FARM
ALERT

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Qualified Farm Property

B. Jason Heinmiller, CPA, CGA, *is a principal in the Yorkton office of Collins Barrow PQ LLP*

In a hot real estate market, farmland owners may start thinking about turning their dirt into cash.
Most people have heard there's no tax on the sale of farmland in Canada, but it's more complicated than that.

The Income Tax Act allows a capital gains deduction for individuals who are resident in Canada throughout the year and dispose of qualified farm property. This deduction may be claimed on their tax return to off-set profit on the land sale.

There are two things to note about the deduction: first, only individuals get a deduction, not corporations. Secondly, those individuals must be resident in Canada - they cannot be a resident of another country.

Clients will often ask if their farmland is qualified farm property, eligible for the capital gains deduction. Sometimes they think it is and it turns out it isn't. On other occasions, they think it isn't and it turns out it is.

Land Acquired after June 17, 1987

If a seller acquired land after June 17, 1987, it must have been owned by that individual, their spouse, child/grandchild or parent/grandparent, for at least two years to be considered qualified farm property. The Income Tax Act extends the definition of child/grandchild and parent/grandparent to include a spouse's child/grandchild or parent/grandparent.

In addition, the property had to be used principally in a farming business, and for any two years, the gross revenue from the agricultural business of the farmer needed to be more than all other income for the year. This is known as the gross revenue test. The individual who is selling the land does not need to be the farmer. It can be their spouse, child/grandchild, parent/grandparent, or their spouse's child/grandchild or parent/grandparent.

Alternately, if the property was used by a farming corporation or by a farm partnership, (for at least two years) in which the individual, their spouse, child/grandchild, or parent/grandparent was actively engaged, it may also be qualified farm property.

Land Acquired prior to June 17, 1987

If the land was acquired before June 17, 1987, to be considered qualified farm property, it must have been used principally in a farming business in the year of sale by the individual, their spouse, child/grandchild, or parent/grandparent, or for at least five years during its ownership. There is no gross revenue test.

Cautions

Assuming the criteria above is met and the land is qualified farm property, there are still some things to consider before claiming a capital gains deduction.

The Income Tax Act places an emphasis on an individual's lineage. It's their (or their spouse's) parent/grandparent or child/grandchild that is often looked at to meet the gross revenue test, especially in the case of a non-farming seller.

Caution #1 - One pitfall that is often overlooked, and is a quirk of the lineage rules, is when a non-farming couple inherits a parcel of farmland that belonged to one of the spouse's parents/grandparents who did farm. If the non-farming child of that parent/grandparent passes away, the land would not be qualified farm property in the hands of the surviving spouse. For example, a non-farming couple inherits a parcel of farmland from the husband's father, who was

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an active farmer and met the gross revenue test. While the couple is together, the Income Tax Act considers the husband's father to be the wife's father as well. However, if the husband was to pass away, the surviving spouse would no longer have someone in her lineage who could meet the gross revenue test – her deceased husband's father is not part of her lineage.

Caution #2 - One of the questions we ask couples who consider selling their farmland is whether the land was acquired by one of them prior to their marriage. If it was, then the sale of that property cannot be split on the couple's tax return; the entire profit must be reported by the individual who acquired the land in the first place. In this case, the only way it can be split is if the individual actually sold a half-share of the parcel, for market value, to their spouse.

Caution #3 - One final pitfall is when farmland was acquired for less than market value, or at no cost, from a parent/grandparent. In these cases, the land may be qualified farm property, but if it was owned for less than three years before being sold, then the profit must be reported by the parent/grandparent.

To find out if your farmland is qualified farm property, or for more information on the capital gains deduction, contact your Collins Barrow advisor.

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