



## **2016 Pre-Budget Consultation**

### **The Canadian Real Estate Association's Priorities for the 2016 Federal Budget**

Dear Minister:

The Canadian Real Estate Association (CREA) represents over 110,000 REALTORS® across the country and is proud to participate again in this year's Pre-Budget Consultation. We welcome the opportunity to share our ideas directly with you, as the federal budget of 2016 presents an opportunity to make targeted investments that support sustainable growth and a strong middle class.

Canada's housing market is a key component of Canada's overall economic stability and an important generator of jobs and economic security for the middle class. In 2015, each home sale generated an estimated \$51,510 in spin-off spending. This translated to one job for every three transactions. MLS® home sales and purchases in 2015 added an estimated \$26.1 billion in spin-off consumer spending to the economy and created 187,164 jobs. In 2016, spin-off consumer spending and employment creation is estimated at over \$26 billion and over 184,000 jobs.

To ensure the continued stability of the Canadian housing market and its contribution to job creation and a strong economy, CREA believes Budget 2016 should implement the following four recommendations:

1. Modernize and extend the eligibility of the Home Buyers' Plan (HBP) for Canadians who have recently relocated to secure employment, decided to accommodate an elderly family member, lost a spouse, or become divorced.
2. Index the withdrawal limit of the Home Buyers' Plan (HBP) in \$2,500 increments to the Consumer Price Index (CPI), a limit that has not increased with inflation since 2009.
3. Modernize the definition of an active specified investment business to recognize that Canadian-controlled private corporations that own and manage five or more residential rental units, or more than 15,000 square feet of gross rental commercial space, are active businesses.
4. Allow sellers of investment real estate to defer the recapture of previously claimed depreciation (Capital Cost Allowance [CCA]) on investment property when the proceeds are reinvested in another investment property.



## ***Recommendation #1 – Help Homeowners Through Life Changes***

Vulnerable populations and individuals in life changing situations may not be able to continue to own a home without assistance. CREA believes the HBP should be available to help Canadians maintain homeownership after significant life changes, such as job relocation, a decision to accommodate an elderly family member, the death of a spouse, or marital breakdown.

Jobs are the foundation of a strong economy. Relocating for work is a reality for many Canadian workers. At a time when the government is looking to fuel job growth, the price of housing need not serve as a barrier to job relocation. The HBP can encourage labour mobility by easing affordability concerns.

The proportion of seniors in the Canadian population is rapidly growing, with the 2011 census reporting a record 4.9 million seniors in Canada. This record proportion is projected to increase by a further 10% over the next two decades. Innovative policy solutions are necessary to deal with the emerging issue of accommodating these individuals' specialized needs. Affordability concerns need to be addressed. Extending the HBP would help ensure Canadian families have viable options for accommodating an elderly family member in their home.

In 2013, 50,900 Canadians became widowed and 38,800 divorced. These individuals may require support to keep housing within reach through this disruptive and often difficult period of change. Helping lessen affordability concerns is already a principle of the program. Individuals requiring new housing as a result of becoming disabled can use the HBP, as can those who have been out of the housing market for more than five years. The current structure of the rules and reporting requirements in the Income Tax Act can readily and effectively facilitate an extension of the HBP to accommodate the significant life changes described above.

Extending the HBP is a compassionate and fiscally responsible way to help modern Canadian families finance the purchase of a new home. The HBP effectively amounts to a zero-interest self-loan because it allows Canadians to borrow from their own savings. The only costs to the government are attributable to a loss in tax revenue from Canadians contributing more to their Registered Retirement Savings Plans (RRSPs) in the year of a home purchase in order to take advantage of the HBP.



## ***Recommendation #2 – Make Homeownership Affordable***

The HBP allows first-time homebuyers to borrow up to \$25,000 from their RRSP to use as a down payment towards a home purchase. Unfortunately, this key support for first-time homebuyers is losing its purchasing power to inflation. CREA recommends the HBP withdrawal limit be indexed to the Consumer Price Index (CPI) and adjusted at \$2,500 increments to prevent inflation from eroding its value.

To date, more than 2.8 million Canadians have used the HBP to help make homeownership more affordable. In spite of the HBP's importance, it has lost over \$5,200 in purchasing power relative to its value in 1992 and over \$2,400 since it was last adjusted in 2009. If left unadjusted, a homebuyer in 2020 will receive \$8,000 less value from the HBP since its inception in 1992.

Maintaining the value of the HBP is critical, since it gives first-time homebuyers an opportunity to make larger down payments, which can reduce or avoid mortgage default insurance fees and help build home equity sooner. Interest charges can also be reduced by the HBP by allowing first-time homebuyers to borrow from themselves and rely less on financial institutions. In addition, the HBP makes it easier for Canadians to build home equity and save for retirement at the same time, thus incentivizing greater financial preparedness.

