

Builders call Ottawa's tax break 'major needle mover' on construction of rental units

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A townhome development project under construction in Toronto, Sept 13, 2023.

FRED LUM/THE GLOBE AND MAIL

Real estate companies say Ottawa's new GST break on construction will spur them to develop thousands of new rental units by offsetting rising financing and building costs.

Fitzrovia Real Estate, an apartment developer and property manager, said the new five-per-cent tax discount would allow it to build 3,000 more rental units within the

next 10 months. "It's a very significant bold step in moving new supply forward," chief executive officer Adrian Rocca said.

Tricon Residential Inc., which also builds and manages rental apartments, said it would be able to go ahead with more than 1,000 units within the next six months. "We've certainly had to take a pause on some projects because of high construction costs and interest rates. And this is going to help close the gap," said Andrew Joyner, managing director of Tricon's Toronto investments.

Prime Minister Justin Trudeau announced the tax relief last Thursday in a bid to kick-start construction on rental units amid a surge in housing costs and increased demand from residents and newcomers. Ontario, the country's most populated province, has already vowed to cut the provincial sales tax from new rental construction, which further reduces costs for builders.

Residential building expenses have climbed 55 per cent over the course of the pandemic and into this year because of a shortage of materials and competition for construction workers. As well, the cost of financing has spiked as the Bank of Canada raised its interest rate to five per cent from 0.25 per cent to slow inflation.

The higher costs have made it unprofitable for real estate companies to develop rental units, also known as purpose-built rentals. Many developers either put their purpose-built rentals on hold or turned them into condos, where profits are realized as soon as the unit is sold.

The tax break is a huge win for the building industry, which had been lobbying for the GST elimination among other measures to reduce development costs.

"There were projects on the books that got shelved and our members are saying this can provide the solution to get those projects going again," said Kevin Lee, CEO of the Canadian Home Builders' Association, the national construction industry group.

The elimination of the five-per-cent federal goods and services tax became effective on Thursday. Called the Enhanced GST Rental Rebate, the new policy applies to rental construction that begins by 2030 and is completed by the end of 2035.

Developers will no longer have to pay the five-per-cent GST on the assessed value of a completed rental unit, according to federal government's Finance Department's website. For example, if the assessed value of the apartment unit is \$1-million, the developer will not have to pay the five-per-cent GST of \$50,000.

The move helps purpose-built rental developers cut upfront costs, which take a longer time to recoup than with condos. Condo developers recover their expenses and earn a profit immediately after they sell their condo units, whereas purpose-built rental developers only recover their expenses and earn a profit after their units have been rented over a longer period of time.

Non-profit housing groups have also been calling for the elimination of the GST on new construction. Habitat For Humanity Canada, which builds new homes and helps families buy them, said the tax break will significantly increase the supply of rental units. It would also like Ottawa to expand the rebate to new home construction.

“We know that reducing these costs will help non-profits create more housing with the resources we have,” said Julia Deans, CEO of Habitat for Humanity Canada.

The typical price of a home across the country has topped \$700,000 and the average monthly rent for a one-bedroom is more than \$2,000. But even though condos have become the dominant type of rental housing in the country, tenants can be kicked out of their unit if the owner wants to sell their condo or move back into the unit.

Purpose-built rental buildings typically give tenants a more permanent place to live than a condo or house owned by an individual. They were a bigger part of the housing market in the 1970s. However, rental construction dropped in the 1990s and fell to a low of six per cent of the country's total housing starts in 1997. But the pace has been increasing as the government has pushed for more rental housing. Last year, purpose-built rental starts made up 34 per cent of the country's new home construction, according to data from the federal housing agency Canada Mortgage and Housing Corp.

“The GST rebate will help. We really need more purpose-built rental housing,” said CMHC's deputy chief economist Aled ab Iorwerth. CMHC estimates that the country needs an additional 5.2 million homes to be built by 2030 in order to cut housing

costs and ensure that residents are not paying more than 40 per cent of their disposable income on shelter.

Tricon and Fitzrovia said the tax break would allow their respective companies to build more.

“Every year, we’re looking to add sites and build more rental housing. And now this is going to help us be able to actually do that,” said Mr. Joyner. “Instead of looking at 100 sites and being able to build one project a year, we’re all looking at 100 sites and hopefully be able to build many more than that,” he said.

Like Tricon, Fitzrovia is also looking for new sites. Mr. Rocca estimates that his company will add an additional 2,500 units to its pipeline. As well, Fitzrovia is expanding outside of Toronto into smaller Ontario cities such as London, Guelph, Hamilton and Kitchener-Waterloo. “This is a major needle mover for us,” he said.

The federal government has estimated that the GST elimination will cost the treasury \$4.6-billion in its first six years. Ottawa did not disclose how it will recover the lost revenue.

Quebec and Nova Scotia have said they were reviewing the federal decision. British Columbia does not charge provincial sales tax on the sale of purpose-built rental buildings and Alberta does not have a provincial sales tax.

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