



Canada Revenue
Agency

Agence du revenu
du Canada

Farming Income

2004

Before You Start

Is this guide for you?

This guide is for you if you earned income as a self-employed farmer or as a partner in a farm partnership. It will help you calculate the farming income you will report on your 2004 income tax return. If you are participating in the Canadian Agricultural Income Stabilization (CAIS) program, you have to use the *Farming Income and the CAIS Program* guide. However, CAIS participants in Quebec should use this guide for their tax return, and contact La Financière agricole du Québec, at 1-800-749-3646, regarding CAIS participation.

Forms and publications

In the middle of this guide, you will find two copies of Form T2042, *Statement of Farming Activities*.

Throughout the guide, we refer to other forms and publications. If you need any forms or publications, visit our Web site at www.cra.gc.ca. You may want to bookmark this address for easier access to our site in the future.

You can also order forms and publications by calling us at **1-800-959-2221**.

Wherever we make reference to an Information Circular or Interpretation Bulletin, we are referring to the current version of the circular or bulletin. We have deleted reference to release numbers. For example, we refer to IT-309R2 as IT-309.

Recent Changes

Throughout the guide, we use the name, Canada Revenue Agency, and the acronym, CRA, to reflect the new structure of the Canada Customs and Revenue Agency (CCRA.)

What's New for 2004?

Capital Cost Allowance (CCA) – The 2004 Federal Budget proposes new CCA classes for computer equipment and data network infrastructure equipment, acquired after March 22, 2004. The new rates will better reflect the useful life of these assets. For more information, see “Electronic office equipment” on page 33.

Non-capital loss – The 2004 Federal Budget proposes to extend the carry-forward period for non-capital losses from 7 to 10 years for taxation years ending after March 22, 2004. For further information, see “Non-capital loss” on page 43.

Do you need more information?

This guide uses plain language to explain the most common tax situations. If, after reading this guide, you need more information about farming activities, call us at **1-800-959-5525**.

Visually impaired persons can get our publications in braille, large print, or etext (computer diskette), or on audio cassette by visiting our Web site at www.cra.gc.ca/alternate or by calling **1-800-267-1267** weekdays from 8:15 a.m. to 5:00 p.m. (Eastern Time).

La version française de ce guide est intitulée *Revenus d'agriculture*.

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Chapter 1 – General Information

What is farming income?

Farming income includes income you earned from the following activities:

- soil tilling
- livestock raising or showing
- racehorse maintenance
- poultry raising
- dairy farming
- fur farming
- tree farming
- fruit growing
- beekeeping
- cultivating crops in water or hydroponics
- Christmas tree growing
- operating a wild-game reserve
- chicken hatchery
- operating a feedlot

In certain circumstances, you may also earn farming income from:

- raising fish
- doing market gardening
- operating a nursery or greenhouse

Farming income **does not** include income you earned from working as an employee in a farming business, or from trapping.

You were asking?

- Q. When does a farming business start? Can I deduct the costs I incur before and during the start of my farming business?
- A. We look at each case on its own merits. Generally, we consider that a farming business starts whenever you begin some significant activity that is a regular part of the farming business, or that is necessary to get the business going.

For example, suppose you decide to buy enough poultry for resale to start your farming business. We would consider this to be the starting point of your farming business. You can usually deduct all of the expenses you have incurred from that point to earn farming income. You could still deduct the expenses even if, despite all your efforts, your farming business wound up. On the other hand, if you review several different types of farming activities in the hope of going into a farming business of some kind, we would not consider that your business has begun, and you cannot deduct any of those costs.

For more details about the start of a business, see Interpretation Bulletin IT-364, *Commencement of Business Operations*.

The law allows Statistics Canada to access business information collected by the Canada Revenue Agency (CRA). Statistics Canada can now share with provincial statistical agencies, for research and analysis purposes only, data concerning business activities carried out in their respective province.

How do you report your farming income?

You can earn farming income as a self-employed farmer or as a partner of a farm partnership. Most of the rules that apply to a self-employed farmer also apply to a partner. However, if you are a partner, you should also read “Reporting partnership income” on page 6.

You report your farming income based on a **fiscal period**. A fiscal period is the time covered from the day your farming business starts its business year, to the day your farming business ends its business year. For an existing business, the fiscal period is usually 12 months. A fiscal period cannot be longer than 12 months. However, it can be shorter than 12 months in some cases, such as when a new business starts or when a business stops.

Self-employed individuals generally have to use a December 31 year-end. If you are an eligible individual, you may be able to use an alternative method of reporting your business income that allows you to keep a fiscal period that does not end on December 31. To determine if you are eligible to have a fiscal year-end that is not December 31, see the *Reconciliation of Business Income for Tax Purposes* guide, which includes Form T1139, *Reconciliation of 2004 Business Income for Tax Purposes*. It explains how to calculate the amount of farming income to report on your 2004 income tax return, and it also tells you if you have to file Form T1139 for 2004. In most cases, if you filed one for 2003, you will generally have to do so again for 2004.

Reporting methods

You can report your farming income using the cash method or the accrual method of accounting.

When you use the **cash method**, you:

- report income in the fiscal period you receive it; and
- deduct expenses in the fiscal period you pay them.

For special rules on prepaid expenses, see “Prepaid expenses” on page 14.

If you use the cash method and receive a post-dated cheque as security for a debt, include the amount in income when the cheque is payable.

If you receive a post-dated cheque as an absolute payment for a debt, include the amount in income when you get the cheque. If the bank does not honour the cheque, you can adjust your income then.

Note

The preceding post-dated cheque rules apply to income-producing transactions, such as the sale of grain. They do not apply to transactions involving capital property, such as the sale of a tractor.

When you use the cash method, do not include inventory when you calculate your income. However, there are two exceptions to this rule. For details, see “Line 9941 – Optional inventory adjustment included in 2004” and “Line 9942 – Mandatory inventory adjustment included in 2004” on pages 23 and 24.

For more details on the cash method for farming income, see Interpretation Bulletin IT-433, *Farming or Fishing – Use of Cash Method*.

When you use the **accrual method**, you:

- report income in the fiscal period you earn it, no matter when you receive it; and
- deduct expenses in the fiscal period you incur them, whether or not you pay them in that period.

When you calculate your income using the accrual method, the value of all inventories, such as livestock, crops, feed, and fertilizer will form part of the calculation. Make a list of your inventory and count it at the end of your fiscal period. Keep this list as part of your business records.

You can use **one** of the following three methods to value your inventory:

- value all inventory at its fair market value (see page 28 for the definition of fair market value);
- value individual items at cost or fair market value, whichever is lower (when you cannot easily tell one item from another, you can value the items as a group); or
- value livestock according to the unit price base. For this method, complete Form T2034, *Election to Establish Inventory Unit Prices for Animals*.

Use the same method you used in past years to value your inventory. The value of your inventory at the start of your 2004 fiscal period is the same as the value at the end of your 2003 fiscal period. If this is your first year of operating a farming business, you will not have an opening inventory at the start of your fiscal period.

For more details on inventories, see Interpretation Bulletin IT-473, *Inventory Valuation*.

Note

If you use the accrual method to calculate your farming income, calculate your cost of goods sold on a separate piece of paper. Form T2042 does not have a line to calculate this amount.

Changing your method of reporting income

If you decide to change your method of reporting income from the accrual method to the cash method, use the cash method when you file your income tax return. Make sure you include a statement that shows each adjustment you had to make to your income and expenses because of the difference in methods.

If you decide to change from the cash method to the accrual method, you have to ask the director of your tax services office for approval, in writing, before the deadline for filing your income tax return. In your letter, explain why you want to change methods.

Because there is a difference between the cash and accrual methods, the first time you complete your income tax return using the accrual method, file a statement showing each adjustment you had to make to your income and expenses.

Business records

Keep a record of your daily income and expenses. We do not issue record books or suggest any particular type of book or set of books. Many record books and bookkeeping systems are available. For example, you can use a book that has columns and separate pages for income and expenses. Some provincial departments of agriculture provide bookkeeping records you can use.

Keep your books, along with your receipts, duplicate deposit slips, bank statements, and cancelled cheques. Keep separate records for each business you run. If you keep computerized records, make sure they are clear and easy to read.

Note

Do not send your records with your income tax return. However, you must keep them in case we ask to see them. If you do not keep the necessary information and you do not have any other proof, we may have to determine your income using other methods. We may also have to reduce the expenses you deducted.

Income records

Keep track of the gross income your farming business earns. Gross income is your total income before you deduct expenses. Your income records should show the date, amount, and source of the income. Record the income whether you received cash, property, or services.

You must be able to support all income entries with original documents. Original documents include such things as sales invoices, cash-register tapes, receipts, cash purchase tickets from the sale of grain, and cheque stubs from marketing boards.

Expense records

Always get receipts, invoices, or other vouchers when you buy goods or services. The receipts have to show:

- the date of the purchase;
- the name and address of the seller or supplier;
- the name and address of the purchaser; and
- a full description of the goods or services.

Keep a record of the properties you bought. This record should show who sold you the property, the cost, and the date you bought it. It will also help you calculate your capital cost allowance (CCA). Chapter 3 explains how to calculate CCA.

If you sell or trade a property, keep a record showing the date you sold or traded it, and the amount you got from the sale or trade-in.

Time limits

Depending on the situation, you have to keep your books, records, and related vouchers for the following lengths of time:

- if you file your income tax return on time, a minimum of six years after the end of the tax year to which they relate;
- if you file your income tax return late, six years from the date you file that return; or
- if you file an objection or an appeal, until either the issue is settled and the time for filing any further appeal expires, or until the six-year period mentioned above expires, whichever is later.

These retention periods do not apply to certain records. For more details, see Information Circular 78-10, *Books and Records Retention/Destruction*, and its Special Release.

If you want to destroy your books, records, and related vouchers before the minimum six-year period is over, you must first get written permission from the director of your tax services office. To do this, either use Form T137, *Request for Destruction of Books and Records*, or prepare your own written request.

Penalties

Include all your income when you calculate it for tax purposes. If you repeatedly fail to report your income, you may be subject to a penalty of 10% of the amount you failed to report.

Instalment payments

As a self-employed farmer, you may have to pay an annual instalment by December 31, 2005. If our records indicate that you may have to pay tax by instalments, we will send you an *Instalment Reminder* in late November indicating the amount you have to pay.

You may have to pay interest and a penalty if you do not pay the full instalment that you owe on time.

For more information and to see how to calculate your instalments, see our pamphlet *Paying Your Income Tax by Instalments*.

Dates to remember

February 28, 2005 – If you have employees, file your 2004 T4 *Summary* and T4A *Summary* forms. Also, give your employees their copies of the T4 and T4A slips.

March 31, 2005 – Most farm partnerships will file a partnership information return by March 31, 2005. However, there are exceptions. For details, see the *Guide for the Partnership Information Return* and Information Circular 89-5, *Partnership Information Return*, and its Special Release.

April 30, 2005 – Payment of any balance owing is due. You will have to file your 2004 income tax return by April 30, 2005, if the expenditures of your farming business are primarily connected with tax shelters.

June 15, 2005 – If you have farming business income or if you are the spouse or common-law partner of someone who does, you have until June 15, 2005 to file your 2004 income tax return, unless the expenditures of the business are primarily connected with tax shelters. However, you have to pay any balance owing by April 30, 2005, to avoid interest charges.

December 31, 2005 – Pay your 2005 instalment for income tax and Canada Pension Plan (CPP) contributions.

Note

If any of the dates mentioned above fall on a Saturday, Sunday, or statutory holiday, you have until the next business day to file your return or make your payment.

Goods and services tax/harmonized sales tax (GST/HST) registration

If your total gross revenue from your GST/HST taxable sales (those taxed at the rates of 0%, 7%, and 15%) is more than \$30,000 in a current calendar quarter or in four consecutive calendar quarters, you have to register for GST/HST.

If your gross revenue is equal to or less than \$30,000, you do not have to register, but you may do so voluntarily. If you register, you can claim input tax credits.

For information about GST/HST taxable farm goods and services, zero-rated farm products, and zero-rated farm purchases, see page 52.

Note

Nova Scotia, New Brunswick, and Newfoundland and Labrador harmonized the GST with their provincial sales tax to create the HST. The HST rate in these provinces is 15% and the GST rate in the rest of Canada is 7%.

Reporting partnership income

A partnership does not pay income tax on its income or file a tax return. Instead, each partner files an income tax return to report his or her share of the partnership's net income or loss. The partners have to do this whether the share of income was received in cash, or as a credit to a capital account in the partnership.

Interpretation Bulletin IT-90, *What is a Partnership?*, has more details about partnerships.

Partnership information return

Partnerships that had six or more partners at any time in the fiscal period have to file a partnership information return. Partnerships of five or fewer partners throughout the year also have to file a partnership information return if one or more of the partners is another partnership.

Partnerships also have to file a partnership information return if they invested in flow-through shares of a principal-business corporation that incurred Canadian resource expenses and renounced those expenses to the

partnership. If you are a partner in a partnership that has to file a partnership information return, you should get two copies of a T5013 slip, *Statement of Partnership Income*, from the partnership. If you do not receive this slip, contact the person who prepares the forms for the partnership.

The *Guide for the Partnership Information Return* has more details about the return.

On your tax return, report the gross partnership income and your share of the net partnership income or loss. You will get these amounts from your T5013 slip or partnership financial statement. Attach copy 2 of your T5013 slip to your income tax return. Do not attach the partnership's income and expense statement.

You may also need to adjust your share of the net partnership income or loss shown on your T5013 slip. Use Form T2042, *Statement of Farming Activities*, to deduct any business expenses you incur for which the partnership did not repay you. For more information, see "Line 9943 – Other amounts deductible from your share of net partnership income (loss)" on page 26.

Capital cost allowance (CCA)

As an individual partner, you cannot claim CCA on property owned by a partnership to which you belong. Only the partnership can claim CCA on the depreciable property that the partnership owns. Any CCA calculated at the partnership level will, however, be allocated to you according to your share of the partnership interest. It will, therefore, reduce the amount of net income that the partnership allocates to you.

From the capital cost of depreciable property, the partnership has to subtract the following amounts:

- any investment tax credit allocated to the individual partners (we consider this allocation to be made at the end of the partnership's fiscal period); and
- any type of government assistance.

For more details about CCA and the adjustments to capital cost, see Chapter 3. Also see "Column 4 – Adjustments" in Chapter 9 of the *Guide for the Partnership Information Return*.

Any capital gain or recapture from the sale of property the partnership owns is income of the partnership. Also, any capital or terminal loss from the sale of partnership-owned property is the loss of the partnership. See Chapter 6 for more details about capital gains and losses. For more details about recapture and terminal losses, see "Column 5 – UCC after additions and dispositions" on page 31.

Eligible capital expenditures

A partnership can own eligible capital property and deduct an annual allowance. Any income from the sale of eligible capital property the partnership owns is income of the partnership. See Chapter 4 for more details about eligible capital expenditures.

Investment tax credit (ITC)

The ITC lets you subtract, from the taxes you owe, part of the cost of some types of property you acquired or

expenditures you incurred. You may be able to claim this credit if in 2004 you:

- bought qualifying property;
- incurred qualifying expenditures, including monies paid to agricultural organizations through check-offs, levies, or cash assistance; or
- received renounced Canadian exploration expenses.

You may also be able to claim the credit if you have unused ITCs from years before 2004.

For more information about ITCs, see Form T2038(IND), *Investment Tax Credit (Individuals)*.

Goods and services tax/harmonized sales tax (GST/HST) rebate

If you are a partner in a partnership and you claimed expenses on your tax return, you may be able to get a rebate for any GST/HST you paid on the expenses.

The GST/HST rebate is available to you as long as you meet **both** of these conditions:

- you are a partner in a GST/HST-registered partnership; and
- on your tax return, you deducted expenses incurred to earn partnership income for which the partnership did not repay you.

We base the rebate on the amount of the expenses subject to GST/HST that you deduct on your income tax return.

For more details about the GST/HST rebate, see the *GST/HST Rebate for Partners* guide, which includes Form GST370, *Employee and Partner GST/HST Rebate Application*.

Chapter 2 – Calculating Your Farming Income or Loss

As a self-employed farmer, you have to give us a statement that accurately shows your farming activities for the year.

We have included Form T2042, *Statement of Farming Activities*, in the middle of this guide to help you calculate your farming income and expenses for income tax purposes. Although we accept other types of financial statements, we encourage you to use Form T2042. If you are participating in the Canadian Agricultural Income Stabilization (CAIS) program, do not use Form T2042. Instead, use Form T1163, *Statement A – CAIS Program Account Information and Statement of Farming Activities for Individuals*. We have included Form T1163 in the *Farming Income and the CAIS Program* guide. If you need Form T1163 or the CAIS Program guide, visit our Web site at www.cra.gc.ca or call us at 1-800-959-2221.

This chapter explains how to complete Form T2042. You have to complete a separate form for each business you operate. Interpretation Bulletin IT-206, *Separate Businesses*,

has more details about the tax consequences of operating more than one business.

Form T2042, Statement of Farming Activities

If you use Form T2042 and you are:

- **A sole proprietor** of a farming business, complete the entire form.
- **A partner in a partnership and you receive a T5013 slip**, complete only the items in the “Identification” area of Form T2042 that do not appear on your T5013 slip. Enter the amount from box 18 of your T5013 slip on line d on page 2 of Form T2042.

On page 4 of Form T2042, complete the “Other amounts deductible from your share of net partnership income (loss)” chart to claim any expenses for which the partnership did not reimburse you, or other amounts you may be able to deduct. If it applies to you, complete the “Calculation of business-use-of-home expenses” chart on page 4 of Form T2042. For more information, see page 27.

- **A partner in a partnership and you did not receive a T5013 slip**, complete all the areas and lines on Form T2042. Report the income and the business part of expenses for the partnership on Form T2042.

On page 4 of Form T2042, complete the “Other amounts deductible from your share of net partnership income (loss)” chart to claim any expenses for which the partnership did not reimburse you or any other amounts you may be able to deduct. If it applies, complete the “Calculation of business-use-of-home expenses” chart on page 4 of Form T2042. For more information, see page 27.

Complete the “Details of other partners” chart on page 4 of Form T2042.

To find out if your partnership has to file a partnership information return, see “Partnership information return” on page 6.

In the following text, we explain how to complete each of the lines on Form T2042.

Identification

The “Identification” area is self-explanatory. You will, however, need details on the industry code. Enter the **industry code** that best describes your farming activity. If more than 50% of your farming business involved one specific activity, choose the code that identifies that main activity. However, if your farming operation involved more than one type of farming activity, and none of these makes up more than 50% of your farming business, choose the appropriate combination farming code from the list. The following are lists of these codes for farming operations:

Livestock farm

- 112110 Beef cattle, including feedlots
- 112120 Dairy cattle and milk
- 112210 Hogs and pigs
- 112310 Chicken eggs (including hatching eggs)

- 112320 Broiler and other meat-type chickens
- 112330 Turkeys
- 112340 Poultry hatcheries
- 112391 Combination poultry and eggs
- 112399 All other poultry and eggs
- 112410 Sheep
- 112420 Goats
- 112510 Animal aquaculture (such as frogs, fishes, shellfishes)
- 115210 Support activities for animal production (husbandry services)
- 112991 Livestock combination farming, and livestock farming with secondary crop farming

Other animal specialties farm

- 112910 Apiculture (beekeeping)
- 112920 Horses and other equines
- 112930 Fur-bearing animals and rabbits
- 112999 All other miscellaneous animals

Field-crop farm

- 111110 Soybeans
- 111120 Oilseed (including canola, flax, mustard, and sunflowers)
- 111130 Pulse crops (such as dry field peas, beans, and lentils)
- 111140 Wheat
- 111150 Corn
- 111190 Cereals (such as barley, oats, rye, and growing wild rice)
- 111211 Potatoes
- 111219 Other vegetables (except potatoes) and melons
- 111330 Non-citrus fruit and tree nuts
- 111411 Mushrooms
- 111419 Other food crops grown under cover
- 111421 Nursery and tree production
- 111422 Floriculture
- 111910 Tobacco
- 111940 Hay
- 111993 Fruit and vegetable combination farming
- 111999 Miscellaneous crops, combination of crops, and combination of crops with secondary livestock farming
- 115110 Support activities for crop production (soil preparation, pruning, spraying, harvesting, fruit picking, crop clearing, sorting, grading) on contract

Farming income

Line 9370 – Total grains and oilseeds

Enter the income from the sale of your grains and oilseeds on the proper lines. Enter the total sales on line 9370.

If you sold grain directly or through an agency, include in income all the amounts you received from these sales. For example, include any Canadian Wheat Board payments from the sale of wheat, durum wheat, and barley.

