Investing in Real Estate

The right structure to achieve your real estate investment goals

Investing in real estate can be a sound business move, especially for those looking to diversify their holdings or optimize cash flow. With property prices steadily on the rise in Canada, coupled with low interest rates, many Canadians are setting their sights on real estate to help expand their investment portfolios and achieve competitive returns.

Before even looking at properties, however, you may want to think about how to structure the investment. Personal purchase or corporate? Partnership or joint venture? You can structure the ownership of your real estate investment many different ways, each with its own benefits and risks, rules and regulations. You should start by understanding your options.

Personal

Holding real estate personally can potentially lower your taxes (depending on your marginal tax bracket) and gives you access to the real estate income without any need to distribute it from another entity.

In general, it also comes with the simplest tax reporting obligations. However, personal ownership of real estate does not provide the liability protection of a corporation.

Also, depending on your marginal income tax rate, you might pay a higher rate of tax than if the income is earned elsewhere.

Corporate

Owning real estate in a Canadian corporation gives you the ability to access other corporate funds on a tax deferred basis for investment use, the potential to access low corporate tax rates in certain situations and the ability to strategize more tax efficiently. Also, the corporation structure limits personal liability.

Non-residents investing in Canadian real estate can use Canadian corporations to ensure the real estate rental income (and potential capital gain on sale of real estate) is not subject to withholding requirements, which can improve your bottom line.

Lastly, corporations can, in certain situations, create a loss with the claiming of capital cost allowance, whereas an individual cannot.

Trust

Owning real estate in a trust, carries the benefit of splitting the associated rental income and capital gain amongst the various beneficiaries.

In situations where there are a number of beneficiaries in low marginal tax brackets, the result can be highly rewarding.

On the other hand, any losses the trust realizes remain trapped in the trust, without direct access to it by the beneficiaries.

Joint venture

Joint ventures work best in situations where multiple participants own the real estate. Each participant benefits because they can actually mortgage their separate interest (subject to the joint venture agreement) if desired.

As well, each participant records their share of the joint venture's income or loss on their books and can take tax depreciation at their discretion on their respective interest.

The CRA has been performing a number of HST audits on joint ventures recently, however, so you need to ensure your joint venture is properly structured both for legal and HST purposes.

Partnership

A partnership typically takes the form of a limited partnership or a general partnership.

General partnerships do not require registration and each partner is jointly and severally liable for the partnership's obligations.

Limited partnerships should be registered and provide limited liability to the passive (or limited) partners. If a passive partner takes a more active role in the partnership, the person will lose the limited liability protection. A limited partnership has, in addition to the limited partners, a general partner who effectively manages the partnership.

Partnerships that are 100 percent Canadian owned have access to favourable tax benefits, so only Canadian partners should commonly form a partnership. If a non-resident wishes to invest in a Canadian partnership, he or she may want to hold their interest through a Canadian corporation in order to keep the Canadian partnership tax status.

Carefully review your ownership structure options

Depending on the type of real estate you are considering, your status as a buyer (individual, corporation, one of several investors) and your current tax position, you need to carefully review the different types of structures to determine which one is best suited to you and your project.

Once you have selected the right structure, you are well positioned to make the myriad of other decisions that come with purchasing a property and achieving your real estate investment goals.

This article is on a high level and very general basis, and care should be taken when relying on the above.

To learn more about how Zeifmans can help you structure your next real estate deal, contact one of our real estate services professionals or your Zeifmans advisor:

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