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Principal Residence Exemption

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Basics

Your principal residence is the place where you live, own or jointly own, and legally declare as your principal residence.
The Principal Residence Exemption (PRE) allows for a full or partial capital gains tax exemption based on the term you have owned and lived in the residence.
Spouses or a household may only declare one principal residence between them.

Capital Gains Tax Exemptions

- The capital gain on the sale of your principal residence is completely exempt if that residence has retained the status as your principal residence, for the entire time you owned it.
- If your residence was not your principal residence for the entire time you owned it, you must report the capital gain pertaining to the years it was not a principal residence. The exempt amount of capital gains is calculated in the following way:

$$\text{PRE} = \frac{(\text{\# of years home is principal residence}) \times \text{capital gain}}{\text{\# of years home is owned}}$$

Multiple Principal Residences

Before 1982, spouses could each declare a separate principal residence (ex. House and cottage). So for those who owned multiple properties before 1982, and individually designated separate principal residences; both these may qualify for the Principal Residence Exemption for the years before 1982.

Other properties held that are not the principal residence are considered to be Personal Use Property if they are used for the enjoyment of the taxpayer, their family, or the taxpayer being a trust or beneficiary of a trust. Capital gains on these properties are taxable; however, the PRE can be deducted from your capital gain if your property was at any point declared a principal residence.

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Changing Uses of a Principal Residence

In some cases, people use their principal residence to generate income, either for a home business, or rental purposes. In these cases, the square footage of these activities must be reported, and will be exempt from the PRE; causing that area to be taxed if a capital gain occurs at the point of sale.

If all or part of a principal residence changes use to generate income, the owner must declare a Deemed Disposition, which requires them to report the Fair Market Value of the property to the CRA. If the FMV is greater than the expense of acquiring the property, then a capital gain has occurred and is taxable.

There are a large variety of exceptions and specifications concerning the PRE. Speak with Steele Wealth Management if you want to know more.

Sources

Canada Revenue Agency (Online)
http://www.cra-arc.gc.ca/tx/ndvdls/tpcs/ncm-tx/rtrn/cmpltng/rprtng-ncm/lns101-170/127/rsdnc/menu-eng.html

*All conditions and figures apply to 2013 PRE regulations.

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