When you delivered grain to a licensed public elevator or process elevator, you received a storage ticket, a cash purchase ticket, or a deferred cash purchase ticket.

If you received a **storage ticket**, a sale did **not** take place. Therefore, you do not have to include that amount in income.

However, if you received a **cash purchase ticket**, a sale **did** take place. Because we consider that you received a payment at the time you received the ticket, you have to include the amount in income.

If you received a **deferred cash purchase ticket**, you may be able to defer the income until the following tax year. You can do this if the ticket provides for payment after the end of the tax year in which you delivered the grain. This carry-over of income is only allowable in specific situations. For more details, see Interpretation Bulletin IT-184, *Deferred Cash Purchase Tickets Issued for Grain*.

Cash advances

Under the *Agricultural Marketing Programs Act*, you may be able to get advances for crops that someone stores in your name. We consider these advances to be loans. Do not include these payments in your income until the crops are sold. However, for the tax year in which the sale occurs, include the full amount from the sale of your crops in your income.

Lines 9421 to 9424 (inclusive)

Enter the total income from the sale of the identified produce on the applicable line. Whether you sold produce directly or through an agency, include in income all the amounts you received from these sales.

Do not include amounts received from the sale of greenhouse vegetables. See line 9425 for details on these vegetables.

Line 9420 – Other crops

Enter the total income from the sale of pulse crops, sugar beets, hops, or any other crops you have not identified on another line.

Line 9425 – Greenhouse and nursery products

Enter the total income from the sale of such things as ornamental plants, shrubs, trees, cut and field-grown flowers, rooted cuttings, seeds and bulbs, sod and turf, and greenhouse vegetables.

Line 9426 – Forage crops or seeds

Enter the total income from the sale of hay, alfalfa, clover and clover seed, alsike, timothy, fescue, grass seed, or any other forage crops or seeds.

Lines 9471 to 9474 (inclusive) – Livestock sold

On the applicable line, enter the total income from the sale of the identified livestock. In some cases you can defer including some amounts in income, as explained below. These deferrals do not apply if you were a non-resident and were not carrying on a farming business through a fixed place of business in Canada at the end of the tax year. They also do not apply in the year of the farmer's death.

Line 9470 – Other animal specialties

Enter on this line the total income from the sale of any other livestock not specifically identified on another line (for example, the sale of horses, ponies, goats or llamas). Include amounts from the sale of fur-bearing animals you raised in captivity, such as fox, chinchilla, mink, or rabbit, as well as income from an apiary operation.

Prescribed drought region (PDR)

In some cases, you may be able to defer the applicable income received from the sale of breeding animals in your 2004 fiscal period to a later fiscal period. To be able to do this, the following **two** conditions have to apply:

- your farming business was located in a PDR at some time during your 2004 fiscal period; and
- you reduced, by sale or other means, the number of breeding animals in your breeding herd by at least 15%.

For a list of PDRs, contact us or Agriculture and Agri-Food Canada. You will find the addresses and telephone numbers in the government section of your telephone book.

The following are considered to be breeding animals:

- bovine cattle;
- bison;
- goats;
- sheep;
- deer, elk, and other similar grazing ungulates you keep for breeding; and
- horses you breed to produce pregnant mares' urine that you sell.

All your breeding animals must be older than 12 months.

To determine the size of your breeding herd at the end of your 2004 fiscal period, complete Part 1 and Part 2 of the following chart.

Breeding herd chart

Part 1

How many of your female bovine cattle over 12 months of age (held at the end of your 2004 fiscal year) have given birth? _____ **A**

How many of your female bovine cattle over 12 months of age (held at the end of your 2004 fiscal year) have **never** given birth? _____ **B**

Enter one half of the amount from line A _____ **C**

Enter either the amount from line B or line C, whichever is less _____ **D**

Part 2

How many breeding animals did you have at the end of your 2004 fiscal period? _____ **E**

Enter the amount from line B _____ **F**

Enter the amount from line D _____ **G**

Line F **minus** line G _____ **H**

Number of breeding animals in your breeding herd at the end of your 2004 fiscal period: Line E **minus** line H _____ **I**

If the figure from line I is **not** more than 85% of the total number of animals in your breeding herd at the end of your 2003 fiscal year, you can defer part of the income received in 2004 from the sale of breeding animals.

Before you determine how much you can defer, you need to calculate a few amounts. First, determine your sales of breeding animals for your 2004 fiscal period minus any reserves you claimed for these sales.

A **reserve** is created when you sell property and do not receive the full proceeds at the time of the sale. Instead, the amount of proceeds is spread over a number of years, which allows you to defer reporting these proceeds to the year in which you receive them. For more details on reserves, see Interpretation Bulletin IT-154, *Special Reserves*.

After you have determined your sales of breeding animals, subtract from this amount the cost of breeding animals you bought in your 2004 fiscal period. The result is your net sales amount.

You then determine how much you can defer as follows:

- if the amount at line I is more than 70% and not more than 85% of your breeding herd at the end of your 2003 fiscal period, you can defer up to 30% of your net sales amount; or
- if the amount at line I is between 0% and 70% of your breeding herd at the end of your 2003 fiscal period, you can defer up to 90% of your net sales amount.

You do not have to defer all of this income. You can include any part of it in your 2004 income. The deferred income must, however, be reported in the fiscal period that ends in:

- the year beginning after the period or periods when the region stops being a PDR;
- the year when a farmer dies; or

- the first year when, at the end of that year, the farmer is a non-resident and has ceased to carry on business through a fixed place of business in Canada.

If you want, you can elect to report the deferred income in the year after you deferred it.

If your farming business was not in a PDR at any time during your 2004 fiscal period, you cannot defer the amount you received when you sold breeding animals. Also, you have to include in your 2004 income any unreported amounts you deferred in earlier years.

However, as long as your farming business was in a PDR at any time in your 2004 fiscal period, you do not have to include income you deferred in earlier years.

Line 9476 – Milk and cream, (not including dairy subsidies) and Line 9477 – Eggs

On the applicable line, enter the total income from selling eggs, milk, and cream. Do not include any amount you received as dairy subsidies. Include dairy or milk subsidies you received in your 2004 fiscal period on line 9541.

Line 9520 – Other commodities

On this line, enter the total income from selling any other commodity not specifically identified on another line. Other commodities include the sale of semen, stud services, embryo transplants, artificial insemination, and pregnant mares' urine. Also include amounts from the sale of maple products, mushrooms, and ginseng.

Program payments

You should receive an AGR-1 slip, *Statement of Farm-Support Payments*, to identify your 2004 taxable farm-support payments. According to the *Income Tax Regulations*, you have to provide your social insurance number, when requested, to organizations that issue farm-support payments.

You should receive an AGR-1 slip for all farm-support programs from which you received payments of more than \$100. These include farm-support programs administered by the federal, provincial, territorial, and municipal governments, and by producer associations.

You have to include in income all taxable farm-support payments you received in your 2004 fiscal period, including amounts of \$100 or less.

If your farm is operated as a partnership, only one partner should attach the AGR-1 slip to his or her income tax return. However, if your partnership has to file a partnership information return, you should file the slip with that return.

If the annual period of the AGR-1 slip is not the same as the fiscal period of your farming operation, report only the part of the farm-support payments that you earned during your normal fiscal period. For example, if your farming business has a fiscal period ending on June 30, 2004, and your AGR-1 slip shows income of \$10,000 in box 14, but you earned only \$6,000 of that income by June 30, 2004, include only \$6,000 in your income for your 2004 fiscal period. Include the remaining \$4,000 in your next fiscal period.

However, include the AGR-1 slip issued for the 2004 calendar year with your 2004 income tax return.

If you are a former Net Income Stabilization Account (NISA) program participant and received an AGR-1 slip with a positive amount in box 18, report it as income on line 130 of your income tax return. The figure in box 18 represents taxable amounts paid out of your NISA Fund 2 account.

The back of the AGR-1 slip contains information about how to report amounts that appear in the various boxes.

Line 9541 – Dairy subsidies

Include in your income the dairy or milk subsidies you received.

Line 9542 – Crop insurance

Include in your income any insurance proceeds you received from federal, provincial, or joint federal/provincial programs for loss of crops.

Line 9540 – Other payments

Include the total income you received from all other stabilization and farm-subsidy programs made to farm producers under federal, provincial, municipal, or joint programs.

Disaster assistance program payments – Enter any payments you received from federal or provincial disaster assistance programs. These include the following:

- the Agricultural Income Disaster Assistance (AIDA) Program in Saskatchewan, Manitoba, Nova Scotia, Newfoundland and Labrador, New Brunswick, Prince Edward Island, and Quebec
- the Canadian Farm Income Program (CFIP) in Saskatchewan, Manitoba, Nova Scotia, Newfoundland and Labrador, New Brunswick, Prince Edward Island, and Quebec
- the Whole Farm Insurance Pilot (WFIP) Program in British Columbia
- the Farm Income Disaster Program (FIDP) in Alberta
- the Ontario Whole Farm Relief Program (OWFRP) and the Ontario Farm Income Disaster Program (OFIDP) in Ontario

Destroying livestock – You have to include in income any payments you received under the *Health of Animals Act* for destroying animals. You can choose to deduct all or part of the payment as an expense in the year. However, if you choose to do this, you have to include in your income for your next fiscal period the amount you deduct in your 2004 fiscal period. If you deferred payments in your 2003 fiscal period, you have to include the deferred amounts as income in this fiscal period.

Line 9570 – Rebates

Include the amount of the rebate, grant, or assistance you received on this line. Before doing so, reduce any related expense or the capital cost of a related depreciable asset by the amount of the rebate, grant, or assistance you received.

For more details, see “Rebates, grants, or assistance” on page 13. For information about GST/HST rebates, see “Goods and services tax/harmonized sales tax (GST/HST) rebate” on page 6.

Line 9601 – Custom or contract work, and machine rentals

Enter the total of your incidental farming income from such things as custom or contract work, hauling, custom trucking, harvesting, combining, crop dusting or spraying, seeding, drying, packing, cleaning, treating seeds, and renting farm machinery.

Line 9604 – Insurance proceeds

Enter the amount of any insurance proceeds you received as compensation for loss or damage to certain types of property. For example, you may have received insurance proceeds for damage to a building due to fire, or for the loss of livestock to disease.

Enter the total insurance proceeds on this line if you are being reimbursed for:

- the cost of non-depreciable property that you previously deducted as a current expense; or
- the cost of property that was a saleable item, such as livestock.

If the insurance proceeds compensated you for **damages** to depreciable property, and you used all of them to **repair** the property within a reasonable period of time, include the proceeds as income on this line. Claim a deduction for the same amount in the “Other expenses” area on page 2 of Form T2042. Claim repairs to depreciable property that is machinery on line 9760 and repairs to motor vehicles on line 9819. If you did not spend all of the insurance proceeds on repairs within a reasonable length of time, we consider the amounts you did not spend to be proceeds of disposition. Report these amounts in column 4 of Area E on page 3 of Form T2042. For details, see “Column 4 – Proceeds of disposition in the year” on page 30.

Insurance proceeds that compensate you for **replacement** of **lost** or **destroyed** depreciable property are considered to be proceeds of disposition for that depreciable property. Do not include this type of insurance proceeds on this line. For details, see Chapter 3. For information on how insurance affects the adjusted cost base of capital property, you can also see Chapter 6.

Do not include insurance proceeds from federal, provincial, or municipal government programs. For details on government insurance programs, see lines 9540 and 9542 on this page.

Line 9605 – Patronage dividends

Include all patronage dividends (other than those for consumer goods or services) you received. We consider a patronage dividend that is a share or certificate of indebtedness to be income at the time you received it.

Line 9600 – Other income

Enter the total of any other farming income that you have not specifically identified on another line. The following paragraphs identify some of these income items.

Wood sales (including stumps)

If you operated or regularly harvested a woodlot, include in your income the amounts from the sale of trees, lumber, logs, poles, or firewood.

From this income, you can deduct a type of capital cost allowance known as a depletion allowance. For details, see Interpretation Bulletin IT-481, *Timber Resource Property and Timber Limits*.

If you earned the income by letting other people remove standing timber from your woodlot, the proceeds may be a capital receipt. A taxable capital gain or an allowable capital loss may result. For more details on capital gains and losses, see Chapter 6 of this guide and the *Capital Gains* guide.

For more details on the sale of wood, see Interpretation Bulletin IT-373, *Woodlots*.

Gifts

In your income, include the fair market value of livestock or other items you gave away that you would normally have sold. For the definition of fair market value, see page 28.

Once you give the livestock or other items away, you cannot deduct any more costs for raising or maintaining them.

Payment in kind

A payment in kind occurs when you receive or give goods or services instead of money. For instance, to pay someone for a business expense, you may give them something you produced on your farm instead of money. When you do this, include the fair market value of the goods or services in income. Deduct the same amount as an expense.

If you received a payment in kind for a product you would normally have sold, include the fair market value of the product in income.

If you were a landlord renting out land involved in sharecropping, we consider any payment in kind you received to be rental income.

Surface rental for petroleum or natural gas exploration

If you received payments for leasing your farmland for petroleum or natural gas exploration, these payments will be either income or a capital receipt.

Include in your income the yearly amounts for rental, severance, or inconvenience from a surface rental agreement.

The first payment from these agreements is often larger than the rest of the annual payments. However, the agreement may not specify how much of the first payment is for such things as damage to land, land improvements, severance, inconvenience, or the first year's rent. When this happens, in the year you received the first payment, include in income an amount that is equal to the annual payment you will receive in the following years. The rest of

the first payment is a payment for property. This may result in either a capital gain or loss. For details about capital gains, see Chapter 6.

Rental income

Except for the surface rental previously explained, you do not usually include rental income in your farming income. To determine your rental income, use Form T776, *Statement of Real Estate Rentals*. You will find this form in the *Rental Income* guide.

If you were a landlord renting out land involved in sharecropping, we consider the payments you received, whether in kind or cash, to be rental income for tax purposes.

Recapture of capital cost allowance (CCA)

Include in your income the amount of any recapture of CCA you have from selling depreciable property such as tools and equipment.

Complete the applicable areas on Form T2042 to find out if you have any recapture of CCA. For details, see Chapter 3.

Miscellaneous

Include in your income amounts you receive from the sale of soil, sand, gravel, or stone. For some of these items, you can claim a depletion allowance.

You can deduct 100% of the cost of property such as small tools if they cost less than \$200. If you did this and you later sold that property, you have to include in income the amount you received from the sale.

Include in your income prizes you won from fairs or farming exhibitions. For more details, see Interpretation Bulletin IT-213, *Prizes From Lottery Schemes, Pool System Betting and Giveaway Contests*.

Line 9659 – Gross income

Gross farming income is your total farming income before you deduct expenses. Enter your gross farming income on line 168 of your income tax return.

Farming expenses

The phrase “enter business part only” on Form T2042 means that you cannot include any of the following as part of your expenses:

- the cost of saleable goods or services you, your family, or your partners and their families personally used or consumed (saleable goods include items such as dairy products, eggs, fruit, vegetables, poultry, and meat)
- the part of any expenses that you can attribute to your personal use of the farming business, or partnership property or services
- salary, wages, or drawings paid to yourself, partner(s), or both
- donations to charities and political contributions
- interest and penalties you paid on your personal tax return

- most life insurance premiums (see line 9804 on page 16 for details on a limited exception).

Current or capital expenses

Renovations and expenses that extend the useful life of your property or improve it beyond its original condition are usually capital expenses. However, an increase in a

property's market value because of an expense is not a major factor in deciding whether the expense is capital or current. To decide whether an amount is a current expense or a capital expense, consider your answers to the questions on the following chart.

Current or capital expenses		
Criteria	Capital expenses	Current expenses
Does the expense provide a lasting benefit?	A capital expense generally gives a lasting benefit or advantage. For example, the cost of putting vinyl siding on the exterior walls of a wooden house is a capital expense.	A current expense is one that usually recurs after a short period. For example, the cost of painting the exterior of a wooden house is a current expense.
Does the expense maintain or improve the property?	The cost of a repair that improves a property beyond its original condition is probably a capital expense. If you replace wooden steps with concrete steps, the cost is a capital expense.	An expense that simply restores a property to its original condition is usually a current expense. For example, the cost of repairing wooden steps is a current expense.
Is the expense for a part of a property or for a separate asset?	The cost of replacing a separate asset within that property is a capital expense. For example, the cost of buying a compressor for use in your business operation is a capital expense. This is the case because a compressor is a separate asset, and is not a part of the building.	The cost of repairing a property by replacing one of its parts is usually a current expense. For instance, electrical wiring is part of a building. Therefore, an amount you spend to rewire is usually a current expense, as long as the rewiring does not improve the property beyond its original condition.
What is the value of the expense? (Use this test only if you cannot determine whether an expense is capital or current by considering the three previous tests.)	Compare the cost of the expense to the value of the property. Generally, if the cost is of considerable value in relation to the property, it is a capital expense.	This test is not a determining factor by itself. You might spend a large amount of money for maintenance and repairs to your property all at once. If this cost was for ordinary maintenance that was not done when it was necessary, it is a maintenance expense, and you deduct it as a current expense.
Is the expense for repairs to used property that you acquired to put it in suitable condition for use?	The cost of repairing used property that you acquired to put it in a suitable condition for use in your business is considered a capital expense even though in other circumstances it would be treated as a current operating expense.	Where the repairs were for ordinary maintenance of a property that you already had in your business, the expense is usually current.
Is the expense for repairs made to an asset in order to sell it?	The cost of repairs made in anticipation of the sale of a property, or as a condition of sale, is regarded as a capital expense.	Where the repairs would have been made anyway, but a sale was negotiated during the course of the repairs or after their completion, the cost is regarded as current.

For more information, see Chapter 3 and Interpretation Bulletin IT-128, *Capital Cost Allowance – Depreciable Property*.

Rebates, grants, or assistance

You should subtract from the applicable expense any rebate, grant, or assistance you received. Enter the net expense on the appropriate line on Form T2042.

If the rebate, grant, or assistance is for a depreciable asset, subtract it from the property's capital cost before calculating CCA. For details, see Chapter 3. If the asset qualifies for the investment tax credit, this reduction to the capital cost will also affect your claim. For details, see Form T2038(IND), *Investment Tax Credit (Individuals)*.

If you cannot apply the rebate, grant, or assistance to reduce a particular expense or a property's capital cost, include the amount as income on line 9570. Only include the amount that was not used to reduce the cost of a property or the amount of an outlay or expense.

GST/HST input tax credits

If you claim the GST/HST you paid on your farming business expenses as an input tax credit (ITC), reduce the amounts of the business expenses you show on Form T2042 by the amount of the ITC. Do this when the GST/HST for which you are claiming the ITC was paid or became

payable. Enter the net expense figure on the proper line on Form T2042.

ITCs that you claim for the purchase of depreciable property used in your business will affect your claim for CCA. If you cannot apply the credit you received to reduce a particular expense, or to reduce an asset's capital cost, include the amount as income at line 9570, "Rebates," on Form T2042.

For details about how input tax credits affect your claim for CCA, see "Column 2 – Undepreciated capital cost (UCC) at the start of the year" on page 29.

Prepaid expenses

A prepaid expense is the cost of a service you paid for ahead of time. For example, insurance, property taxes, and rent would be prepaid expenses if you paid in one year, but did not receive the benefits until the next year.

If you use the accrual method to determine your farming income, you can deduct the part of the prepaid expenses that applies to the tax year you receive the benefit.

If you use the cash method for reporting income, you cannot deduct a prepaid expense amount (other than for inventory) relating to a tax year that is two or more years after the year the expense is paid. However, you can deduct the part of an amount you paid in a previous year for benefits received in the current tax year. These amounts are deductible as long as you have not previously deducted them.

For example, if you paid \$600 for a three-year lease in 2004, you can deduct \$400 in 2004. This represents the part of the expense that applies to 2004 and 2005. On your 2006 income tax return, you could then deduct the balance of \$200 for the part of the prepaid lease that applies to 2006.

Line 9661 – Containers and twine

Enter the total amount you paid for material to package, contain, or ship your farm produce or products.

If you operated a nursery or greenhouse, deduct the cost of your containers and pots for the plants you sold.

Line 9662 – Fertilizers and lime

Enter the total amount you paid for fertilizers and lime you used in your farming business.

Line 9663 – Pesticides (herbicides, insecticides, fungicides)

Enter the total amount you paid for herbicides, insecticides, and fungicides.

Line 9664 – Seeds and plants

Enter the total amount you paid for seeds and plants. Do not include the cost of seeds and plants you used in your personal vegetable or flower garden.

