Wealth Management
Dominion Securities

Life events: Selling a farm

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Financial checklist

If you have a farm you intend to either pass on to family or sell to arm's length parties, you may be able to take advantage of several beneficial tax strategies that can either defer and/or reduce tax payable.

Ordinarily when property is transferred to another party it is considered a disposition for tax purposes. This will be the case in inter vivos (while alive) or testamentary transfers (on death). In many cases, a taxable capital gain will arise. However, the Income Tax Act (ITA) provides special rules that apply to eligible farm property.

Sale/Transfers to arm's-length parties

Where a farm is being sold to an arm's-length party (typically not a family member) there will be a deemed disposition for tax purposes at the current Fair Market Value of the property. This will probably result in either capital gains or losses. However, some tax relief may be gained by taking advantage of the Capital Gains Exemption and or Principal Residence Exemption (discussed below).

Inter vivos transfers (while the transferor is alive)

If you want to pass your farm on to your family, typically children, you can do this on a tax-free basis provided the situation meets specific criteria. The rules can be quite complex and specific and although professional assistance should always be sought out in practice, following are some of the rules:

Child

- A child is basically defined as a natural or adopted child, grandchild or great-grandchild
- The child must be a resident in Canada immediately before the transfer

Farm

- The farm must be located in Canada
- The farm must have been used principally for the purpose of farming immediately before the transfer by the transferor, his/her spouse, or children
- The farm could be a farming corporation or farm partnership

If these criteria are met, you have the choice to select a transfer price anywhere between the cost of the property (Adjusted Cost Base or ACB) and the Fair Market Value (FMV). The child will receive the property with an ACB equal to the transfer price chosen.

Legal/Ethical issues on transfers of a farm to family members

While there are definite tax advantages available for transfers of a farm to a family member (typically a child) there are other factors that should be considered:

- Provincial family law accords certain rights to spouses, dependent children, and to a lesser extent, adult children. Consequently, when making farm transfers to a particular family member you must ensure that the property rights of other family members are not being compromised.
- You may want to be sure that all family members are being treated fairly when transferring a farm. This will be of particular importance where there are multiple children. Life insurance is one strategy that can be employed to achieve estate equalization.

The capital gains exemption (CGE)

Another very attractive tax advantage that may be available on the transfer of farm property is the $1 million capital gains exemption. The CGE allows for the protection of up to $1 million in capital gains on the transfer of eligible farm property. The definition of farm property is quite specific and somewhat more rigorous than for the farm rollover.

Example:

Further to the example above, Lily Usher decided to make use of the CGE when transferring the farm to her daughter. Since her farm qualified as eligible, she chose a transfer price of $1.2 million. She therefore incurred a capital gain of $1 million ($1.2 million - $200,000) which she was able to completely offset using the CGE. Her daughter then had a farm with an ACB of $1 million and an FMV of $1.2 million.

Farm transfers on death

The rules concerning transfers of property on death are quite similar to the Inter Vivos rules and the deceased's representative can choose to take advantage of the child rollover rules and/or the CGE if the required criteria are met.

Principal residence exemption

Where the farm property includes a house that meets the definition of a 'Principal Residence' the capital gain on the house can be determined separately from the farm itself and protected using the Principal Residence Exemption. As mentioned above, the actual rules and requirements for using the Farm rollover and CGE can be involved and complex. Your Advisor will have a lot more information but it is highly recommended to seek professional legal/tax assistance when contemplating a farm transfer.