



## Turn Your Cottage into Your Home

Turning your cottage into a retirement haven may seem like a good plan, but there are important issues to consider before you decide to go ahead and make it your permanent home.

“This decision affects your finances and your lifestyle, so plan ahead and get advice,” advises Chartered Accountant Karen Yull, Tax Principal with Grant Thornton LLP in Toronto.

“Selling your home and moving to your cottage is not a straightforward decision, as it involves complex tax issues and planning,” says Chartered Accountant Martin Kretzschmann, Partner with Brabant & Kretzschmann in Midland, Ontario.

What are these issues?

“Many people don’t realize that they may have to pay capital gains tax on one of their properties when they sell it,” explains Karen Yull.

“The tax legislation was changed in 1981 to allow only one property to be designated a principal residence each year, per family unit. Now, when you sell the property and it is not designated as your principal residence for all years after 1981, there is a complex calculation to determine the capital gains tax you may have to pay.”

So what can you do?

“A common strategy is to determine which property has risen most in value since 1981. Given the jump in cottage prices, it may be advantageous to designate your cottage as your principal residence for some or all of those years, so have a valuation done by a real estate appraiser,” says Martin Kretzschmann.

“If you took advantage of the special one-time capital-gains-tax election in 1994, which allowed property owners to increase the cost of the property for tax purposes, then this must also be considered in determining which property to designate as your principal residence.

“However, it is difficult to generalize, and this calculation can be very complex,” continues Yull.

---

“If you conducted major renovations to convert your cottage into your home, you may be eligible to receive back a portion of the GST paid on the renovation costs, under the GST New Housing Rebate,” Kretzschmann advises.

Estate-planning issues are another consideration. Even though you decide to make your cottage your permanent home, you may still want to leave it to your children as a recreational cottage.

According to Yull it can be tricky to deal equitably with all of your children based on unknown future values.

“Some children may live nearby, some may not want the cottage. If you leave it to one child, how do you make sure your other children are provided for equally?”

“One strategy to keep the cottage as a family asset is to set up a trust. If you or your spouse are over 65, putting the cottage in an alter-ego or joint spousal trust helps avoid probate fees that, in Ontario, are among the highest in the country.”

Is there anything else you should think about?

“Yes,” says Kretzschmann, “snow.”

“Consider the costs of winterizing your summer home, updating your utilities and heating systems. Find out if the road is accessible in winter. Deal with a reliable contractor who knows the local building codes and conditions. Renovations may fall under newer building codes than those in place when the cottage was originally built, resulting in unanticipated costs, such as moving a septic bed or well.”

Both Yull and Kretzschmann offer one final piece of advice. Spending time at the cottage in the winter is very different from spending time there in the summer, and living there year-round will mean a change in lifestyle. Where is the nearest hospital? How close are your neighbours? What will you do for entertainment?

Before you make the decision to turn your cottage into your home, consider all the issues and, most importantly, seek professional financial advice.

For further information, contact a Chartered Accountant.

*Brought to you by The Institute of Chartered Accountants of Ontario.*