Line 9711 – Feed, supplements, straw, and bedding

Enter the total amount you paid for feed, supplements, straw, and bedding you purchased for your farming business. You cannot deduct the value of the feed, straw, or bedding you grew.

Line 9712 – Livestock purchased

Enter the amount you paid for all livestock you purchased.

Line 9713 – Veterinary fees, medicine, and breeding fees

Enter the total amount you paid for medicine for your animals, and for veterinary and breeding fees. Examples of such fees include the cost of artificial insemination, stud service and semen, embryo transplants, disease testing, and neutering or spaying.

Machinery expenses

The expense of operating and maintaining your machinery is the total of line 9760 and line 9764 below.

Line 9760 – Repairs, licences, and insurance

Enter the total amount of repair, licence fee, and insurance premium expenses you incurred for your machinery. If you received insurance proceeds to help pay for repairs, see "Line 9604 – Insurance proceeds" on page 11 for more information.

Line 9764 – Gasoline, diesel fuel, and oil

Enter the total amount you paid for fuel and lubricants for your machinery.

Line 9795 – Building and fence repairs

Deduct repairs to fences and all buildings you used for farming, except your farmhouse. Do not include the value of your own labour. If the expenditure improved a fence or building beyond its original condition, the costs are capital expenditures. Add the expenditure to the cost of the asset on your capital cost allowance (CCA) charts on Form T2042. We explain the CCA charts in Chapter 3.

For more details on capital expenditures, see Interpretation Bulletin IT-128, *Capital Cost Allowance – Depreciable Property*.

If you used your farmhouse for business reasons, see "Line 9945 – Business-use-of-home expenses" on page 27.

Note

You may have received insurance proceeds to pay for the cost of repairs. If the insurance proceeds compensated you for damages to depreciable property such as buildings or fences, and you used all of them to repair the property within a reasonable period of time, you can claim a deduction for the amount spent on repairs on line 9795. However, you have to include the insurance proceeds as income on line 9604. If you did

not spend all of the insurance proceeds on repairs within a reasonable length of time, include the unexpended excess as proceeds of disposition in column 4 of "Area E – Calculation of capital cost allowance (CCA)" on Form T2042. For more details, see "Column 4 – Proceeds of disposition in the year" on page 30.

Line 9796 – Clearing, levelling, and draining land

Enter the total of the expenses listed below. In most cases, you can deduct the costs for:

- clearing the land of brush, trees, roots, stones, and so on;
- first ploughing the land for farm use;
- building an unpaved road; and
- installing land drainage.

You do not have to deduct all the costs in the year you paid them. If you paid all the costs, you can deduct any part of them in the year you paid them. You can carry forward any part of the costs you did not deduct to another year.

However, if you rented land to someone else, you cannot deduct the costs mentioned above. Instead, you may be able either to:

- add these costs to the cost of the land; or
- if you plan on building on the land right away, add these costs to the cost of the building; or
- if you installed a tile, plastic, or concrete land drainage system, the cost can be included under class 8 in the CCA charts on Form T776, *Statement of Real Estate Rentals*.

In this case, add the costs for a tile, plastic, or concrete land drainage system to class 8 on your CCA charts on Form T2042. For details, see Chapter 3.

For more details, see Interpretation Bulletin IT-485, *Cost of Clearing or Levelling Land*.

Improving land

You cannot deduct the cost of a paved road. Instead, you have to add this cost to class 17 on your CCA charts on Form T2042. For details, see Chapter 3.

You can deduct most of the cost to drill or dig water wells in the year you did the work. However, you have to add some of the costs to class 8 on your CCA charts. The costs you add to class 8 are those you incurred to purchase and install:

- the casing and cribwork for the well; and
- the system that distributes water, including the pump and pipes.

You can deduct amounts you paid to have public utilities brought to your farm, as long as the installations remain the property of the utility.

You can deduct amounts you paid under the *Canada Cooperative Associations Act* to build a distribution system under a gas service contract.

Line 9797 – Crop insurance

Enter the amount of deductible premiums to the Crop Insurance Program. Do not include any premiums for private, business-related, or motor vehicle insurance. For details on other types of insurance, see line 9760 on page 14, line 9804 on page 16, and line 9819 on page 19.

Line 9798 – Custom or contract work, and machinery rental

Enter the expenses you incurred for custom and contract work, and machinery rental. For example, you could have had a contract with someone who cleaned, sorted, graded, and sprayed the eggs your hens produced, or someone who had facilities to age the cheese you produced. You could have also contracted someone to do your harvesting, combining, crop dusting, or seed cleaning.

Line 9799 – Electricity

Only the part of your electricity costs that relates to your farming business is deductible. To determine the part you can deduct, keep a separate record of the amounts that apply to the farmhouse, and to other farm properties.

For example, the business part of your electricity expense will depend on how much electricity you used for the barns and shops. Because the electricity for the farmhouse is a personal expense, you cannot deduct it unless you meet the conditions we explain in "Line 9945 – Business-use-of-home expenses" on page 27.

Do not include on Form T2042 the electricity expense for a house that you rented to someone else. This is a rental expense, which you enter on Form T776, *Statement of Real Estate Rentals*. You can get Form T776 in the *Rental Income* guide.

Line 9802 – Heating fuel

Enter the total amount you paid for natural gas, coal, and oil to heat farm buildings. Also enter your expenses for fuel used for curing tobacco, crop drying, or greenhouses.

You can deduct only the part of these costs that relates to your farming business. To determine the part you can deduct, keep a separate record of the amounts you paid for the farmhouse and for other farm properties.

For example, the business part of your heating fuel expense will depend on how much heating fuel you used for the barns and shops. Because the heating fuel for the farmhouse is a personal expense, you cannot deduct it unless you meet the conditions we explain in "Line 9945 – Business-use-of-home expenses" on page 27.

Do not include on your statement of farming activities the heating fuel expenses for a house that you rented to someone else. This is a rental expense, which you enter on Form T776, *Statement of Real Estate Rentals*. You can get Form T776 in the *Rental Income* guide.

Line 9803 – Insurance program overpayment recapture

Enter the amount of any insurance program overpayment recapture you incurred. You should receive an AGR-1 slip,

Statement of Farm-Support Payments, identifying the amount of the recapture in box 17.

Line 9804 – Other insurance

Enter the amount of business-related insurance premiums you paid to insure your farm buildings, farm equipment (excluding machinery and motor vehicles), livestock, and business interruption.

In most cases, you cannot deduct your life insurance premiums. However, if you use your life insurance policy as collateral for a loan related to your farming business, you may be able to deduct a limited part of the premiums you paid. For more details, see Interpretation Bulletin IT-309, *Premiums on Life Insurance Used as Collateral*.

In most cases, you cannot deduct the amounts you paid to insure personal property such as your home or car. However, if you used the personal property for your farming business, you can deduct the business part of these costs. For more details, see “Line 9945 – Business-use-of-home expenses” on page 27 and “Line 9819 – Motor vehicle expenses” on page 19.

Premiums to private health services plans (PHSP)

You can deduct premiums paid or payable to a private health services plan (PHSP) if you meet the following conditions:

- your net income from self-employment (excluding losses and PHSP deductions) for the current or previous year is more than 50% of your **total income**,* or your **income from sources other than self-employment**** is \$10,000 or less, for the current or previous year;
- you are actively engaged in your farming business on a regular and continuous basis, individually or as a partner; and
- the premiums are paid or payable to insure yourself, your spouse or common-law partner, or any member of your household.

* For the purpose of this claim, calculate your **total income** as follows:

- the amount from line 150 of your 2003 or 2004 income tax return, whichever applies, before you deduct any amounts for PHSPs; **minus**
- the amounts you entered on lines 207, 212, 217, 221, 229, 231, and 232 on your 2003 or 2004 income tax return, whichever applies.

** For the purpose of this claim, calculate your **income from sources other than self-employment** as follows:

- the amount from line 150 of your 2003 or 2004 income tax return, whichever applies, before you deduct any amounts for PHSPs; **minus**
- the amounts you entered on lines 135, 137, 139, 141, 143 (excluding business losses which reduced the amount on those lines), 207, 212, 217, 221, 229, 231, and 232 on your 2003 or 2004 income tax return, whichever applies.

You cannot claim a deduction for PHSP premiums if another person deducted the amount, or if you or anyone

else claimed the premiums as a medical expense. For your premiums to be deductible, your PHSP coverage has to be paid or payable under a contract with one of the following:

- an insurance company
- a trust company
- a person or partnership in the business of administering PHSPs
- a tax-exempt trade union of which you or the majority of your employees are members
- a tax-exempt business organization or a tax-exempt professional organization of which you are a member

For more information on PHSPs, see Interpretation Bulletin IT-339, *Meaning of “private health services plan”*.

Note

In a cost-plus plan, the plan will only qualify as a PHSP if there is at least one employee. For example, a cost-plus plan that provides coverage for a sole proprietor and household members who are not employees will not qualify as a PHSP, since it is not an insurance plan.

Definitions

For the purpose of this claim, the following definitions apply:

- **Qualified employees** are arm’s length, full-time employees who have three months service since they last became employed with a business carried on by you, with a business in which you are a majority interest partner, or with a business carried on by a corporation affiliated with you. Temporary or seasonal workers are not qualified employees.
- **Arm’s length employees** are, generally, employees who are not related to you and who are not carrying on your business with you, for example, as your partners. For more details, see “Non-arm’s length transaction” on page 28.
- **Insurable persons** are people to whom coverage is extended and who are:
 - qualified employees;
 - people who would be qualified employees if they had worked for you for three months; or
 - people carrying on your business (including yourself and your partners).

How to calculate your maximum deduction for PHSPs

The following sections explain how to calculate your maximum PHSP deduction based on whether you had employees, and whether you insured them throughout the year or part of the year. Find the section that describes your situation.

If you did not have any employees throughout 2004

Your PHSP deduction is restricted by a dollar limit on an annual basis. The limit is a maximum of:

- \$1,500 for yourself
- \$1,500 for your spouse or common-law partner and household members who were 18 years of age or older at the start of the period when they were insured

- \$750 for household members under the age of 18 at the start of the period

The maximum deduction is also limited by the number of days the person was insured. Calculate your allowable maximum for the year by using the following formula:

$$\frac{A}{365} \times (B + C), \text{ where:}$$

- A is the number of days during the period of the year when you insured yourself and household members, if applicable, but insured less than 50% of your employees
- B equals \$1,500 × the number of household members 18 and over insured during that period
- C equals \$750 × the number of household members under 18 insured during that period

Example 1

Edwin was a sole proprietor who ran his farm alone in 2004. He had no employees and did not insure any of his household members. Edwin paid \$2,000 for PHSP coverage in 2004. His coverage lasted from July 1 to December 31, 2004, a total of 183 days. Edwin's maximum allowable PHSP deduction is calculated as follows:

$$\frac{183}{365} \times \$1,500 = \$752$$

Even though Edwin paid \$2,000 in premiums in 2004, he can only deduct \$752, because the annual limit is \$1,500 and he was only insured for about half of the year. If he had been insured for the entire year, his deduction limit would be \$1,500.

Example 2

Bruce was a sole proprietor who ran his farm alone in 2004. He had no employees. From January 1 to December 31, he insured himself, his wife, and his two sons. Bruce paid \$1,800 to insure himself, \$1,800 to insure his wife, and \$1,000 for each of his sons. One of his sons was 15 years old and the other turned 18 on September 1. Bruce's PHSP deduction is limited to the following amounts:

- for himself – \$1,500
- for his wife – \$1,500
- for his 15-year-old son – \$750
- for the son who turned 18 – \$750. This limit applies because he did not turn 18 until after the insured period began.

If you had employees throughout 2004

If you had at least one qualified employee throughout all of 2004, and at least 50% of the insurable persons in your business were qualified employees, your claim for PHSP premiums is limited in a different way. Your limit is based on the lowest cost of **equivalent coverage** for each of your qualified employees. See page 16 for a definition of qualified employee.

Use the following steps to calculate your maximum allowable claim for the PHSP premiums paid or payable for yourself, your spouse or common-law partner, and your household members.

For each of your qualified employees, do the following calculation:

$X \times Y = Z$, where:

- X equals the amount you would pay to provide yourself, your spouse or common-law partner, and your household members with coverage equivalent to that provided to a particular employee, his or her spouse or common-law partner and household members
- Y equals the percentage of the premium you pay for that particular employee
- Z equals your limit based on that particular employee

Example

You have one qualified employee. To provide yourself with coverage equivalent to his or hers, you pay a premium of \$1,800. You pay 60% of your employee's premium. Your deduction limit for yourself is \$1,080, calculated as follows:

$$\$1,800 (\text{amount X}) \times 60\% (\text{amount Y}) = \$1,080 (\text{amount Z})$$

The maximum you can claim is \$1,080, if you had only one qualified employee.

If you had more than one qualified employee, you have to do the $X \times Y = Z$ calculation for each employee. Your limit is then the least amount you calculate for each and every employee.

Example

You have three qualified employees, Jack, Jill, and Sue. The following table shows how much you would pay for coverage equivalent to each of theirs, and the percentage of each employee's premium that you pay.

Name of employee	Cost of equivalent coverage for yourself	% of the employee's premium you pay
Jack	\$1,500	20%
Jill	\$1,800	50%
Sue	\$1,400	40%

You have to do the following three calculations:

$$\text{Jack: } \$1,500 (X) \times 20\% (Y) = \$300 (Z)$$

$$\text{Jill: } \$1,800 (X) \times 50\% (Y) = \$900 (Z)$$

$$\text{Sue: } \$1,400 (X) \times 40\% (Y) = \$560 (Z)$$

Your limit is \$300, the least of the amounts calculated for the three employees.

Note

If you have a qualified employee with no coverage, you cannot claim your PHSP premiums as a deduction from self-employment income. You may, however, be able to claim them as medical expenses.

If you had employees throughout 2004 but the number of **arm's length** employees you insured was less than 50% of all of the insurable persons in your business, your

maximum allowable deduction is the **lesser** of the following two amounts:

Amount 1

Determine this amount by using the following formula:

$\frac{A}{365} \times (B + C)$, where:

- A is the number of days during the period of the year when you insured yourself and household members, if applicable, but insured less than 50% of your employees
- B equals $\$1,500 \times$ the number of household members 18 and over insured during that period
- C equals $\$750 \times$ the number of household members under 18 insured during that period

Amount 2

If you had at least one qualified employee, amount 2 is the lowest cost of equivalent coverage for each qualified employee, calculated by using the $X \times Y = Z$ formula on page 17. If you did not have at least one qualified employee, the limit in amount 1 will apply.

If you had employees for part of the year

For the part of the year when you had at least one qualified employee and your insurable arm's length employees represented at least 50% of all the insurable persons in your business, calculate your limit **for that period** the same way as in the previous section called "If you had employees throughout 2004."

For the remainder of the year when you had no employees or when your insurable arm's length employees represented less than 50% of all the insurable persons in your business, your deduction limit for that remaining period is the lesser of the following two amounts:

Amount 1

$\frac{A}{365} \times (B + C)$, where:

- A is the number of days during the period of the year when you insured yourself and household members, if applicable, but insured less than 50% of your employees
- B equals $\$1,500 \times$ the number of household members 18 and over insured during that period
- C equals $\$750 \times$ the number of household members under 18 insured during that period

Amount 2

If you had at least one qualified employee, amount 2 is the lowest cost of equivalent coverage for each qualified employee, calculated by using the $X \times Y = Z$ formula on page 17. If you did not have at least one qualified employee, the limit in amount 1 will apply.

Undeducted premiums

If you deduct only a part of your PHSP premium at line 9804 and you paid the premium in the year, you can include the undeducted balance in the calculation of your non-refundable medical expense tax credit. For details, see "Line 330" in your *General Income Tax and Benefit Guide*.

Line 9805 – Interest

Enter the interest you paid on money you borrowed to earn farming income, such as interest on a loan you used to buy a baler. Do not include the interest on money you borrowed to buy a motor vehicle used in your farming business. Include this amount on "Line 9819 – Motor vehicle expenses," as explained on page 19.

You can deduct interest you paid on any real estate mortgage you incurred to earn farming income, but you cannot deduct the principal part of loan or mortgage payments. Do not deduct interest on money you borrowed for personal purposes or to pay overdue income taxes.

You may be able to deduct interest expenses for a property that you used for farming business purposes, even if you have stopped using the property for such purposes because you are no longer in the farming business. For more information, call us at **1-800-959-5525**.

Line 9808 – Office expenses

Enter the amount of office expenses, such as stationery, invoices, receipt and accounting books, and any other office supplies.

Line 9809 – Legal and accounting fees

In most cases, you can deduct legal fees you incurred for your farming business. Also, you can deduct any accounting or bookkeeping fees you incurred to have someone keep your books and records, and prepare your income tax return and GST/HST returns.

If you paid accounting or legal fees to file an appeal against an assessment or decision under the *Income Tax Act*, the *Canada Pension Plan*, the *Quebec Pension Plan*, the *Employment Insurance Act*, or the *Unemployment Insurance Act*, do not deduct them here. Deduct these fees on line 232 of your income tax return. You should subtract any reimbursement from the applicable fees, and enter the result on line 232.

If you deducted these types of fees in a previous year and received a reimbursement in 2004, enter the amount of the reimbursement on line 130 of your income tax return.

Do not deduct any legal or other fees you incurred to buy property, such as land, buildings, and equipment. Add these fees to the adjusted cost base of the property if the property is used in your farming business.

For more details, see Interpretation Bulletin IT-99, *Legal and Accounting Fees*.

Line 9810 – Property taxes

Enter the amount of land, municipal, and realty taxes you paid for property used in your farming business. Since the municipal tax for the farmhouse is a personal expense, you cannot deduct it unless you meet the conditions we explain in "Line 9945 – Business-use-of-home expenses" on page 27.

If you are repaying a loan for land drainage through your property tax payments to your township, you cannot include the amount you repaid as part of your property tax expense.

Line 9811 – Rent (land, buildings, and pasture)

Enter the amount of rent expenses you paid for land, buildings, and pasture you used for your farming business.

If you farmed on a sharecrop basis and paid your landlord a share of the crop, you can do **one** of the following:

- Add to your income the fair market value of the crops you gave your landlord. Deduct the same amount as a rent expense (see page 28 for the definition of fair market value).
- Do not include the fair market value in income and do not deduct the amount as a rent expense.

Line 9814 – Salaries, wages, and benefits (including employer's contributions)

Enter the amount of gross salaries and wages you paid to your employees.

For line 9814, the terms, salaries and wages, are used interchangeably.

Include the cost of board for hired help. However, do not include the cost of board for dependants.

As the employer, also include in this total your share of the Canada Pension Plan or Quebec Pension Plan contributions and Employment Insurance premiums. Do not deduct the amounts you withheld from your employees' remuneration, since you already deducted them in the amount you claimed as wages.

Keep a detailed record of the amounts you paid to each employee and the employee's name, address, and social insurance number.

Do not deduct salaries or drawings paid or payable to yourself or to a partner. You can deduct the wages you paid to your child, as long as you meet **all** these conditions:

- you paid the wages by cheque, in cash or in kind;
- the work your child did was necessary for you to earn farming income;
- the wages were reasonable when you consider your child's age; and
- the amount you paid is what you would have paid someone else to do the same work.

Keep documents as proof of the wages you paid to your child. If you paid your child by cheque, keep the cancelled cheque. If you paid cash, have your child sign a receipt.

You may have paid wages in kind to your employees. For example, you may have paid your employees by giving them something you produced on the farm (such as grain or livestock) instead of cash.

If you did this:

- include the value of the items given to your employees in your gross sales for the year and deduct the same amount as a wage expense
- the employees would include the value of the items given in their income

You can also deduct wages you paid to your spouse or common-law partner, as long as you follow the same rules, and as long as that person is not a partner in your business. If you were a partner in a farm partnership that employed your spouse or common-law partner, the farm partnership can deduct that person's wages if it incurred the expense to earn farming income, and the wages were reasonable.

Line 9819 – Motor vehicle expenses (not including CCA)

Enter the amount of motor vehicle expenses, excluding the capital cost allowance (CCA). For details on CCA, see Chapter 3.

The kind of vehicle you own can affect the expenses you can deduct. For income tax purposes, there are three definitions of vehicles you should know about. They are:

- motor vehicles
- automobiles
- passenger vehicles

If you owned or leased a passenger vehicle, there may be a limit on the amounts you can deduct for CCA, interest, and leasing costs. We cover the CCA limits in Chapter 3. You will find the limits on interest and leasing costs later in this section.

A **motor vehicle** is an automotive vehicle for use on streets or highways.

