

SUBJECT: Issues Impacting Rental Accommodation Construction

SUBMITTED BY: Investment and Growth Committee

BACKGROUND/ISSUE

The level of rental housing construction in Saskatchewan has been low for many decades, resulting in a shortage of rental housing that is getting worse as more people move to the province as a result of Saskatchewan's growing economy.

Through unattractive taxation, the federal government is discouraging the construction of new rental properties in Saskatchewan and indirectly causing higher rents due to a lack of supply. Many individuals throughout the province have looked at building rental properties, but have decided not to as soon as they find out about the federal tax policies that are applied to the construction of rental accommodations.

The first problem is that Revenue Canada classifies rental income as "inactive" income for a business that has less than five employees. This inactive income is taxed at 46.7%, which is quite high when compared to the federal small business tax rate of 10.5% and corporate tax rate of 15%.

Second, if the owner of the building borrows money to construct the building, the cost to borrow this money doubles because of federal and provincial taxes. Consider an owner who must borrow \$100,000 per rental unit for construction costs: this owner must first pay back the \$100,000 principal amount to the bank. They will then also pay the bank \$62,000 in interest (7% over 15 years) and also pay the federal government 46.7% tax on any income generated from the property (assuming the owner employs less than five people to service the building), plus 12% in provincial corporate tax.

This high cost to the owner is important because of its impact on the high rental rate per unit that must be charged just to cover the cost of borrowing the money to build the unit.

Rental units in Saskatchewan cost between \$60,000 and \$150,000 per apartment to build. This means that the owner needs to charge between \$750 and \$2,070 per month just to cover the cost of capital to build the rental units. This does not include the cost of running the units – janitorial, repair and maintenance, insurance, vacant months, property taxes, regulatory compliance – which must all be paid before there is any return on the investment.

Those who blame the owners, as opposed to the government, for the low number of rental units being built will argue that owners can depreciate buildings. This is true, but they will still pay the 46.7% tax on any funds they recapture by depreciating the building. Plus, if they sell the building and have a capital gain, they pay the capital gains tax on any profit they make.

In addition, municipal governments levy higher property taxes on rental units than on other residential properties. In Saskatchewan the property tax rate on rental properties is 10% to 15% higher than on other residential properties. The result of this discrimination in property taxes is higher costs, resulting in even higher rents and the decision by many investors not to build rental units, but to instead invest in other types of property.

Finally, *The Residential Tenancies Act* in Saskatchewan is biased in favour of the tenant. Landlords have few rights to protect themselves against those tenants who do not pay their rents, are disruptive to other tenants, or damage the rental property. This bias in the Act is made worse by the Office of Residential Tenancies often acting as an advocate for the tenant and not acknowledging the reality that tenants are not always innocent and that owners are not always behaving badly.

RECOMMENDED

- 1) That the Government of Canada eliminate the inactive tax rate on rental accommodations and instead use the rates and rules that are applicable to regular small, medium, and large businesses. A federal tax rebate program on new rental unit construction could also be considered.
- 2) That Saskatchewan's municipal governments end the discrimination against rental properties and levy the same property tax on them as they do upon other residential property.
- 3) That *The Residential Tenancies Act* be amended to better protect the rights of both the tenant and the owner. Also, the Office of Residential Tenancies should be made responsible for regulatory enforcement that will be unbiased toward either the renter or the landlord. The public already perceives the Office as representing the renter, so the Office's current quasi-judicial role can easily be expanded to enforce the rights of the owner as well as the tenant.
- 4) That the Government of Canada allow owners of rental properties to roll over capital gains if the capital gain is immediately reinvested into new rental accommodation construction.
- 5) That the Government of Saskatchewan continue to reject the implementation of rent control in the province because such programs make it even less financially attractive for people to invest into building or renovating rental housing.