedule 3, Capital Gains of your return. On this schedule, which is currently being modified, you will be required to report basic information such as the date of acquisition of the residence and a description of the property, along with the proceeds of disposition.

If you forget to claim the PRE in the year you sell your residence, you will be required to amend your return for that year in order to be eligible for the PRE; however, be forewarned as a late designation penalty of \$100 per month, up to a maximum of \$8,000, may apply to a late filing.

Finally, a new proposed measure will provide the CRA with the authority to reassess taxpayers beyond the normal three-year reassessment limitation period in cases where the disposition or real estate is not reported in your return for the year in which the disposition occurs.

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