An **automobile** is a motor vehicle that is designed or adapted mainly to carry passengers on streets and highways, and that seats no more than the driver and eight passengers. However, an automobile does not include:

- an ambulance
- a clearly marked police and fire emergency-response vehicle
- a motor vehicle you bought to use more than 50% as a taxi, a bus used in the business of transporting passengers, or a hearse in a funeral business
- a motor vehicle you bought to sell, rent, or lease in a motor vehicle sales, rental, or leasing business
- a motor vehicle (except a hearse) you bought to use in a funeral business to transport passengers
- a van, pick-up truck, or similar vehicle that seats no more than the driver and two passengers which, in the tax year you bought or leased it, was used more than 50% to transport goods or equipment to earn income
- a van, pick-up truck, or similar vehicle which, in the tax year you bought or leased it, was used 90% or more to transport goods, equipment, or passengers to earn income
- a pick-up truck that, in the tax year you bought or leased it, was used more than 50% to transport goods, equipment, or passengers while earning or producing income at a remote work location or at a special work site that is at least 30 kilometres from the nearest community having a population of at least 40,000 persons

A **passenger vehicle** is an automobile you bought after June 17, 1987. A passenger vehicle is also an automobile that you leased under a lease agreement you entered into, extended, or renewed after June 17, 1987.

Most cars, station wagons, vans, and some pick-up trucks are passenger vehicles. They are subject to the limits for CCA, interest, and leasing.

The following chart will help you determine if you have a motor vehicle, an automobile, or a passenger vehicle. The chart does not cover every situation, but it gives some of the main definitions for vehicles bought or leased and used to earn business income.

Vehicle definitions			
Type of vehicle	Seating (includes driver)	Business use in year bought or leased	Vehicle definition
Coupe, sedan, station wagon, sports car, or luxury car	1 to 9	1% to 100%	passenger
Pick-up truck used to transport goods or equipment	1 to 3	more than 50%	motor
Pick-up truck (other than above)	1 to 3	1% to 100%	passenger
Pick-up truck with extended cab used to transport goods, equipment, or passengers	4 to 9	90% or more	motor
Pick-up truck with extended cab (other than above)	4 to 9	1% to 100%	passenger
Sport-utility used to transport goods, equipment, or passengers	4 to 9	90% or more	motor
Sport-utility (other than above)	4 to 9	1% to 100%	passenger
Van or minivan used to transport goods or equipment	1 to 3	more than 50%	motor
Van or minivan (other than above)	1 to 3	1% to 100%	passenger
Van or minivan used to transport goods, equipment, or passengers	4 to 9	90% or more	motor
Van or minivan (other than above)	4 to 9	1% to 100%	passenger

Business use of a motor vehicle

If you used your motor vehicle for personal and business reasons, you can deduct the part of your expenses that was for farming-business use. Farming business use includes things such as trips to pick up parts and farm supplies, or to deliver grain. If you did not live on your farm, the travel between the farm and your home is not considered business travel.

Keep a record of the total kilometres you drive and the kilometres you drive for farming business use. Also, keep track of what it costs you to run and maintain the motor vehicle for your fiscal period.

Example

Murray’s farming business has a December 31 year-end. He owns a truck that is not a passenger vehicle. He uses the truck to pick up supplies and equipment. Murray kept the following records for his 2004 fiscal period:

Farming business kilometres..... 27,000 km
 Total kilometres 30,000 km

Expenses:

Gasoline and oil.....\$ 3,500
 Repairs and maintenance.....\$ 500
 Insurance.....\$ 1,000
 Interest (on loan to buy truck).....\$ 1,900
 Licence and registration fees\$ 100
 Total expenses for the truck.....\$ 7,000

This is how Murray determines the motor vehicle expenses he can deduct in his 2004 fiscal period:

$$\frac{27,000 \text{ (farming business kilometres)}}{30,000 \text{ (total kilometres)}} \times \$7,000 = \$6,300$$

Murray can deduct \$6,300 on line 9819 of Form T2042 as motor vehicle expenses for his 2004 fiscal period.

If you received insurance proceeds to help pay for repairs, see “Line 9604 – Insurance proceeds” on page 11 for more information.

Interest on the money you borrow for a passenger vehicle

When you used a passenger vehicle to earn farming business income, there is a limit on the amount of interest you can deduct.

Whether you use the cash or accrual method to determine your income, complete the following chart to calculate the interest you can deduct. If you used your passenger vehicle for both personal and farming business use, complete the chart before you determine how much interest you can deduct as an expense.

Interest chart

Total interest you paid
(cash method) or that is payable
(accrual method) in your fiscal year. \$ _____ **A**

\$10* x _____ number of days in
your fiscal year for
which interest was
paid or payable \$ _____ **B**

Your available interest expense is either
A or B, whichever amount is less \$ _____

* For passenger vehicles bought:

- from September 1, 1989, to December 31, 1996, and from 2001 to 2004, use \$10
- from 1997 to 2000, use \$8.33

Example

Heather's farming business has a December 31 year-end. On January 1, 2004, she bought a new passenger vehicle that she uses for both personal and business use. She borrowed money to buy the vehicle, and the interest she paid in her 2004 fiscal period was \$2,200. Since the car that Heather bought is a passenger vehicle, there is a limit on the interest she can deduct. Heather's available interest is either one of these two amounts, whichever is less:

- \$2,200 (the total interest she paid in her 2004 fiscal period); or
- \$3,650 (\$10 × 365 days).

Heather kept the following records for her 2004 fiscal period:

Farming business kilometres..... 20,000 km
Total kilometres 25,000 km

Expenses:

Gasoline and oil.....	\$2,000
Repairs and maintenance	\$1,000
Insurance	\$1,900
Interest (on loan to buy vehicle).....	\$2,200
Licence and registration.....	\$ 60
Total vehicle expenses.....	<u>\$7,160</u>

Here is how Heather determines the motor vehicle expenses she can deduct in her 2004 fiscal period:

$$\frac{20,000 \text{ (farming business kilometres)}}{25,000 \text{ (total kilometres)}} \times \$7,160 = \$5,728$$

Heather can deduct \$5,728 on line 9819 of Form T2042 as motor vehicle expenses for her 2004 fiscal period.

Leasing costs for a passenger vehicle

When you use a passenger vehicle to earn farming business income, there is a limit on the amount of the leasing costs you can deduct. To calculate your eligible leasing costs, complete the chart. "Eligible leasing costs for passenger vehicles" on page 22.

The lease agreement for your passenger vehicle may include items such as insurance, maintenance, and taxes. In this case, include them as part of the lease charges on line A when you complete the chart.

Note

Generally, leases include taxes such as GST and PST, or HST. Include them on line A. If you pay for items such as insurance and maintenance separately, do not include them in the amount on line A. Claim them separately on the appropriate lines on Form T2042.

Eligible leasing costs for passenger vehicles

Total lease charges incurred in your 2004 fiscal period for the vehicle	\$ _____ A
Total lease payments deducted before your 2004 fiscal period for the vehicle.....	\$ _____ B
Total number of days the vehicle was leased in your 2004 and previous fiscal periods	_____ C
Manufacturer's list price	\$ _____ D
The amount on line D or (\$35,294 + GST and PST, or HST on \$35,294), whichever is more \$ _____ × 85% =	\$ _____ E
$\frac{[(\$800 + \text{GST and PST, or HST on } \$800) \times \text{line C}] - \text{line B}}{30}$	\$ _____ F
$\frac{[(\$30,000 + \text{GST and PST, or HST on } \$30,000) \times \text{line A}]}{\text{line E}}$	\$ _____ G
Eligible leasing cost: Line F or line G, whichever is less	\$ _____

If you entered into a lease agreement for a passenger vehicle before January 1, 2001, make these changes to the chart:

Fiscal year you entered into lease agreement	After 1990 and before 1997	1997	1998 and 1999	2000
■ when calculating line E, replace \$35,294 with:	\$28,235	\$29,412	\$30,588	\$31,765
■ when calculating line F, replace \$800 with:	\$650	\$550	\$650	\$700
■ when calculating line G, replace \$30,000 with:	\$24,000	\$25,000	\$26,000	\$27,000

Repayments and imputed interest

When you lease a passenger vehicle, you may have a repayment owing to you, or you may have imputed interest. If this is the case, you will not be able to use the chart.

Imputed interest is interest that would be owing to you if interest were paid on the money you deposited to lease a passenger vehicle. Calculate imputed interest for leasing costs on a passenger vehicle only if **all** of the following apply:

- you made one or more deposits for the leased passenger vehicle;
- the deposit is, or the deposits are, refundable; and
- the total of the deposits is more than \$1,000.

For more information, see Interpretation Bulletin IT-521, *Motor Vehicle Expenses Claimed by Self-Employed Individuals*.

More than one vehicle

If you used more than one motor vehicle for your farming business, keep a separate record that shows the total kilometres and farming business kilometres you drove, and the cost to run and maintain each vehicle. Calculate each vehicle's expenses separately.

Joint ownership of a passenger vehicle

If you and someone else owned or leased the same passenger vehicle, the limits on CCA, interest, and leasing costs still apply. The amount you can deduct as joint

owners cannot be more than the amount one person owning or leasing the passenger vehicle could deduct. Each of you has to claim expenses in proportion to your share of the passenger vehicle. Your share is based on the part of the purchase price or lease costs that you paid.

For more details on motor vehicle expenses, see Interpretation Bulletin IT-521, *Motor Vehicle Expenses Claimed by Self-Employed Individuals*.

Line 9820 – Small tools

If a tool costs you less than \$200, deduct its full cost. If it costs you \$200 or more, add the cost to your CCA schedule as class 8 property. For details, see Chapter 3.

Line 9937 – Mandatory inventory adjustment included in 2003

If you included an amount for the mandatory inventory adjustment (MIA) on line 9942 in your 2003 fiscal period, deduct the amount as an expense in your 2004 fiscal period. Do not include the valuation of inventories if you are using the accrual method of accounting. For details about the accrual method, see "Reporting methods" on page 4.

For more details on MIA, see line 9942 on page 24.

Line 9938 – Optional inventory adjustment included in 2003

If you included an amount for the optional inventory adjustment (OIA) on line 9941 in your 2003 fiscal period,

deduct the amount as an expense in your 2004 fiscal period. Do not include the valuation of inventories if you are using the accrual method of accounting. For details about the accrual method, see "Reporting methods" on page 4.

For more details on OIA, see line 9941 on this page.

Line 9790 – Other expenses

You may have other expenses that are not specifically covered on Form T2042. We explain some of these other expenses in the following paragraphs. Deduct these other expenses on these lines.

You can pay some of your expenses by having them deducted from your cash grain tickets or grain stabilization payments. These expenses include seed, feed, sprays, or fertilizers. You can deduct these expenses if you include in your income the gross amount of the grain sale or stabilization payment.

Payment in kind

If you made a payment in kind for a farming business expense, include the fair market value of the good or service in income. Deduct the same amount as an expense. For more details, see the definition of payment in kind on page 12.

Leasing costs

Enter the expenses you incurred in your 2004 fiscal period for leasing property used to earn your farming income. If you lease a passenger vehicle, see "Line 9819 – Motor vehicle expenses" on page 19.

If you entered into a lease agreement after April 26, 1989, you can choose to treat your lease payments as combined payments of principal and interest. However, you and the person from whom you are leasing have to agree to treat the payments this way. In this case, we consider that:

- you have bought the property rather than leased it; and
- you have borrowed an amount equal to the fair market value of the leased property. We define fair market value on page 28.

You can deduct the interest part of the payment as an expense. You can also claim CCA on the property. For details on CCA, see Chapter 3.

You can make this choice as long as the property qualifies and the total fair market value (FMV) of all the property that is subject to the lease is more than \$25,000. For example, a combine that you lease with a FMV of \$35,000 qualifies. However, office furniture and automobiles often do not.

To make this choice regarding your lease, complete **one** of the following forms and file it with your income tax return for the year you make the lease agreement:

- Form T2145, *Election in Respect of the Leasing of Property*; or
- Form T2146, *Election in Respect of Assigned Leases or Subleased Property*.

Advertising

Deduct the cost of any advertising done for your farming business.

Telephone expenses

Do not deduct the basic monthly rate of your home telephone. However, you can deduct any long distance telephone calls you made on your home telephone for farming business.

If you have a separate telephone to use in your business and you use it for business calls only, you can deduct its basic monthly rate.

Memberships and subscriptions

Enter the amount of fees you incurred for memberships in farming organizations and for subscriptions to farming publications used in your farming activities.

Freight and trucking

Deduct the expenses you incurred for delivery, shipping, trucking, or other distribution costs related to your farming business.

Line 9935 – Allowance on eligible capital property

We explain how to determine this allowance in Chapter 4.

Line 9936 – Capital cost allowance

Enter the amount of capital cost allowance (CCA) you calculate on the charts found on pages 2 and 3 of Form T2042. For details on how to complete these charts, see Chapter 3.

Line 9898 – Total farm expenses

Enter the total of lines 9790, 9935, and 9936. Enter the business part only.

Line 9899 – Net income (loss) before adjustments

Enter the gross income minus the total farm expenses. If you are a partner in a partnership, this amount is the net farming business income of all partners. If you have a loss, enter the amount in brackets.

Line 9941 – Optional inventory adjustment included in 2004

If you want to include an inventory amount in income, read this section. By making the optional inventory adjustment (OIA), you can include in your income an amount up to the fair market value of your inventory minus the mandatory inventory adjustment (MIA). You can only make the OIA if you use the cash method. For the definitions of inventory and fair market value, see "Line 9942" on page 24.

For the OIA, unlike for the MIA, the inventory does **not** have to be purchased inventory. It is all the inventory you still have at the end of your 2004 fiscal period.

Enter the amount of your OIA on line 9941. You must deduct this amount as an expense in your next fiscal period.

Line 9942 – Mandatory inventory adjustment included in 2004

The mandatory inventory adjustment (MIA) decreases your net loss if you held inventory at the end of your fiscal period. Read this section, even if you do not have to make the MIA. This section will show you how to determine the value of the farm inventory you bought and still have at the end of your 2004 fiscal period. You will need to know this value if you have to make the MIA this year or in the future.

You have to make the MIA if **all** of the following apply:

- you use the cash method to report your income;
- you have a net loss on line 9899 of Form T2042; and
- you bought inventory and still have it at the end of your 2004 fiscal period. This does not refer only to inventory that you bought in 2004. It includes inventory that you had previously bought and still owned at the end of your 2004 fiscal period.

Your MIA is one of these two amounts, whichever is less:

- the net loss before adjustments on line 9899; or
- the value of the purchased inventory you still have at the end of your 2004 fiscal period.

To calculate your MIA, complete charts 1, 2, 3, and 4 on page 51. Once you have completed chart 4, enter the amount on line 9942. For more information, see Interpretation Bulletin IT-526, *Farming – Cash Method Inventory Adjustments*.

In your 2005 fiscal period, deduct the MIA you added to your net loss in your 2004 fiscal period.

Note

If you bought a specified animal (as defined below) in a non-arm's length transaction, we consider that you bought the animal in the same year and at the same price for which the seller bought it. A non-arm's length transaction is, for example, a transaction between members of a family, such as a husband and wife, or a parent and child. See page 28 for the definition of non-arm's length transaction.

Definitions

To value your inventory, you need to know the meaning of the following terms.

Inventory is a group of items that a business holds and intends to consume or sell to its customers.

Farm inventory is tangible property that is:

- held for sale, such as harvested grain;
- used in the production of saleable goods, such as seed and feed; or
- in the process of being produced, such as standing crops, or feeder livestock.

Seed that you have already planted, and fertilizer or chemicals that you have already applied, are no longer part of your inventory items, but are included in the value of the standing crop that may be included in the Optional Inventory Adjustment (OIA).

Purchased inventory is inventory you have bought and paid for.

Specified animals are horses. You may also choose to designate cattle you registered under the *Animal Pedigree Act* as specified animals. To make this choice, put a note on your income tax return saying you want to designate the animal this way. If you indicate on your return that it is a specified animal, we will continue to consider it as such until you sell it.

Cash cost is the amount you paid to buy your inventory.

Fair market value (FMV) is generally the highest dollar value you can get for your property in an open and unrestricted market between an informed and willing buyer and an informed and willing seller, who are dealing with each other at arm's length. We define non-arm's length transaction on page 28.

Valuing your purchased inventory

To value your purchased inventory, read the text that follows and the example of how to complete the MIA charts. On page 51 of this guide, there are blank charts for you to use. Keep these charts as part of your records. Except for specified animals, you have to value any purchased inventory you bought before or during your 2004 fiscal period at one of the two following amounts, whichever is less:

- the cash cost; or
- the fair market value.

To determine which amount is less, separately compare each item or group of items in the inventory.

Value, at one of the following amounts, the specified animals you bought **in** your 2004 fiscal period and still have at the end of this period:

- the cash cost;
- 70% of the cash cost; or
- any amount between these two amounts.

Value, at one of the following amounts, the specified animals you bought **before** your 2004 fiscal period and still have at the end of this period:

- the cash cost;
- 70% of:
 - the value of the specified animals for MIA purposes as determined at the end of your 2003 fiscal period; **plus**
 - any amounts you paid in your 2004 fiscal period toward the purchase price; or
- any amount between these two amounts.

Example

Doug started his farming business in 1994 and uses the cash method to report his income. His year-end is December 31. Doug shows a net loss of \$55,000 in 2004 on line 9899. Doug has purchased inventory at the end of his 2004 fiscal period. This means he has to decrease his net loss by the MIA. Doug made a chart for the cash cost of his livestock that is purchased inventory at the end of his 2004 fiscal period.

Livestock

Year of purchase	Cost of purchase	Amount Doug paid by the end of his 2004 fiscal period
2004	\$30,000	\$25,000
2003	\$26,000	\$26,000*
2002	\$22,000	\$22,000
2001	\$20,000	\$20,000

* For livestock bought in his 2003 fiscal period, Doug paid \$19,000 in 2003, and \$7,000 in 2004.

Doug's other inventory is fertilizer, seed, and fuel. The cash cost is the same as the fair market value for this inventory. Its value is as follows:

- bought in his 2004 fiscal period: \$ 15,000
- bought in his 2003 fiscal period: \$ 6,000
- bought in his 2002 fiscal period: \$ 5,000

At the end of his 2004 fiscal period, Doug did not have any other inventory that he bought before his 2002 fiscal period. Doug has registered his livestock under the *Animal Pedigree Act*. He wants to designate these animals as specified animals. Doug completes chart 1 as follows:

Chart 1 Cash cost of purchased inventory		
Doug enters the amount he paid by the end of his 2004 fiscal period for the specified animals he bought:		
Fiscal period	Cash cost	
■ in his 2004 fiscal period	\$ <u>25,000</u>	A
■ in his 2003 fiscal period	\$ <u>26,000</u>	B
■ in his 2002 fiscal period	\$ <u>22,000</u>	C
■ in his 2001 fiscal period	\$ <u>20,000</u>	D
■ before his 2001 fiscal period	\$ <u> 0</u>	E
Doug enters the amount he paid by the end of his 2004 fiscal period for all other inventory he bought:		
■ in his 2004 fiscal period	\$ <u>15,000</u>	F
■ in his 2003 fiscal period	\$ <u>6,000</u>	G
■ in his 2002 fiscal period	\$ <u>5,000</u>	H
■ in his 2001 fiscal period	\$ <u> 0</u>	I
■ before his 2001 fiscal period	\$ <u> 0</u>	J

Doug now knows the cash cost of his purchased inventory, including his specified animals. He uses these amounts to calculate the value of his purchased inventory at the end of his 2004 fiscal period. To do this, he completes charts 2, 3, and 4 as follows:

Chart 2 Value of purchased inventory for specified animals		
The small letters in front of each line match the paragraphs at the end of this chart. These paragraphs explain how Doug calculates the number on each line.		
Inventory bought in his 2004 fiscal period		
Doug enters an amount that is not more than the amount on line A, but not less than 70% of this amount.	a) \$ <u>20,000</u>	K
Inventory bought in his 2003 fiscal period		
Doug enters an amount that is not more than the amount on line B, but not less than 70% of the total of the value at the end of his 2003 fiscal period, plus any amounts he paid in his 2004 fiscal period toward the purchase price.	b) \$ <u>14,210</u>	L
Inventory bought in his 2002 fiscal period		
Doug enters an amount that is not more than the amount on line C, but not less than 70% of the total of the value at the end of his 2003 fiscal period, plus any amounts he paid in his 2004 fiscal period toward the purchase price.	c) \$ <u>7,546</u>	M
Inventory bought in his 2001 fiscal period		
Doug enters an amount that is not more than the amount on line D, but not less than 70% of the total of the value at the end of his 2003 fiscal period, plus any amounts he paid in his 2004 fiscal period toward the purchase price.	d) \$ <u>4,802</u>	N
Inventory bought before his 2001 fiscal period		
	e) \$ <u> 0</u>	O

- a) Doug chose \$20,000, which is between the cash cost of \$25,000 and \$17,500 (70% of the cash cost).
- b) Doug chose to value the inventory he bought in his 2003 fiscal period at 70% of the cash cost. Therefore, the value of this inventory at the end of his 2003 fiscal period was \$13,300 (\$19,000 × 70%). Remember, Doug paid \$19,000 for these specified animals in 2003. He paid \$7,000 in 2004.