Home purchases involving the HBP in turn generate spin-off spending and create jobs. In 2015, home purchases involving the use of the HBP resulted in over \$2.8 billion in spin-off spending and more than 20,700 jobs. In 2016, spin-off spending and employment creation is estimated at over 2.9 billion and 20,400 jobs.

Polling conducted by Nanos Research shows a majority of Canadians view the HBP as a valuable tool for Canadians interested in buying a home and believe it makes sense to index the HBP. Nanos Research found 76% of Canadians support or somewhat support adjusting the maximum withdrawal amount of the HBP to keep pace with rising consumer prices.

Finally, indexing the HBP is an affordable way for government to support first-time homebuyers and help middle class Canadian families finance the purchase of a home. Using Budget 2009 as a starting point, the plan would adjust by \$2,500 in 2016 at an estimated cost of \$7.5 million. Based on current trends, we estimate a further \$2,500 adjustment would not occur until 2020 at an estimated cost of \$7.5 million.



### ***Recommendation #3 – Support Business Models and Modernize the Test for Active Business***

Current specified investment business rules stipulate that ‘active businesses’ must have more than five employees. This arbitrary benchmark was set in the 1980s and does not reflect the modern reality that many active businesses operate with fewer than five employees. CREA believes the test for an active specified investment business needs to change to reflect technological advancements and the reality that active businesses in the 21<sup>st</sup> century do not necessarily have more than five employees. With new technologies disrupting old economic models, we need modern rules that help to foster a more cutting-edge business environment that will boost Canada’s innovation capacity.

Specifically, CREA recommends that the test for Canadian-Controlled Private Corporations that run income property businesses should be set at the management of five or more residential rental units, or more than 15,000 square feet of gross rental commercial space. Passing this threshold would grant these businesses active business status and make them eligible for the small business tax deduction (SBD). This recommended threshold for qualification recognizes that many active businesses have fewer than five employees; nevertheless it also ensures that only owners who maintain a significant level of activity to run their income property business would qualify for the deduction.

Small businesses play a critical role in a healthy economy and are instrumental to job creation in the vast array of services that are ancillary to the industry and to investing in local communities. Eligibility for the SBD for businesses in the Real Estate, Rental and Leasing industry is important, just as it is for all small businesses in providing lower marginal effective tax rates on income from their activities which would provide a stimulus to enable sustained investment.

Eligibility would increase the cash flow of affected businesses, thereby increasing the availability of equity financing for new investments. For each dollar of increased equity financing enabled by the use of the SBD, the real estate small business corporation would typically reinvest in retrofit and more capital investment, because debt financing would be more readily available to supplement the increase in equity. This proposed change would support modern Canadian businesses and create good-paying middle class jobs.



### ***Recommendation #4 – Encourage Community Reinvestment***

To promote reinvestment and revitalization of Canadian communities, CREA proposes investors be allowed to defer taxes on the recapture of previously accumulated depreciation (Capital Cost Allowance [CCA]) when they sell one investment property to reinvest in another of equal or greater cost.

Currently, income taxes act as a significant deterrent to many investors to sell income properties. This is because depreciation that was deducted from income is taxed when the property is sold, which often leaves insufficient after-tax proceeds to reinvest in another property even of similar cost.

CREA believes a deferral of previously claimed depreciation (Capital Cost Allowance [CCA]) should be allowed on an investment property when a seller reinvests the proceeds of sale into another property. The current system acts as a deterrent and many hold on to the properties instead of reinvesting. CREA's proposal would promote reinvestment and revitalization of neighbourhoods, which would strengthen Canadian communities and ultimately Canada's economic success.

Investment in property triggers renovations, retrofits and redevelopment, which benefits the economy. Furthermore, since this proposal would trigger federal revenue that otherwise would not be collected (Capital Gains Tax from property sales, GST/HST and income tax from spin-off activity), the net cost of this recommendation in the first year is estimated to be \$12 million. By year two, it would be net revenue positive, earning the government \$7 million because the deferred recapture serves to reduce the depreciable base of the replacement property yielding lesser depreciation deductions in the future, thereby resulting in higher taxable income from the replacement property. All deferred CCA is ultimately collected when investors decide not to reinvest, or later through their estates.

Allowing deferral of CCA levels the playing field for small investors as developers already benefit from other tax measures that effectively provide for deferral on reinvestment. Over 50% of the individuals that would benefit from this measure have annual incomes below \$50,000. An additional 14% of beneficiaries' incomes are under \$75,000 and as a result the measure would be instrumental in levelling out their average income over time, as opposed to the current situation that pushes an individual's income into a higher marginal tax bracket as a result of recapture in the year of sale.

This proposal also benefits tenants by encouraging redevelopment and renovation of buildings, which provides spin-off benefits, including investments in infrastructure and an improved quality of life, for communities where these improvements take place.