For his 2004 fiscal period, Doug chose to value the inventory he bought in his 2003 fiscal period at 70% of the total of the value at the end of the 2003 fiscal period plus any amounts he paid in his 2004 fiscal period toward the purchase price. Therefore, the amount he enters on line L is \$14,210 [70% × (\$13,300 + \$7,000)]. He could choose any amount between the cash cost of \$26,000 and the lowest acceptable inventory value of \$14,210.

- c) Doug chose to value the inventory he bought in his 2002 fiscal period at 70% of the cash cost. Therefore, the value of this inventory at the end of his 2002 fiscal period was \$15,400 (\$22,000 × 70%).

For his 2003 fiscal period, Doug chose to value the inventory he bought in his 2002 fiscal period at 70% of the total of the value at the end of his 2002 fiscal period. Therefore, the value of this inventory at the end of his 2003 fiscal period was \$10,780 (\$15,400 × 70%).

For his 2004 fiscal period, Doug chose to value the inventory he bought in his 2002 fiscal period at 70% of the total of the value at the end of his 2003 fiscal period. Therefore, the amount he enters on line M is \$7,546 ($\$10,780 \times 70\%$). He could choose any amount between the cash cost of \$22,000 and the lowest acceptable inventory value of \$7,546.

- d) Doug chose to value the inventory he bought in his 2001 fiscal period at 70% of the cash cost. Therefore, the value of this inventory at the end of his 2001 fiscal period was \$14,000 ($\$20,000 \times 70\%$).

For his 2002 fiscal period, Doug chose to value the inventory he bought in his 2001 fiscal period at 70% of the total of the value at the end of his 2001 fiscal period. Therefore, the value of this inventory at the end of his 2002 fiscal period was \$9,800 ($\$14,000 \times 70\%$).

For his 2003 fiscal period, Doug chose to value the inventory he bought in his 2001 fiscal period at 70% of the total of the value at the end of his 2002 fiscal period. Therefore, the value of this inventory at the end of his 2003 fiscal period was \$6,860 ($\$9,800 \times 70\%$).

For his 2004 fiscal period, Doug chose to value the inventory he bought in his 2001 fiscal period at 70% of the total of the value at the end of his 2003 fiscal period. Therefore, the amount he enters on line N is \$4,802 ($\$6,860 \times 70\%$). He could choose any amount between the cash cost of \$20,000 and the lowest acceptable inventory value of \$4,802.

- e) Doug had not purchased any specified animals before his 2001 fiscal period.

Chart 3	
Value of purchased inventory for all other inventory	
Inventory bought in his 2004 fiscal period: Doug enters the amount on line F or the fair market value, whichever is less.	<u>\$15,000</u> P
Inventory bought in his 2003 fiscal period: Doug enters the amount on line G or the fair market value, whichever is less.	<u>6,000</u> Q
Inventory bought in his 2002 fiscal period: Doug enters the amount on line H or the fair market value, whichever is less.	<u>5,000</u> R
Inventory bought in his 2001 fiscal period: Doug enters the amount on line I or the fair market value, whichever is less.	<u>0</u> S
Inventory bought before his 2001 fiscal period: Doug enters the amount on line J or the fair market value, whichever is less.	<u>0</u> T

Chart 4 Calculation of MIA

Doug enters the amount of his net loss from line 9899 of Form T2042.	<u>\$ 55,000</u>	U
Doug enters the value of his inventory from charts 2 and 3:		
■ the amount on line K	<u>\$ 20,000</u>	
■ the amount on line L	<u>14,210</u>	
■ the amount on line M	<u>7,546</u>	
■ the amount on line N	<u>4,802</u>	
■ the amount on line O	<u>0</u>	
■ the amount on line P	<u>15,000</u>	
■ the amount on line Q	<u>6,000</u>	
■ the amount on line R	<u>5,000</u>	
■ the amount on line S	<u>0</u>	
■ the amount on line T	<u>0</u>	
Total value of inventory	<u>\$ 72,558</u>	<u>\$ 72,558</u> V
MIA – Doug enters the amount on line U or line V, whichever is less.	<u>\$ 55,000</u>	W

The MIA that Doug uses for his 2004 fiscal period will be the same amount he deducts from his farming income when he calculates his income for his next fiscal period.

Enter the figure from line W of chart 4 on line 9942 of Form T2042.

Your share of line c

Enter your share of the total of line 9899, line 9941, and line 9942 of Form T2042. This is the amount left after you subtract the amounts the other partners are responsible for reporting. On the chart "Details of other partners" on page 4 of Form T2042, show the full names and addresses of the other partners, as well as a breakdown of their shares of the income and their percentages of the partnership.

Line 9943 – Other amounts deductible from your share of net partnership income (loss)

Use the chart "Other amounts deductible from your share of net partnership income (loss)" on page 4 of Form T2042. Claim extra expenses you incurred to earn your share of the partnership income, such as the farming business part of allowable motor vehicle expenses, including CCA. Claim these amounts only if the partnership did not repay you for them. You can also claim any other deductible amounts. The limits discussed in this chapter also apply to these expenses. You must not have claimed these expenses anywhere else on Form T2042.

You can also use this chart to claim a business income reduction if you are a partner in a partnership that sold eligible capital property and you filed a capital gains election in 1994 relating to your partnership interest. For more information, see the *Business and Professional Income* guide.

Line 9945 – Business-use-of-home expenses

You can deduct expenses for the farming business use of a work space in your home, as long as you meet **one** of these conditions:

- the work space is your principal place of business; or
- you use the space only to earn your farming business income, and you use it on a regular and ongoing basis to meet your clients or customers.

You can deduct part of your maintenance costs, such as heating, home insurance, electricity, and cleaning materials. You can also deduct part of your property taxes, mortgage interest, and capital cost allowance. To calculate the part you can deduct, use a reasonable basis, such as the area of the work space divided by the total area.

The capital gain and recapture rules will apply if you deduct capital cost allowance on the business-use part of your home and you later sell your home. For more information about these rules, see chapters 3 and 6.

If you rent your home, you can deduct the part of the rent and any expenses you incur that relate to the work space.

The amount you can deduct for business-use-of-home expenses cannot be more than your net income from the farming business before you deduct these expenses. In other words, you cannot use these expenses to increase or create a business loss.

You can deduct whichever of the following amounts is **less**:

- any amount you carry forward from your 2003 fiscal period, plus the business-use-of-home expenses you incur in your 2004 fiscal period; or
- the income amount on line f of Form T2042.

In a future year, you can use any expense you could not deduct in your 2004 fiscal period, as long as you meet one of the previous two conditions. The same rules apply.

You can use the chart “Calculation of business-use-of-home expenses” on page 4 of Form T2042 to calculate your allowable claim for business-use-of-home expenses.

Note

If you are claiming CCA for the business use of a work space in your home, you have to deduct it on the chart “Calculation of business-use-of-home expenses” on page 4 of Form T2042. Subtract the CCA calculated for business-use-of-home expenses from the total CCA claimed in Area E before entering your claim on line 9936, “Capital cost allowance” on page 2 of Form T2042.

For more details, see Interpretation Bulletin IT-514, *Work Space in Home Expenses*.

Line 9946 – Your net income (loss)

Enter your net farming income or loss on this line, and also on line 141 of your income tax return. If you have a loss, enter the amount in brackets. For more information about losses, see Chapter 5.

Note

You may have to adjust the figure from line 9946 before entering it on your income tax return. You may have filed Form T1139, *Reconciliation of 2003 Business Income for Tax Purposes*, with your 2003 tax return. If so, you will probably have to complete the same form for 2004. To find out if you have to file Form T1139, and calculate the amount of farming income to report on your 2004 income tax return, see the *Reconciliation of Business Income for Tax Purposes* guide. The guide includes Form T1139.

Details of equity (chart on page 4 of Form T2042)

Line 9931 – Total business liabilities

A liability is a debt or an obligation of a business. Total business liabilities are the total of all amounts your farming business owes at the end of its fiscal period. This includes accounts payable, notes payable, taxes payable, unpaid salaries, wages and benefits, interest payable, deferred or unearned revenues, loans payable, mortgages payable, or any other outstanding balance.

Line 9932 – Drawings in 2004

A drawing is any withdrawal of cash or other assets and services of a business by the proprietor or partners. This includes transactions by the proprietor or partners (or family members), such as withdrawing cash for non-business use, and using business assets and services for personal use.

Line 9933 – Capital contributions in 2004

A capital contribution is an addition of cash or other assets that you made to the farming business during its fiscal period. This includes adding personal funds to the business account, paying business debts with personal funds, and transferring personal assets to the farming business.

Details of other partners (chart on page 4 of Form T2042)

If you are a partner in a partnership that does **not** have to file a partnership information return (see Chapter 1 for these requirements), complete the chart, “Details of other partners,” on Form T2042. If you are a partner in a partnership that **does** have to file a partnership information return, you do not need to complete the chart.

Chapter 3 – Capital Cost Allowance (CCA)

What is CCA?

You might acquire a depreciable property, such as a building, machinery, or equipment, to use in your farming business. You cannot deduct the cost of the property when you calculate your net farming income for the year.

However, because these properties may wear out or become outdated over time, you can deduct their cost over a period of several years. The deduction for this is called capital cost allowance (CCA).

Definitions

To calculate your CCA claim, you will need to know the meaning of the following terms.

Available for use

You can claim CCA on a depreciable property only when it becomes available for use.

Property, other than a building, generally becomes available for use on the earliest of the following dates:

- the date you first use the property to earn income;
- the second tax year after the year you acquire the property;
- the time just before you dispose of the property; or
- the date the property is delivered or made available to you and is capable of producing a saleable product or service, or of performing the function for which you acquired it.

Example

If you buy a tractor and the seller delivers it to you in 2004, but it is not in working order until 2005, you cannot claim CCA on it until 2005. However, if you buy a tractor and the seller delivers it to you in working order in 2004, but you did not use it until 2005, you can still claim CCA in 2004 because it was available for use.

A building, or part of a building, usually becomes available for use on the earliest of the following dates:

- the date you start using 90% or more of the building for the purpose you acquired it;
- the date the construction is completed;
- the second tax year after the year you acquire the building; or
- the time just before you dispose of the building.

We consider any **construction, renovation, or alteration** to a particular building to be a separate building for the purposes of applying the available-for-use rules.

Capital cost

This is the amount on which you first claim CCA. The capital cost of a depreciable property is generally the total of:

- the purchase price not including the cost of land, which is not depreciable (see “Land” on page 30);
- the part of your legal, accounting, engineering, installation, and other fees that relates to the purchase or construction of the depreciable property (not including the part that applies to land);

- the cost of any additions or improvements you made to the depreciable property after you acquired it, provided you have not claimed these costs as a current expense; and
- soft costs (such as interest, legal and accounting fees, and property taxes) related to the period you are constructing, renovating, or altering the building provided you have not claimed these costs as a current expense.

Depreciable property

This is any property on which you can claim CCA. You usually group depreciable properties into classes. For example, diggers, drills, and tools that cost \$200 or more belong to class 8. You have to base your CCA claim on a rate assigned to each class of property.

See “Classes of depreciable property” on page 32 for the most common classes of depreciable property you could use in your farming operation, and “Capital Cost Allowance (CCA) Rates” on page 50.

Fair market value (FMV)

Fair market value is generally the highest dollar value that you can get for your farm property in an open and unrestricted market between an informed and willing buyer and an informed and willing seller who are dealing at arm’s length with each other.

Non-arm’s length transaction

A non-arm’s length transaction includes a transaction between parties who are related, such as members of a family. An example of a non-arm’s length transaction would be the sale of property between a husband and wife, or a parent and child. For more details on non-arm’s length transactions, see Interpretation Bulletin IT-419, *Meaning of Arm’s Length*.

Proceeds of disposition

Your proceeds of disposition are usually the amount you receive, or that we consider you to have received, when you dispose of your depreciable property. This could include compensation you receive for depreciable property that someone destroys, expropriates, steals, or damages. For more details about proceeds of disposition, see Interpretation Bulletin IT-220, *Capital Cost Allowance – Proceeds of Disposition of Depreciable Property*, and its Special Release, and Interpretation Bulletin IT-285, *Capital Cost Allowance – General Comments*.

Undepreciated capital cost (UCC)

The UCC is generally the amount left after you deduct CCA from the capital cost of a depreciable property. The CCA you claim each year reduces the UCC of the property each year.

How much CCA can you claim?

Base your CCA claim on your fiscal period, not on the calendar year. The amount of CCA you can claim depends on the type of property you own, and the date you acquired it. You group the depreciable property you own into

classes. A different rate of CCA applies to each class. We explain the most common classes of depreciable property in “Classes of depreciable property” on page 32. We list most of the classes of depreciable property and the rates for each class in “Capital Cost Allowance (CCA) Rates” on page 50.

Guidelines for claiming CCA

- In most cases, CCA is calculated using the declining balance method. This means that you claim CCA on the capital cost of the property minus the CCA, if any, you claimed in previous years. The remaining balance declines over the years as you claim CCA.
- You do not have to claim the maximum amount of CCA in any given year. You can claim any amount you like, from zero to the maximum allowed for the year. For example, if you do not have to pay income tax for the year, you may not want to claim CCA. Claiming CCA reduces the balance of the class by the amount of CCA claimed. As a result, the available CCA for future years will be reduced.
- In the year you acquire a depreciable property, you normally can claim CCA only on one-half of your net additions to a class. We explain this 50% rule in “Column 6 – Adjustment for current-year additions” on page 31. The available-for-use rules may also affect the amount of CCA you can claim. See the definition of available for use on page 28.
- You cannot claim CCA on most land or on living things such as trees, shrubs, or animals. However, you can claim CCA on timber limits, cutting rights, and wood assets. For more details, see Interpretation Bulletin IT-481, *Timber Resource Property and Timber Limits*.
- If you receive income from a quarry, sand, or gravel pit, or a woodlot, you can claim a type of allowance known as a depletion allowance. For more details, see Interpretation Bulletins IT-373, *Farm Woodlots and Tree Farms*, and its Special Release, and IT-492, *Capital Cost Allowance – Industrial Mineral Mines*.
- If you claim CCA and you later dispose of the property, you may have to add an amount to your income as a recapture of CCA. Alternatively, you may be able to deduct an additional amount from your income as a terminal loss. For more information, see “Column 5 – UCC after additions and dispositions” on page 31.
- If you used depreciable property in 2004 that you used in your farming business before January 1, 1972, complete “Area E – Part XVII properties” on Form T2042.
- If you are a partner in a partnership that provides you with a T5013 slip, *Statement of Partnership Income*, you cannot personally claim CCA for property owned by the partnership. The T5013 slip you receive will have already allocated to you a share of the partnership’s CCA on the depreciable farm property.

You were asking?

- Q. If I start a farming business on June 1, 2004, how do I determine my CCA claim to December 31, 2004?

- A. Since the period is shorter than 365 days, you have to prorate your CCA claim. Calculate your CCA using the rules we discuss in this chapter. However, base your CCA claim on the number of days in your fiscal period compared to 365 days.

In your case, your fiscal period is 214 days. Suppose you calculate your CCA to be \$3,500. The amount of CCA you can claim is \$2,052 ($\$3,500 \times 214/365$).

How do you make your claim?

Use Area E on page 3 of Form T2042 to calculate your CCA deduction for your 2004 fiscal period.

If you acquired or disposed of buildings or equipment during the year, you will need to complete areas A, B, C, or D (whichever applies) before you complete Area E.

Even if you are not claiming a deduction for CCA for your 2004 fiscal period, you should complete these areas to show any additions or disposals during the year. They are located on pages 2 and 3 of Form T2042. For details on how to complete all these areas, see the following sections.

Column 1 – Class number

If this is the first year you are claiming CCA, read “Classes of depreciable property” on page 32, for the most common classes of depreciable properties you can use in your farming operation, and “Capital Cost Allowance (CCA) Rates” on page 50.

If you claimed CCA last year, you can get the class numbers from last year’s Form T2042.

Generally, if you own several properties in the same class, you combine the capital cost of all these properties in one class. You then enter the total in Area E.

Column 2 – Undepreciated capital cost (UCC) at the start of the year

If this is the first year you are claiming CCA, skip this column.

Otherwise, enter the UCC for each class at the end of last year in this column. If you completed Area E on Form T2042 last year, you will find these amounts in column 10.

You may have received a GST/HST input tax credit in 2003 for a passenger vehicle you used less than 90% of the time in your business. In this case, subtract the amount of the credit from the beginning UCC for your 2004 fiscal period. For more information, see “Grants, subsidies, and rebates” on page 35.

Subtract any investment tax credit you claimed or were refunded in 2003 from your UCC at the start of your 2004 fiscal period. Also, subtract any 2003 investment tax credit you carried back to a year before 2003.

Note

In 2004, you may be claiming, carrying back, or getting a refund of an investment tax credit. If you still have depreciable property in the class, you have to adjust the UCC of the class to which the property belongs in 2005. To do this, subtract the amount of the credit

from the UCC at the beginning of 2005. When there is no property left in the class, report the amount of the investment tax credit as income in 2005.

Column 3 – Cost of additions in the year

If you acquire or make improvements to depreciable property in the year, we generally consider the improvements to be additions to the class in which the property belongs. See “Class 3 (5%)” on page 32 for an exception to this rule. Enter the details of your 2004 additions on Form T2042 as explained below:

- complete Area A and Area B (whichever applies) on Form T2042; and
- for each class, enter in column 3 of Area E the corresponding amount from column 5 of Area A and Area B.

When completing Area A and Area B (see below) in the column called “Personal part,” enter the part of the property that you use personally, separate from the part you use for business. For example, if you use 25% of the building in which you live for your farming business, your personal part is the other 75%.

Do not include the value of your own labour in the cost of a property you build or improve. Include the cost of surveying or valuing a property you acquire in the capital cost of the property. Remember that a property usually has to be available for use before you can claim CCA. See the definition of available for use on page 28.

Note

If you received insurance proceeds to reimburse you for the **loss** or **destruction** of depreciable property, enter the amount you spent to **replace** the property in column 3 of Area E, and also in Area A or B, whichever applies. Include the amount of insurance proceeds as proceeds of disposition in column 4 of Area E and also in column 3 of Area C or D, whichever applies. For more information, see “Line 9604 – Insurance proceeds” on page 11.

If you replaced a lost or destroyed property within a year of the loss, special rules for replacement property may apply. See Interpretation Bulletin IT-259, *Exchanges of Property*, and Interpretation Bulletin IT-491, *Former Business Property*, and its Special Release.

You should also see “Special situations” on page 34 to see if any of the situations apply to you.

Area A – Details of equipment additions in the year

List the details of all equipment, machinery, or motor vehicles you acquired or improved in 2004. Group the equipment into the applicable classes, and put each class on a separate line. **Enter on line 9925** the total business part of the cost of the equipment.

Area B – Details of building additions in the year

List the details of all buildings you acquired or improved in 2004. Group the buildings into the applicable classes, and put each class on a separate line.

Enter on line 9927 the total business part of the cost of the buildings. The cost includes the purchase price of the

building, plus any related expenses that you should add to the capital cost of the building, such as legal fees, land transfer taxes, and mortgage fees.

Land

Land is not depreciable property. Therefore, you cannot claim CCA on its cost. If you acquire a farm property that includes both land and a building, enter in column 3 of Area B only the cost of the building. To work out the building’s capital cost, you have to split any fees that relate to the purchase of the property between the land and the building. Related fees may include legal and accounting fees.

Calculate the part of the related fees you can include in the capital cost of the building as follows:

<u>building value</u>	legal,	the part of the fees
total purchase price	× accounting, or	= you can include in
	other fees	the building’s cost

You do not have to split a fee if it relates specifically to the land or the building. In this case, you would add the amount of the fee to the cost to which it relates, either the land or the building.

Area F – Details of land additions and dispositions in the year

Enter on line 9923 the total cost of acquiring land in 2004. The cost includes the purchase price of the land, plus any related expenses that you should add to the capital cost of the land, such as legal fees, land transfer taxes, and mortgage fees.

You cannot claim CCA on land. Do **not** enter this amount in column 3 of Area E.

Area G – Details of quota additions and dispositions in the year

Enter on line 9929 the total cost of acquiring quotas in 2004.

Column 4 – Proceeds of disposition in the year

If you disposed of a depreciable property during your 2004 fiscal period:

- complete Area C and Area D on Form T2042, if they apply; and
- for each class, enter in column 4 of Area E the corresponding amount from column 5 of Area C and Area D.

When completing Area C and Area D, enter in column 3 one of the following amounts, whichever is less:

- your proceeds of disposition (see the definition on page 28) minus any related expenses; or
- the capital cost of your depreciable property.

Note

If you received insurance proceeds to reimburse you for the **loss** or **destruction** of depreciable property, enter the amount you received as proceeds of disposition in column 4 of Area E and in column 3 of Area C or D, whichever applies. Enter the amount you spent to **replace** the property in column 3 of Area E, and in Area

A or B, whichever applies. For more information, see “Line 9604 – Insurance proceeds” on page 11.

If you replaced a lost or destroyed property within a year of the loss, special rules for replacement property may apply. See Interpretation Bulletin IT-259, *Exchanges of Property*, and Interpretation Bulletin IT-491, *Former Business Property*, and its Special Release.

Special rules may apply if you dispose of a building for less than both its undepreciated capital cost and your capital cost. If this is the case, see “Special rules for disposing of a building in the year” on page 36 for details.

If you dispose of a depreciable property for more than its cost, you will have a capital gain. For details on capital gains, see Chapter 6. You cannot have a capital loss when you sell depreciable property. However, you may have a terminal loss. See “Column 5 – UCC after additions and dispositions” on this page for an explanation of terminal losses.

If you need more details, see Interpretation Bulletin IT-220, *Capital Cost Allowance – Proceeds of Disposition of Depreciable Property*, and its Special Release.

Note

When completing Area C and Area D (see below), in the column called “Personal part,” enter the part of the property that you use personally, separately from the part you use for business. For example, if you use 25% of the building in which you live for your farming business, your personal part is the other 75%.

Area C – Details of equipment dispositions in the year

In this area, list the details of all equipment, machinery, or motor vehicles you disposed of in 2004. Group the properties into the applicable classes, and put each class on a separate line. **Enter on line 9926** the total business part of the proceeds of disposition of the equipment, machinery, and motor vehicles.

Area D – Details of building dispositions in the year

In this area, list the details of all buildings you disposed of in 2004. Group the buildings into the applicable classes, and put each class on a separate line. **Enter on line 9928** the total business part of the proceeds of disposition of the buildings.

Area F – Details of land additions and dispositions in the year

Enter on line 9924 the total of all amounts you received or will receive for disposing of land in the year.

Area G – Details of quota additions and dispositions in the year

Enter on line 9930 the total of all amounts you received or will receive for disposing of quotas in the year.

Column 5 – UCC after additions and dispositions

You cannot claim CCA when the amount in column 5 is:

- **negative** (see “Recapture of CCA” below); or

- **positive**, and you do not have any property left in that class at the end of your 2004 fiscal period (see “Terminal loss” below).

In either case, enter “0” in column 10.

Recapture of CCA

If the amount in column 5 is negative, you have a recapture of CCA. Include your recapture on line 9600, “Other income.” A recapture of CCA can occur, for example, when you get a government grant or claim an investment tax credit. It can also happen if the proceeds from the sale of depreciable property are more than the total of:

- the UCC of the class at the beginning of the year; and
- the capital cost of any new additions during the year.

In some cases, you may be able to postpone a recapture of CCA. For example, you may sell a property and replace it with a similar one, someone may expropriate your property, or you may transfer property to a corporation, a partnership, or your child.

Terminal loss

If the amount in column 5 is positive and you no longer own any property in that class, you may have a terminal loss. More precisely, you may have a terminal loss when, at the end of your fiscal period, you have no more property in the class but you still have an amount that you have not deducted as CCA. You can usually subtract this terminal loss from your gross farming income in the fiscal period you disposed of the depreciable property. Include your terminal loss on line 9790, “Other expenses.”

For more information on recapture of CCA and terminal loss, see Interpretation Bulletin IT-478, *Capital Cost Allowance – Recapture and Terminal Loss*.

Note

The rules for recapture of CCA and terminal loss do not apply to passenger vehicles in class 10.1. However, see the comments in “Column 7 – Base amount for CCA,” on page 32, to calculate your CCA claim.

Column 6 – Adjustment for current-year additions

In the year you acquire or make additions to a depreciable property, you can usually claim CCA on only one half of your net additions (the amount in column 3 minus the amount in column 4). We call this the **50% rule**.

Calculate your CCA claim only on the net adjusted amount. Do not reduce the cost of the additions in column 3, or the CCA rate in column 8. For example, if you acquired a property in 2004 for \$30,000, you would base your CCA claim on \$15,000 ($\$30,000 \times 50\%$).

If you acquired and disposed of depreciable property of the same class in 2004, the calculation in column 6 restricts your CCA claim. Calculate the CCA you can claim as follows:

- Determine which of the following amounts is less:
 - the proceeds of disposition of your property, **minus** any related costs or expenses; or
 - the capital cost.
- Subtract the above amount from the capital cost of your addition.
- In column 6, enter 50% of the result. If the result is negative, enter “0.”

In some cases, you do not make an adjustment in column 6. For example, in a non-arm’s length transaction, you may buy depreciable property that the seller continuously owned from the day that is at least 364 days before the end of your 2004 fiscal period to the day the property was purchased. However, if you transfer personal property, such as a car or a personal computer into your business, the 50% rule applies to the particular property transferred.

Also, some properties are not subject to the 50% rule. Some examples are properties in classes 13, 14, 23, 24, 27, 29, and 34, as well as some of those in class 12, such as small tools that cost less than \$200.

The 50% rule does not apply when the available-for-use rule (discussed on page 28) denies a CCA claim until the second tax year after you acquired a property.

If you need more details on the 50% rule, see Interpretation Bulletin IT-285, *Capital Cost Allowance – General Comments*.

Column 7 – Base amount for CCA

Base your CCA claim on this amount.

For a class 10.1 vehicle you disposed of in your 2004 fiscal period, you may be able to claim 50% of the CCA that would be allowed if you still owned the vehicle at the end of your 2004 fiscal period. This is known as the **half-year rule on sale**.

You can use the half-year rule on sale if, at the end of your 2003 fiscal period, you owned the class 10.1 vehicle you disposed of in 2004. If this applies to you, in column 7 enter 50% of the amount in column 2.

Column 8 – Rate (%)

Enter the rate in this column for each class of property in Area E of Form T2042. For a list of rates, see “Capital Cost Allowance (CCA) Rates” on page 50. For more detailed information on certain kinds of property, see “Classes of depreciable property” on this page.

Column 9 – CCA for the year

In column 9, enter the CCA you would like to deduct for 2004. The CCA you deduct cannot be more than the amount you get when you multiply the amount in column 7 by the rate in column 8. You can deduct any amount up to the maximum.

If this is your first year of business, you may have to prorate your CCA claim. See “You were asking?” on page 29.

Add up all the amounts in column 9 for all your classes of depreciable property and enter the total on line 9936,

“Capital cost allowance.” See “Personal use of property” on page 34 to find out how to calculate your CCA claim if you are using the property for both business and personal use.

Column 10 – UCC at the end of the year

This is the UCC at the end of your 2004 fiscal period. It is the amount you will enter in column 2 when you calculate your CCA claim next year.

Enter “0” in column 10 if you have a terminal loss or a recapture of CCA. There will not be an amount in column 10 for a class 10.1 passenger vehicle you dispose of in the year.

The example at the end of this chapter sums up CCA.

Classes of depreciable property

The following are the most common classes of depreciable farm property, and the rates that apply to each class.

Buildings

A building may belong to class 1, 3, or 6, depending on what the building is made of and the date you acquired it. You also include in these classes the parts that make up the building, such as:

- electrical wiring
- lighting fixtures
- plumbing
- sprinkler systems
- heating equipment
- air-conditioning equipment (other than window units)
- elevators
- escalators

Class 1 (4%)

Class 1 includes most buildings acquired after 1987, unless they specifically belong in another class. Class 1 also includes the cost of certain additions or alterations you made after 1987 to a class 3 building. For more information, see the next section.

Class 3 (5%)

Most buildings acquired before 1988 were added to class 3 or class 6. If you acquired a building before 1990 that does not fall into class 6, you can include it in class 3 if **one** of the following applies:

- you acquired the building under the terms of a written agreement entered into before June 18, 1987; or
- the building was under construction by you, or for you, on June 18, 1987.

Do not transfer to class 1 property you previously included in class 3. However, there is a limit to how much you can include in class 3 for the cost of any additions or alterations made after 1987 to a class 3 building. This limit is one of the following amounts, whichever is less:

- \$500,000; or

- 25% of the building's capital cost (including the cost of additions or alterations to the building included in class 3, class 6, or class 20 before 1988).

Include in class 1 the cost of any additions or alterations over this limit.

Class 6 (10%)

Include in class 6 any building you acquired before 1988 that is made of frame, log, stucco on frame, galvanized iron, or corrugated iron. If you acquired the building after 1987, it has to be made of frame, log, stucco on frame, galvanized iron, or any corrugated metal.

In addition, **one** of the following conditions has to apply:

- the building is used for farming or fishing; or
- the building has no footings or other base supports below ground level.

If either of the above conditions applies, you also add to class 6 the full cost of all additions and alterations to the building.

If neither of the above conditions applies, include the building in class 6 if **one** of the following conditions applies:

- you acquired the building before 1979;
- you entered into an agreement before 1979 to acquire the building, and footings or other base supports were started before 1979; or
- you started construction of the building before 1979 (or it was started under the terms of a written agreement you entered into before 1979), and footings or other base supports of the building were started before 1979.

For additions or alterations to such a building:

- Add to class 6:
 - all additions made before 1979; and
 - only the first \$100,000 of additions or alterations made after 1978.
- Add to class 3:
 - the part of the cost of all additions or alterations above \$100,000 made after 1978 and before 1988; and
 - the part of the cost of additions or alterations above \$100,000 made after 1987, but only up to \$500,000 or 25% of the cost of the building, whichever is less.
- Add to class 1 any additions or alterations above these limits.

If you need more information, see Interpretation Bulletin IT-79, *Capital Cost Allowance – Buildings or Other Structures*.

Other property – Class 8 (20%)

Class 8 includes property that is not included in any other class. For example, furniture, appliances, fixtures, most machinery, and equipment you use in your business are all in this class.

Storage facilities for fresh fruit and vegetables – Class 8 (20%)

Include buildings you use to store fresh fruit or vegetables at a controlled temperature in class 8 instead of class 1, 3, or 6. Also include in class 8 any buildings you use to store silage.

Electronic office equipment – Classes 8 (20%), 10 (30%), 12 (100%), 45 (45%) and 46 (30%)

Certain types of computer equipment and office communication and electronic equipment can become obsolete before you can fully deduct their cost for income tax purposes. This includes photocopiers and fax machines. For such property acquired after April 26, 1993, you can elect to include the property in a separate class. The election will only apply to each property that costs \$1,000 or more. This class does not change the CCA rate that applies to the properties. However, the election lets you calculate a separate CCA deduction for a five-year period. In this way, when all the property in the class is disposed of, the undepreciated capital cost (UCC) of the equipment will be fully deductible as a terminal loss. For more information on terminal losses, see "Column 5 – UCC after additions and dispositions" on page 31.

To make an election to include this property in a separate prescribed class, attach a letter to your income tax return for the tax year in which you acquired the property.

Note

You might still own the electronic office equipment at the beginning of the fifth tax year following the tax year in which the property became available for use. If so, you will have to transfer the UCC of each separate class from the separate prescribed class to the general class in which it would otherwise belong.

The 2004 Federal Budget proposes to create a new CCA class 45, with a rate of 45%, for computer equipment bought after March 22, 2004. The separate class election will not apply to this new class. If you elect to do so, computer equipment bought before 2005 can be included in class 10, at the 30% rate. It would then be eligible for the separate class election, as described above.

The 2004 Federal Budget also proposes to create a new CCA class 46, with a rate of 30%, for data network infrastructure equipment acquired after March 22, 2004. This equipment supports advanced telecommunications applications, such as e-mail, Web searching and hosting, and instant messaging. Class 46 would generally include such assets as switches, multiplexers, routers, and modems.

Passenger vehicles – Class 10.1 (30%)

Your passenger vehicle can belong to either class 10 or class 10.1. We define a passenger vehicle on page 20. Include your passenger vehicle in class 10 unless it meets a class 10.1 condition. List each class 10.1 vehicle separately.

Include your passenger vehicle in class 10.1 if you bought it in 2004 or 2003, and it cost more than \$30,000. We consider the capital cost of that vehicle to be \$30,000, plus the related GST and PST or HST.

The \$30,000 amount is the capital cost limit for a passenger vehicle. However, to determine the class to which your passenger vehicle belongs, you have to use the cost of the vehicle before you add GST and PST or HST.

Example

Vivienne owns a farming business. On June 21, 2004, she bought two passenger vehicles to use in her farming business. The PST rate for her province is 8%. Vivienne kept the following records for 2004:

	Cost	GST	PST	Total
Vehicle 1	\$33,000	\$2,310	\$2,640	\$37,950
Vehicle 2	\$28,000	\$1,960	\$2,240	\$32,200

Vivienne puts vehicle 1 in class 10.1, since she bought it in 2004 and it cost her more than \$30,000. Before Vivienne enters an amount in column 3 of Area A, she has to calculate the GST and PST on \$30,000. She does this as follows:

- GST at 7% of \$30,000 = \$2,100
- PST at 8% of \$30,000 = \$2,400

Therefore, Vivienne's capital cost is \$34,500 (\$30,000 + \$2,100 + \$2,400). She enters this amount in column 3 of Area A.

Vivienne puts vehicle 2 into class 10, since she bought it in 2004 and it did not cost her more than \$30,000. Vivienne's capital cost is \$32,200 (\$28,000 + \$1,960 + \$2,240). She enters this amount in column 3 of Area A.

Note

The GST rate is 7% and we used a PST rate of 8% for this example. To determine the PST for your calculation, use the current rate that applies in your province or territory. You may also live in a province that has harmonized sales tax (HST) of 15%. For more information about HST, see the *General Information for GST/HST Registrants* guide.

Special situations

Changing from personal to business use

If you bought a property for personal use and then started using it in your farming business in your 2004 fiscal period, there is a change in use. You need to determine the capital cost for business purposes.

Enter the fair market value (FMV) of the property in column 3 of Area A or B, whichever applies, if, at the time of change in use, the FMV of the depreciable property is less than its original cost.

When you start to use your property for farming business use, you are considered to have disposed of it. If the FMV of the property is greater than its cost, you may have a capital gain unless you file an election. See Chapter 6 for an explanation of capital gains.

Use the following chart to determine the amount to enter in column 3 when the FMV is more than its original cost.

Capital cost calculation	
Actual cost of the property	\$ _____ A
FMV of the property	\$ _____ B
Amount on line A	\$ _____ C
Line B minus line C (if negative, enter "0")	\$ _____ D
Enter all capital gains deductions claimed for the amount on line D*	
\$ _____ × 2 =	\$ _____ E
Line D minus line E (if negative, enter "0")	
\$ _____ × 1/2 =	\$ _____ F
Capital cost (line A plus line F)	\$ _____ G
* Enter the amount that relates to the depreciable property only.	
Enter the capital cost of the property from line G in column 3 of Area A or B.	

We consider that you acquire the land for an amount equal to its FMV when you change its use. Include this amount on line 9923, "Total cost of all land additions in the year," in Area F.

Personal use of property

If you buy property for both business and personal use, you can show the business part of the property in Area A or B in two ways:

- If your business use stays the same from year to year, enter the total cost of the property in column 3, the personal part in column 4, and the business part in column 5. Enter the amount from column 5 in column 3 of Area E to calculate the CCA you can claim.
- If your business use changes from year to year, enter the total cost of the property in column 3 and column 5, and enter "0" in column 4. Enter the amount from column 5 in column 3 of Area E to calculate the CCA you can claim. When you claim CCA, you will have to calculate the allowable part you can claim for business use.

Example

Jennifer owns a business. She bought a car in 2004 that she uses for both personal and business use. The car cost \$20,000, including all charges and taxes. Therefore, she includes the car in class 10. Her business use varies from year to year. She calculates her CCA on the car for 2004 as follows:

She enters \$20,000 in column 3 and column 5 of Area A. She also enters \$20,000 in column 3 of Area E. By completing the other columns in the chart, she calculates a CCA claim of \$3,000. Because Jennifer used her car partly for personal use, she calculates her CCA claim as follows:

$$\frac{12,000 \text{ (business kilometres)}}{18,000 \text{ (total kilometres)}} \times \$3,000 = \$2,000$$

Jennifer enters \$2,000 on line 9936.

Note

The capital cost limits on a class 10.1 vehicle (a passenger vehicle) still apply when you split the capital cost between business and personal use. For more details, see "Passenger vehicles – Class 10.1" on page 33.

Grants, subsidies, and rebates

You may get a grant, subsidy, or rebate from a government or a government agency to buy depreciable property. When this happens, subtract the amount of the grant, subsidy, or rebate from the property's capital cost. Do this before you enter the capital cost in column 3 of Area A or B.

If the rebate is more than the remaining undepreciated capital cost in the particular class, add the excess to income at line 9570, "Rebates."

You may have incurred GST or HST on some of the depreciable property you acquired for your business. If so, you may have also received an input tax credit from us.

The input tax credit is government assistance. Therefore, subtract it from the property's capital cost. Do this before you enter the capital cost in column 3 of Area A or B, whichever applies. If you receive an input tax credit for a passenger vehicle you use in your business, use **one** of these methods:

- For a passenger vehicle you use 90% or more of the time for your business, subtract the amount of the credit from the vehicle's cost before you enter its capital cost in column 3 of Area A.
- For a passenger vehicle you use less than 90% of the time for your business, do not make an adjustment in 2004. In 2005, subtract the amount of the credit from your beginning undepreciated capital cost.

You may get an incentive from a non-government agency to buy depreciable property. If this happens, you can either include the amount in income at line 9570, or subtract the amount from the capital cost of the property.

See Interpretation Bulletin IT-273, *Government Assistance – General Comments*, for more details about government assistance.

Non-arm's length transactions

When you acquire depreciable property in a non-arm's length transaction (see the definition on page 28), there are special rules to follow to determine the property's cost.

These special rules will not apply if you get the property because of someone's death.

You can acquire depreciable property in a non-arm's length transaction from:

- a resident of Canada;
- a partnership with at least one partner who is an individual resident in Canada; or
- a partnership with at least one partner that is another partnership.

If you pay more for the property than the seller paid for the same property, calculate the capital cost as follows:

Capital cost calculation	
The seller's cost or capital cost	\$ _____ A
The seller's proceeds of disposition	\$ _____ B
Amount from line A	\$ _____ C
Line B minus line C (if negative, enter "0")	\$ _____ D
Enter any capital gains deduction claimed for the amount on line D \$ _____ × 2 =	\$ _____ E
Line D minus line E (if negative, enter "0") \$ _____ × 1/2 =	\$ _____ F
Capital cost (line A plus line F)	\$ _____ G

Enter this amount in column 3 of either Area A or B, whichever applies.

Do not include the cost of the related land. Include the cost of the related land on line 9923, "Total cost of all land additions in the year," in Area F on Form T2042.

We consider that you acquire the land for an amount equal to its FMV when you change its use. Include this amount on line 9923.

There is a limit on the cost of a passenger vehicle you buy in a non-arm's length transaction. The cost is one of these amounts, **whichever is the least**:

- the FMV when you buy it;
- if you bought it in 2004 or 2003, \$30,000 **plus** any GST and PST, or HST you would pay on \$30,000; or
- the seller's cost amount of the vehicle when you buy it.

The cost amount can vary, depending on what the seller used the vehicle for before you bought it. If the seller used the vehicle to earn income, the cost amount will be the undepreciated capital cost (UCC) of the vehicle when you buy it. If the seller did not use the vehicle to earn income, the cost amount will usually be the original cost of the vehicle.

You can also buy depreciable property in a non-arm's length transaction from a corporation or an individual who is not a resident of Canada, or a partnership with no partners who are individuals resident in Canada or no partners that are other partnerships. If you pay more for the property than the seller paid for the same property, calculate the capital cost as follows:

Capital cost calculation	
The seller's cost or capital cost	\$ _____ A
The seller's proceeds of disposition	\$ _____ B
Amount from line A	\$ _____ C
Line B minus line C (if negative, enter "0")	
\$ _____ × 1/2 =	\$ _____ D
Capital cost (line A plus line D)	\$ _____ E
Enter this amount in column 3 of either Area A or B, whichever applies. Do not include the cost of the related land. Include the cost of the related land on line 9923, "Total cost of all land additions in the year," in Area F on Form T2042.	

You might have bought depreciable property in a non-arm's length transaction and paid less for it than the seller paid. If that is the case, your capital cost is the same amount as the seller paid. We consider you to have already deducted as CCA the difference between what you paid and what the seller paid. Enter the amount you paid in column 3 of Area E. Enter the same amount in Area A or B, whichever applies.

For more details on non-arm's length transactions, see Interpretation Bulletin IT-419, *Meaning of Arm's Length*.

Special rules for disposing of a building in the year

If you disposed of a building in the year, special rules may apply that change the amount you use as proceeds of disposition for capital cost purposes. This happens when you meet both of the following conditions:

- you disposed of the building for an amount less than both its cost amount, as calculated below, and its capital cost to you; and
- you, or a person with whom you do not deal at arm's length (see the definition on page 28) owned the land that the building is on, or the land next to it, which was necessary for the building's use.

Calculate the **cost amount** as follows:

- If the building was the only property in the class, the cost amount is the undepreciated capital cost (UCC) of the class before you disposed of the building.
- If there is more than one property in the same class, you have to calculate the cost amount of each building as follows:

$$\frac{\text{capital cost of the building}}{\text{capital cost of all the properties in the class that have not been previously disposed of}} \times \text{UCC of the class} = \text{cost amount of the building}$$

Note

If any property in the class of the building that was acquired at non-arm's length was previously used for a purpose other than gaining or producing income, or if the part of a property used for gaining or producing income has changed, the capital cost of such property has to be recalculated to determine the cost amount of the property.

If you disposed of a building under these conditions and you or a person with whom you do not deal at arm's length disposed of the land in the same year, calculate your deemed proceeds of disposition as shown in Calculation A on page 37.

If you, or a person with whom you do not deal at arm's length, did not dispose of the land in the same year as the building, calculate your deemed proceeds of disposition as shown in Calculation B on page 37.

Calculation A**Land and building sold in the same year**

FMV of the building at the time you disposed of it	\$ _____	A
FMV of the land just before you disposed of it	\$ _____	B
Line A plus line B		\$ _____ C
Seller's cost amount of the land	\$ _____	D
Total capital gains (without reserves) from any disposition of the land (such as a change in use) in the three-year period before you or a person not dealing at arm's length with you disposed of the building, to either you or another person not dealing at arm's length with you	\$ _____	E
Line D minus line E (if negative, enter "0")	\$ _____	F
Line B or line F, whichever amount is less		\$ _____ G
Line C minus line G (if negative, enter "0")		\$ _____ H
Cost amount of the building just before you disposed of it	\$ _____	I
Capital cost of the building just before you disposed of it	\$ _____	J
Line I or line J, whichever amount is less	\$ _____	K
Line A or line K, whichever amount is more		\$ _____ L
Deemed proceeds of disposition for the building		
Line H or line L, whichever amount is less (enter this amount in column 3 of Area D, and include it in column 4 of Area E)	\$ _____	M
Deemed proceeds of disposition for the land		
Proceeds of disposition of the building and the land	\$ _____	N
Amount from line M	\$ _____	O
Line N minus line O (include this amount on line 9924 of Area F)	\$ _____	P
If you have a terminal loss on the building, include it on line 9790, "Other expenses."		

Calculation B**Land and building sold in different years**

Cost amount of the building just before you disposed of it	\$ _____	A
FMV of the building just before you disposed of it	\$ _____	B
Line A or line B, whichever amount is more	\$ _____	C
Actual proceeds of disposition, if any	\$ _____	D
Line C minus line D	\$ _____	E
Line E \$ _____ x 1/2	\$ _____	F
Amount from line D	\$ _____	G
Deemed proceeds of disposition for the building		
Line F plus line G (enter this amount in column 3 of Area D, and include it in column 4 of Area E)	\$ _____	H
If you have a terminal loss on the building, include it on line 9790, "Other expenses."		

Ordinarily, you can deduct all of a terminal loss, but only part of a capital loss. Calculation B ensures that you use the same fraction to calculate a terminal loss for a building as you use to calculate a capital loss on land. As a result of this calculation, you add a part of the amount on line E to the actual proceeds of disposition from the building (see "Terminal loss" on page 31).

Replacement property

In a few cases, you can postpone or defer adding a capital gain or recapture of CCA to income. You might sell a business property and replace it with a similar one, or your property might be stolen, destroyed, or expropriated, and you replace it with a similar one. You can defer tax on the amount of sale proceeds if you reinvest them in replacement property within a reasonable period of time. To defer reporting the gain or recapture of CCA, you must acquire, and you, or a person related to you, must use the new property for the same or similar purpose as the one that you are replacing.

See Interpretation Bulletin IT-259, *Exchanges of Property*, and Interpretation Bulletin IT-491, *Former Business Property*, and its Special Release, for more details.

You can also defer a capital gain or recapture of CCA when you transfer property to a corporation, a partnership, or your child. For more details on transferring property to your child, see page 48. For information on transfers to a corporation or a partnership, see:

- Information Circular 76-19, *Transfer of Property to a Corporation Under Section 85*
- Interpretation Bulletin IT-291, *Transfer of Property to a Corporation Under Subsection 85(1)*
- Interpretation Bulletin IT-378, *Winding-Up of a Partnership*
- Interpretation Bulletin IT-413, *Election by Members of a Partnership Under Subsection 97(2)*

The following example summarizes this chapter on CCA:

Example

In 2004, Trevor bought a building to use for his farming business. The total cost was \$95,000 (the sum of the \$90,000 total purchase price and the \$5,000 total expenses connected with the purchase) as follows:

Building value.....	\$75,000
Land value.....	<u>\$15,000</u>
Total purchase price.....	<u>\$90,000</u>

Expenses connected with the purchase:

Legal fees	\$3,000
Land transfer taxes.....	<u>\$2,000</u>
Total fees	<u>\$5,000</u>

Trevor’s farming business has a December 31 year-end. In 2004, Trevor’s farming income was \$6,000, and his expenses were \$4,900. Therefore, his net income before deducting CCA was \$1,100 (\$6,000 – \$4,900).

Before Trevor can complete his CCA schedule, he has to calculate the capital cost of the building. Since land is not depreciable farm property, he has to calculate the part of the expenses connected with the purchase that relates only to the building. To do this, he has to use the following formula, which we explain on page 30 under the heading “Land.”

$$\frac{\$75,000}{\$90,000} \times 5,000 = \$4,166.67$$

This \$4,166.67 represents the part of the \$5,000 in legal fees and land transfer taxes that relates to the purchase of the building, while the remaining \$833.33 relates to the purchase of the land. Therefore, the capital cost of the building is:

Building value.....	\$ 75,000.00
Related expenses	\$ <u>4,166.67</u>
Capital cost of the building.....	\$ <u>79,166.67</u>

Trevor enters \$79,166.67 in column 3 of Area B and \$15,833.33 (\$15,000 + \$833.33) on line 9923 of Area F as the capital cost of the land.

Note

Trevor did not own farm property before 2004. Therefore, he has no undepreciated capital cost to enter in column 2 of Area E.

Trevor acquired his farm property in 2004. Therefore, he is subject to the 50% rule that we explain under the heading “Column 6 – Adjustment for current-year additions” on page 31.

Chapter 4 – Eligible Capital Expenditures

What is an eligible capital expenditure?

You may buy property that has no physical existence, but gives you a lasting economic benefit. Some examples are milk and egg quotas. We call this kind of property **eligible capital property**. The price you pay to buy this kind of property is an **eligible capital expenditure**.

What is an annual allowance?

You cannot deduct the full cost of an eligible capital expenditure, because the cost is capital and the eligible capital property gives you a lasting economic benefit. However, you can deduct part of its cost each year. We call the amount you can deduct your **annual allowance**.

What is a cumulative eligible capital (CEC) account?

This is the bookkeeping record you set up to determine your annual allowance. You also use your CEC account to keep track of the property you buy and sell. We call the property in your CEC account your eligible capital property. You base your annual allowance on the balance in your account at the end of your fiscal period. Keep a separate account for each business.

How to calculate your annual allowance

Complete the following chart to calculate your annual allowance and the balance in your CEC account at the end of your 2004 fiscal period.

Calculating your annual allowance and your CEC account balance at the end of your 2004 fiscal period

Balance in the account at the start of your 2004 fiscal period	_____	A
Eligible capital expenditures you made in your 2004 fiscal period	_____	B
75% × line B	_____	C
Line A plus line C	=====	D
All the amounts you received or are entitled to receive from the sale of eligible capital property in your 2004 fiscal period	_____	E
All the amounts that became receivable in your 2004 fiscal period from the sale of eligible capital properties before June 18, 1987	_____	F
Line E plus line F	_____	G
75% × line G	_____	H
CEC account balance Line D minus line H	=====	I
Annual allowance: 7% × line I	_____	J
CEC account balance at the end of 2004 Line I minus line J	=====	K

Note

An eligible capital expenditure is reduced by the amount of any assistance received or receivable from a government. Also, an amount forgiven (or entitled to be forgiven) on loans from a government regarding an eligible capital expenditure reduces your CEC account.

An eligible capital expenditure made in a non-arm's length transaction is reduced by the capital gains deduction claimed by the seller. **Under proposed amendments**, an eligible capital expenditure made in a non-arm's length transaction after December 20, 2002, is also reduced by the non-taxable portion of the seller's gain.

If your fiscal period is less than 365 days, you have to prorate your claim. Base your claim on the number of days in your fiscal period compared to 365 days.

You can deduct an annual allowance if there is a **positive** balance in your CEC account at the end of your 2004 fiscal period. You can deduct up to a maximum of 7% of the balance, but you do not have to deduct the maximum annual allowance. If there is a **negative** balance in your CEC account, see "Sale of eligible capital property – Fiscal period ending in 2004" on page 40.

Example

Sylvie started her farming business on January 1, 2004. Her business has a December 31 year-end. During 2004, she bought a milk quota for \$135,000. To calculate her annual allowance and her CEC account balance at the end of her fiscal year, she completes the chart as follows:

Sylvie's CEC account

Balance at the start of her 2004 fiscal period	\$ _____	A
Milk quota cost during her 2004 fiscal period	\$ <u>135,000</u>	B
75% × line B	\$ <u>101,250</u>	C
Line A plus line C	\$ <u>101,250</u>	D
Sylvie does not have any amounts on lines E to H. Therefore, her CEC account balance is the amount on line D	\$ <u>101,250</u>	I
Her annual allowance is 7% × line I	\$ <u>7,087</u>	J
Balance at the end of 2004 Line I minus line J	\$ <u>94,163</u>	K

Election

You can elect to treat a disposition of eligible capital property (ECP) as a capital gain instead of including it in the chart "Calculating your annual allowance and your CEC account balance at the end of your 2004 fiscal period" on this page.

If you make the election, the proceeds of disposition on lines E and F of the chart are considered to be equal to the original cost.

You can then declare a capital gain equal to your actual proceeds of disposition **minus** the cost of acquisition. Report the details on the "Real estate, depreciable property, and other properties" line on Schedule 3, *Capital Gains (or Losses) in 2004*.

The election is only available if you meet the following conditions:

- you disposed of an ECP;
- the cost of the ECP can be determined;
- the proceeds of disposition exceed the cost;
- the ECP that you disposed of is not goodwill; and
- you have no exempt gains balance.

Making the election will help you if you have capital losses to apply against your gain.

The election may also help if you are eligible to claim a capital gains deduction and you disposed of an ECP that is a qualified farm property. If you disposed of an ECP that was a qualified farm property, any deemed gain reported under the election is also considered to be from a disposition of qualified farm property. If this is the case, report the details on the "Qualified farm property" line on Schedule 3, *Capital Gains (or Losses) in 2004*, instead of the "Real estate, depreciable property, and other properties" line. See "Qualified farm property and cumulative capital gains deduction" on page 47. Attach a note to your income tax return stating that you are electing under subsection 14(1.01) of the *Income Tax Act*.

Sale of eligible capital property – Fiscal period ending in 2004

When you sell eligible capital property, you have to subtract part of the proceeds of disposition from your CEC account.

You have to do this calculation if you sell eligible capital property:

- in your 2004 fiscal period; or
- before June 18, 1987, and the proceeds of disposition become due to you in your 2004 fiscal period.

For 2004, the amount you have to subtract is 75% of the **total** of these amounts:

- the proceeds of disposition of all eligible capital property you sell in your 2004 fiscal period (include the amount from a sale even if you do not get any or all of the proceeds until after 2004); and
- the amount of any proceeds that become due to you in your 2004 fiscal period from eligible capital property you sold before June 18, 1987.

If you have a negative balance in your CEC account after you subtract the required amount, you have to calculate the part of that amount to include in your farming income.

The part of the negative amount in your CEC account that exceeds the annual allowances deducted is multiplied by 2/3. To that result, you add the excess or annual allowances deducted, whichever is less. This is the amount to include in your farming income. The following example shows how to calculate the amount to include in farming income.

Example

Carol started her farming business on January 1, 1997, with a December 31 year-end. In 1998, she bought an egg quota for \$25,000. Carol sold her farming business on September 1, 2004. She sold her egg quota for \$65,000 and she does not have any other eligible capital property in her farming business. She deducted annual allowances each year as follows:

1998.....	\$ 1313
1999.....	1220
2000.....	1135
2001.....	1056
2002.....	982
2003.....	<u>913</u>
Total	<u>\$ 6,619</u>

The amount included in Carol's farming income on line 9600, "Other income," is the total of amounts A and C:

Calculation of amount A

The lesser of i) or ii):

- i) Excess amount calculated as follows:

Proceeds of disposition: \$65,000	
\$65,000 × 75%	\$ 48,750
Plus: total annual allowances deducted	<u>\$ 6,619</u>
	\$ 55,369

Minus: 75% of eligible capital expenditures	
\$25,000 × 75%	\$ 18,750
Excess amount	\$ 36,619 i

- ii) Total annual allowances deducted \$ 6,619 **ii**
 The lesser of i) or ii) \$ 6,619 **A**

Calculation of amount B

Excess amount	\$36,619	
Minus: total annual deductions taken	<u>\$ 6,619</u>	\$ 30,000 B

Calculation of amount C

Line B × 2/3	\$ 20,000 C
Line A plus line C	<u>\$ 26,619</u>

The amount Carol includes in farming income on line 9600, "Other income," is \$26,619.

Carol does not have an exempt gains balance in this example, because she did not file Form T664, *Election to Report a Capital Gain on Property Owned at the End of February 22, 1994*. If you filed Form T664, see Chapter 5 in the *Business and Professional Income* guide for information about eligible capital property.

If the property is considered to be a qualified farm property, part of the farming income may be eligible for the capital gains deduction. For more details, read the following section.

Farming income from the sale of eligible capital property eligible for the capital gains deduction

Part of your farming income from the sale of eligible capital property (ECP) that is **qualified farm property** may be eligible for the capital gains deduction. You will find the definition of **qualified farm property** on page 47. If you have more than one business, do a separate calculation for each. If you are a sole proprietor, complete Chart 1, on the next page, to calculate the amount eligible for the capital gains deduction from the sale of ECP. If your farming business is a partnership, complete Chart 2.

**Chart 1 – Sole proprietor
Farming income eligible
for the capital gains deduction**

Farming income from the sale of ECP (other than recapture of annual allowances deducted in previous years) for 2004 before applying your exempt gains balance*	_____	A
All or part of your exempt gains balance for the business that you are using to reduce the amount on line A for 2004	_____	B
Line A minus line B	_____	C
All proceeds of disposition from the sale of ECP that is QFP during fiscal periods that began after 1987 and ended before February 28, 2000	_____	D
All eligible capital expenditures made or incurred for QFP sold during fiscal periods that began after 1987 and ended before February 28, 2000	_____	E
Outlays and expenses related to dispositions described on line D not deducted in calculating income	_____	F
Line E plus line F	_____	G
Line D minus line G	_____	H
Amount from line H _____ × 3/4 =	_____	I
All proceeds of disposition from the sale of ECP that is QFP during fiscal periods ending after February 27, 2000, and before October 18, 2000	_____	J
All eligible capital expenditures made or incurred for QFP sold during fiscal periods ending after February 27, 2000, and before October 18, 2000	_____	K
Outlays and expenses related to dispositions described on line J not deducted in calculating income	_____	L
Line K plus line L	_____	M
Line J minus line M	_____	N
Amount from line N _____ × 2/3 =	_____	O

continued in next column

**Chart 1 – Sole proprietor
Farming income eligible
for the capital gains deduction
(continued)**

All proceeds of disposition from the sale of ECP that is QFP during fiscal periods ending after October 17, 2000	_____	P
All eligible capital expenditures made or incurred for QFP sold during fiscal periods ending after October 17, 2000	_____	Q
Outlays and expenses related to dispositions described on line P not deducted in calculating income	_____	R
Line Q plus line R	_____	S
Line P minus line S	_____	T
Amount from line T _____ × 1/2 =	_____	U
Line I plus line O plus line U	_____	V
All taxable capital gains from the dispositions of ECP of the farming business that is QFP for fiscal periods that began after 1987 and ended before February 23, 1994	_____	W
Farming income eligible for the capital gains deduction from the sale of ECP that is QFP for fiscal periods that began after February 22, 1994, and ended before January 1, 2004	_____	X
Line W plus line X	_____	Y
Line V minus line Y	_____	Z
Farming income eligible for the capital gains deduction for 2004 (line C or line Z, whichever is less)	_____	AA

Enter the amount from line **AA** on line 173 of Schedule 3, *Capital Gains (or Losses) in 2004*. You can get this schedule in the *General Income Tax and Benefit Guide* package. To claim the capital gains deduction, use Form T657, *Calculation of Capital Gains Deduction for 2004*.

* You only have an exempt gains balance if you filed Form T664, *Election to Report a Capital Gain on Property Owned at the End of February 22, 1994*. For information on how to apply your exempt capital gains balance, see the *Business and Professional Income* guide.

**Chart 2 – Partnerships
Farming income eligible
for the capital gains deduction**

Farming income from the sale of ECP (other than recapture of annual allowances deducted in previous years) for 2004 _____ **A**

All proceeds of disposition from the sale of ECP that is QFP during fiscal periods that began after 1987 and ended before February 28, 2000 _____ **B**

All eligible capital expenditures made or incurred for QFP sold during fiscal periods that began after 1987 and ended before February 28, 2000 _____ **C**

Outlays and expenses related to dispositions described on line B not deducted in calculating income _____ **D**

Line C **plus** line D _____ **E**

Line B **minus** line E _____ **F**

Amount from line F _____ $\times 3/4 =$ _____ **G**

All proceeds of disposition from the sale of ECP that is QFP during fiscal periods ending after February 27, 2000, and before October 18, 2000 _____ **H**

All eligible capital expenditures made or incurred for QFP sold during fiscal periods ending after February 27, 2000, and before October 18, 2000 _____ **I**

Outlays and expenses related to dispositions described on line H not deducted in calculating income _____ **J**

Line I **plus** line J _____ **K**

Line H **minus** line K _____ **L**

Amount from line L _____ $\times 2/3 =$ _____ **M**

All proceeds of disposition from the sale of ECP that is QFP during fiscal periods ending after October 17, 2000 _____ **N**

continued in next column

**Chart 2 – Partnerships
Farming income eligible
for the capital gains deduction
(continued)**

All eligible capital expenditures made or incurred for QFP sold during fiscal periods ending after October 17, 2000 _____ **O**

Outlays and expenses related to dispositions described on line N not deducted in calculating income _____ **P**

Line O **plus** line P _____ **Q**

Line N **minus** line Q _____ **R**

Amount from line R _____ $\times 1/2 =$ _____ **S**

Line G **plus** line M **plus** line S _____ **T**

All taxable capital gains from the disposition of ECP for the farming business that is QFP for fiscal periods that began after 1987 and ended before February 23, 1994 _____ **U**

Farming income eligible for the capital gains deduction from the sale of ECP that is QFP for fiscal periods that began after February 22, 1994, and ended before January 1, 2004 _____ **V**

Line U **plus** line V _____ **W**

Line T **minus** line W _____ **X**

Farming income eligible for the capital gains deduction for 2004 (the lesser of line A and line X) _____ **Y**

Your share of the amount on line Y _____ **Z**

The amount you claimed as a business income reduction for 2004* _____ **AA**

Your share of the farming income eligible for the capital gains deduction
(line Z **minus** line AA) _____ **BB**

Enter the amount from line **BB** (above) on line 173 of Schedule 3, *Capital Gains (or Losses) in 2004*. To claim the capital gains deduction, use Form T657, *Calculation of Capital Gains Deduction for 2004*.

* You would only have a business income reduction if you filed Form T664, *Election to Report a Capital Gain on Property Owned at the End of February 22, 1994*. For information about applying your business income reduction, see the *Capital Gains* guide.

Replacement property

If you sell an eligible capital property and replace it with another one for the same or similar use, you can postpone all or part of any gain on the sale. This happens if you acquire a replacement eligible capital property within a certain period of time. To do this, you have to replace the property no later than one year after the end of the tax year in which you sell the original property. For more details, see Interpretation Bulletin IT-259, *Exchanges of Property*.

For more information about eligible capital expenditures, see Interpretation Bulletin IT-123, *Transactions Involving Eligible Capital Property*, and Interpretation Bulletin IT-143, *Meaning of Eligible Capital Expenditure*, and its Special Release.

Chapter 5 – Farm Losses

When the expenses for your farming business are more than the income for the year, you have a net operating loss. However, before you can calculate your net farm loss for the year, you may have to increase or decrease the loss by certain adjustments explained in “Line 9941 – Optional inventory adjustment included in 2004” on page 23, and “Line 9942 – Mandatory inventory adjustment included in 2004” on page 24.

If you show a net farm loss for the year, read this chapter for information on how to treat your loss. For more details on farm losses, see Interpretation Bulletin IT-322, *Farm Losses*.

The amount of the net farm loss you can deduct depends on the nature and extent of your business. Your farm loss may be:

- fully deductible
- partly deductible (restricted farm loss)
- non-deductible

Fully deductible farm losses

If you made your living from farming, we consider farming to be your chief source of income. As long as farming was your chief source of income, you can deduct the full amount of your net farm loss from other income. Farming can still be your chief source of income even if your farm did not show a profit. Other income could come from investments, part-time employment, and so on.

To determine if farming was your chief source of income, you need to consider such factors as:

- gross income
- net income
- capital invested
- cash flow
- personal involvement
- your farm’s ability to make a profit (both actual and potential)

- plans to maintain or develop your farm and how you carried out these plans

Although you may have been a partner in a farming business, you still have to determine if farming was your own chief source of income.

When farming is your chief source of income and you show a net farm loss in 2004, you may have to reduce the loss when you have other income in 2004. Any loss that is left is your farm loss for 2004.

Example

Rick’s farming business, which is his chief source of income, has a December 31 fiscal year-end. His farm loss before adjustments is \$50,000. He wants to reduce his loss by the optional inventory adjustment (OIA). Rick kept the following records for 2004:

Net farm loss before adjustments.....	\$50,000
Optional inventory adjustment	\$15,000
Other income	\$ 2,000

To reduce the loss amount, Rick adds back his OIA. He determines his farm loss for 2004 as follows:

Farm loss before adjustments	(\$50,000)
Add optional inventory adjustment	\$15,000
Farm loss after adjustments	(\$35,000)
Add other income	\$ 2,000
Farm loss for 2004	(\$33,000)

Carry back – 2004 farm loss

You can carry back your 2004 farm loss for up to 3 years. You can also carry it forward up to 10 years. In both cases, you can deduct it from your income from all sources in those years.

If you choose to carry back your 2004 farm loss to your 2001, 2002, or 2003 income tax returns, complete Form T1A, *Request for Loss Carryback* and file one copy of the form with your 2004 income tax return. Do not file an amended return for the year to which you apply the loss.

Applying your farm losses from years before 2004

You may be able to apply farm losses you had in any year from 1994 to 2003 on your 2004 income tax return. You can apply these losses if you did not already deduct them, and you have net income in 2004. To apply these losses to 2004, you have to apply the loss from the earliest year first. Enter the amount you wish to deduct on line 252 on your income tax return.

Non-capital loss

You may have incurred a loss in 2004 from a business other than farming. If this loss is more than your other income for the year, you may have a non-capital loss. Use Form T1A to calculate your 2004 non-capital loss.

You can carry back your non-capital loss up to three years and carry it forward seven years.

The 2004 Federal Budget proposes to extend the carry-forward period for non-capital losses from 7 to 10 years for taxation years ending after March 22, 2004.

If you choose to carry back your 2004 non-capital loss to your 2001, 2002, or 2003 income tax returns, complete Form T1A. File one copy of the form with your 2004 return. Do not file an amended return for the year to which you apply the loss.

For more details about non-capital losses, see Interpretation Bulletin IT-232, *Losses – Their Deductibility in the Loss Year or in Other Years*.

Partly deductible losses (restricted farm losses)

You may have run your farm as a business. For your farm to be considered a business, you must have carried on activities with the intention of making a profit and there must be evidence to support that intention.

However, if farming was not your chief source of income (for example, you did not rely on farming alone to make your living), you may be able to deduct only part of your net farm loss.

Each year you have a farm loss, check your situation carefully to see if farming was your chief source of income. It is important to do this, since a farming loss may be restricted in one year, but not in another year.

How to calculate your restricted farm loss

If farming was not your chief source of income and you had a net farm loss, the loss you can deduct depends on the amount of your net farm loss.

When your net farm loss is \$15,000 or more, you can deduct \$8,750 from your other income. The rest of your net farm loss is your restricted farm loss.

When your net farm loss is less than \$15,000, the amount you can deduct from your other income is one of the following two amounts, whichever is **less**:

- A) your net farm loss for the year; or
- B) \$2,500 **plus** 50% × (your net farm loss **minus** \$2,500).

The amount remaining is your restricted farm loss.

Note

When the farm loss you deduct is different from your actual farm loss because of the restricted farm loss calculation, you should indicate this on your income tax return on the line called "Farming Income." For example, you can do this by noting "restricted farm loss," "RFL," or "Section 31" to the left of line 168.

Example

Sharon ran a cattle farm with the intention of making a profit. However, farming was not her chief source of income in 2004. In 2004, she had employment income and a net farm loss of \$9,200, which she calculated on line 9946 of Form T2042.

The part of Sharon's net farm loss she can deduct from her other income in 2004 is either amount A or B, whichever is **less**:

- A) \$9,200; or
- B) \$2,500 **plus** 50% × (\$9,200 – \$2,500)
\$2,500 **plus** 50% × \$6,700

Therefore, B = (\$2,500 + \$3,350) = \$5,850.

Because Sharon can only deduct either A or B, whichever amount is **less**, she enters \$5,850 on line 141 of her income tax return and deducts this amount from her other income in 2004. Her restricted farm loss is the amount that remains, which is \$3,350 (\$9,200 **minus** \$5,850). Sharon prints "Section 31" to the left of line 168 on her income tax return to show that the loss she is deducting is the result of a restricted farm loss calculation.

Applying your 2004 restricted farm loss

You can carry back your 2004 restricted farm loss up to three years, and carry it forward up to ten years. The amount you deduct in any year cannot be more than your net farming income for that year. If you have no net farming income in any of those years, you cannot deduct any restricted farm loss.

To carry back your 2004 restricted farm loss to your 2001, 2002, or 2003 income tax returns, use Form T1A, *Request for Loss Carryback*, and file one copy of the form with your 2004 income tax return. Do not file an amended return for the year to which you would like the loss applied.

Applying your restricted farm losses from years before 2004

You may have net farming income in 2004. If so, you may be able to apply to your 2004 income tax return restricted farm losses you had in any year from 1994 to 2003. You can apply these losses as long as you did not already deduct them from your farming income. Also, you can only apply them up to the amount of your net farming income in 2004. You have to apply the loss from the earliest year first, before you apply the losses from other years. Claim this amount on line 252 of your income tax return.

You may have sold farmland at a time when you had restricted farm losses that you did not claim. When this happens, you may be able to reduce the amount of your capital gain from the sale. For more details, see "Restricted farm losses" on page 47.

Non-deductible farm losses

If you did not run your farm as a business, you cannot deduct any part of your net farm loss. For your farm to have been a business, there must have been an intent to make a profit and evidence supporting that intention.

The size and scope of your farm may make it impossible for the farm to make a profit, either now or in the near future. In this case, you cannot deduct your farm loss. We consider this kind of farm to be personal. Therefore, any farm expenses are personal expenses.

Chapter 6 – Capital Gains

This chapter explains the capital gains rules for people who farm. We cover the general capital gains rules in the *Capital Gains* guide.

Throughout this chapter, we use the terms **sell**, **sold**, **buy**, or **bought**. These words describe most capital transactions. However, the information in this chapter also applies to deemed dispositions or acquisitions. When reading this chapter, you can use the terms **sold** instead of **disposed of**, and **bought** instead of **acquired**, if they more clearly describe your situation.

List the dispositions of all your properties on Schedule 3, *Capital Gains (or Losses) in 2004*. You can get this schedule and other forms and publications from our Web site at www.cra.gc.ca, or by calling us at 1-800-959-2221.

You may be a partner in a partnership that provides you with a T5013 slip, *Statement of Partnership Income*. If the partnership has a capital gain, the partnership will allocate part of that gain to you. The gain will be reported on the partnership's financial statements or on your T5013 slip.

What is a capital gain?

You have a capital gain when you sell, or are considered to have sold, a capital property for **more** than its adjusted cost base **plus** the expenses or outlays you incurred to sell the property. To calculate your capital gain, subtract the adjusted cost base of your property from the proceeds of disposition. From this amount, subtract any outlays or expenses you incurred when selling your property.

In most cases, capital property includes land, buildings, and equipment that you used in your farming business. Therefore, capital property includes depreciable and non-depreciable property.

You have to include your taxable capital gain in income. Not all of your capital gain is taxable. Generally, for 2004 your taxable capital gain is one-half of your capital gain.

A disposition of depreciable property may result in a recapture of capital cost allowance (CCA). We explain recapture on page 31.

What is a capital loss?

You have a capital loss when you sell, or are considered to have sold, non-depreciable capital property for **less** than its adjusted cost base **plus** the expenses or outlays you incurred to sell the property. To calculate your capital loss, subtract the adjusted cost base of your property from the proceeds of disposition. From this amount, subtract any outlays or expenses you incurred when selling your property.

Not all of your capital loss is deductible. For 2004, your allowable capital loss is one-half of your capital loss. You can only deduct an allowable capital loss from a taxable capital gain.

A loss on a disposition of depreciable property may only result in a terminal loss. We explain terminal loss on page 31.

Definitions

Before you can determine your capital gain or loss, you will need to know the following terms.

Proceeds of disposition – In most cases, the proceeds of disposition is the sale price of the property. We define this term on page 28.

Adjusted cost base (ACB) – The ACB is usually the original cost of the property (including amounts you paid to buy it, such as commissions and legal fees). ACB includes other costs, such as the cost of any additions or the cost to renovate or improve the property.

Outlays and expenses – Outlays and expenses are costs you incurred to sell your property. These include costs such as commissions, surveyors' fees, transfer taxes, and advertising costs.

Fair market value (FMV) – This is generally the highest dollar value you can get for your property. We define this term on page 28.

How to calculate your capital gain or loss

To calculate your capital gain or loss, use the following formula:

Proceeds of disposition	\$ _____	A
Adjusted cost base	\$ _____	B
A minus B	\$ _____	C
Outlays and expenses	\$ _____	D
C minus D = Capital gain (loss)	\$ _____	E

Note

You have to calculate the capital gain or loss on each property separately.

Did you sell capital property in 2004 that you owned before 1972?

If you did, you have to apply a special set of rules when you calculate your capital gain or loss, because you did not have to pay tax on capital gains before 1972. To help you calculate your gain or loss from the sale of property you owned before 1972, use Form T1105, *Supplementary Schedule for Dispositions of Capital Property Acquired Before 1972*.

Disposing of farmland that includes your principal residence

Your home is usually your principal residence. If your home was your principal residence for every year you owned it, you generally do not pay tax on any capital gains when you dispose of it. Therefore, if you sold farmland that included your home in 2004, only part of the gain is taxable. You can choose one of two methods to determine your taxable capital gain. Try both methods to see which one is best for you.

We usually consider approximately one acre of land on which your residence is situated to be part of your principal residence. We will allow you more if you can prove that

you needed more land to use and enjoy your principal residence.

Method 1

Separately calculate the capital gain on your principal residence and each of your farm properties. To do this, apportion the proceeds of disposition, the ACB, and any selling expenses between:

- your principal residence; and
- each of your farm properties.

Then, calculate the **taxable** capital gain on your principal residence, if any, and each of the farm properties.

Value the land that is part of your principal residence at one of the following two amounts, whichever is **more**:

- the FMV of the land; or
- the FMV of a comparable residential building site in the area.

Example

On February 1, 2004, Helena sold her 32-acre farm, which included her principal residence. One acre of land is part of her principal residence. Helena has these details:

Value of land when she purchased her farm

FMV of similar farmland per acre	\$ 3,750
FMV of a typical residential building site in the area	\$ 15,000

Value of land when she sold her farm

FMV of similar farmland per acre	\$ 6,250
FMV of a typical residential building site in the area.....	\$ 25,000

Adjusted cost base (ACB) – actual purchase price

Land	\$ 120,000
House.....	60,000
Barn.....	16,000
Silo.....	<u>4,000</u>
Total.....	\$ <u>200,000</u>

Proceeds of disposition – actual sale price

Land	\$ 200,000
House.....	75,000
Barn.....	20,000
Silo.....	<u>5,000</u>
Total.....	\$ <u>300,000</u>

Proceeds of disposition	Principal residence	Farm properties	Total
Land	\$ 25,000*	\$175,000	\$200,000
House	75,000		75,000
Barn		20,000	20,000
Silo		<u>5,000</u>	<u>5,000</u>
	<u>\$100,000</u>	<u>\$200,000</u>	<u>\$300,000</u>

Minus ACB

Land	\$ 15,000*	\$105,000	\$120,000
House	60,000		60,000
Barn		16,000	16,000
Silo		<u>4,000</u>	<u>4,000</u>
	<u>\$ 75,000</u>	<u>\$125,000</u>	<u>\$200,000</u>

Gain on sale	\$ 25,000	\$ 75,000	\$100,000
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Minus:

Gain on principal residence**	<u>25,000</u>	_____	<u>25,000</u>
Capital gain	\$ _____	\$ <u>75,000</u>	\$ <u>75,000</u>
Taxable capital gain	(1/2 × \$75,000)		\$ <u>37,500</u>

* Helena uses the value of a typical residential building site for the land that is part of her principal residence, because the FMV of a typical site in the area is more than the FMV of one acre of farmland.

** Because Helena’s home was her principal residence during all the years she owned it, the capital gain is not taxable.

Note

If your home was **not** your principal residence for every year you owned it, there could be a capital gain on it that you have to include in your income. Form T2091(IND), *Designation of a Property as a Principal Residence by an Individual (Other Than a Personal Trust)*, will help you calculate the number of years you are entitled to designate your home as your principal residence and calculate the part of your gain, if any, that is taxable.

Method 2

Determine the capital gain on your land and your principal residence. Then subtract \$1,000 from the gain. Subtract an additional \$1,000 for each year after 1971 that the property was your principal residence and you were a resident of Canada. Using Method 2, you can reduce a gain to nil, but you cannot create a loss.

To calculate your capital gain, use the following formula:

Proceeds of disposition	\$ _____	A
Adjusted cost base	\$ _____	B
A minus B	\$ _____	C
Outlays and expenses	\$ _____	D
Capital gain before reduction (C minus D)	\$ _____	E
Method 2 reduction	\$ _____	F
Capital gain after reduction (E minus F)	\$ _____	G

Note

Transfer the entries on lines A, B, D, and G to the relevant columns on Schedule 3, *Capital Gains (or Losses) in 2004*, under “Qualified farm property” or “Real estate, depreciable properties, and other property.”

If you choose this method, attach a letter to your income tax return that includes the following information:

- a statement by you that you sold your farm and are electing under subparagraph 40(2)(c)(ii) of the *Income Tax Act*;
- a description of the property you sold; and
- the number of years after 1971 that the farmhouse was your principal residence during which you were a

resident of Canada (if you purchased your farm after 1971, give the date you purchased it).

As proof of the value of your property, regardless of the method you choose, keep documents that have the following information:

- a description of the farm, including the size of the buildings and construction type;
- the cost of the property and the date of purchase;
- the cost of any additions or improvements you made to the property;
- the assessment for property tax purposes;
- any insurance coverage;
- the type of land (arable, bush, or scrub); and
- the type of farm operation.

If you need more details, see Interpretation Bulletin IT-120, *Principal Residence*.

Restricted farm losses

You may have a capital gain from farmland you sell in 2004. You may also have restricted farm losses from previous years that you have not yet used. In this case, you can deduct part of these losses from the gain. The part you can deduct is the property taxes and the interest on money you borrowed to buy the land, if you included these amounts in the calculation of the restricted farm loss in question.

You cannot use the restricted farm loss to create or increase a capital loss on the sale of your farmland.

Qualified farm property and cumulative capital gains deduction

If you have a taxable capital gain from the sale of qualified farm property, you may be able to claim a capital gains deduction. We explain **qualified farm property** on this page. For details on how to calculate your capital gains deduction, see Form T657, *Calculation of Capital Gains Deduction for 2004* and Form T936, *Calculation of Cumulative Net Investment Loss (CNIL) to December 31, 2004*.

You may be a partner in a partnership that sold capital property. In this case, the partnership includes any taxable capital gain in its income. However, as a partner, you can only claim the capital gains deduction for your share of the gain on qualified farm property.

What is qualified farm property?

Qualified farm property is certain property you, your spouse, or common-law partner own. It is also certain property owned by a family-farm partnership in which you, your spouse, or common-law partner hold an interest. We define spouse and common-law partner in the *General Income Tax and Benefit Guide*.

Qualified farm property includes:

- a share of the capital stock of a family-farm corporation that you, your spouse, or common-law partner own

- an interest in a family-farm partnership that you, your spouse, or common-law partner own
- real property, such as land and buildings
- eligible capital property, such as milk and egg quotas

Real property or eligible capital property as qualified farm property

Real property or eligible capital property is qualified farm property only if it is used to carry on a farming business in Canada by any **one** of the following:

- you, your spouse or common-law partner, or any of your parents or children (we define children on page 48);
- the beneficiary of a personal trust, or the spouse or common-law partner, parent, or child of such a beneficiary;
- a family-farm corporation where any of the above persons owns a share of the corporation; or
- a family-farm partnership where any of the above persons (except a family-farm corporation) owns an interest in the partnership.

You may have bought or entered into an agreement to buy real or eligible capital property before June 18, 1987.

We consider you to have used this property in carrying on a farming business in Canada if you meet **one** of these conditions:

- In the year you disposed of it, the property or the one it replaced was used principally in a farming business in Canada by any of the above persons, a family-farm partnership, or corporation, or by a personal trust from which one of the above individuals acquired the property.
- The property, or the property it replaced, was used principally in a farming business in Canada for at least five years by any of the above persons, a family-farm partnership, or corporation, or by a personal trust from which one of the above individuals acquired the property. During this time, the property was owned by any of the above persons or a family-farm partnership or corporation.

We will also consider real or eligible capital property to be used to carry on a farming business in Canada if you meet the following conditions:

- throughout the 24 months before the sale, you, your spouse or common-law partner, any of your children or parents, a personal trust from which one of these persons acquired the property, or a family-farm partnership (in which any of these persons has an interest) must have owned the property; and
- you meet one of the following two conditions:
 - the property or the property it replaced was used mainly in a farming business in Canada in which any of the above persons was actively engaged on a regular and ongoing basis. Also, in any 24 months of ownership, the person's gross income from the farming business was larger than the person's income from all other sources in the year; or

- a family-farm partnership or corporation used the property for at least 24 months, mainly to carry on a farming business in Canada. Also, during this time, you, your spouse or common-law partner, any of your children, or your parents must have been actively engaged on a regular and ongoing basis in the farming business.

Transfer of farm property to a child

You may be able to transfer Canadian farm property to your child. When you do this, you can postpone tax on any taxable capital gain and any recapture of capital cost allowance until the child sells the property. To do this, **both** of these conditions have to be met:

- Your child is a resident of Canada just before the transfer.
- The farm property is used mainly in a farming business in which you, your spouse or common-law partner, or any of your children were actively engaged on a regular and ongoing basis before the transfer.

Your **children** include:

- your natural child, your adopted child, or your spouse's or common-law partner's child
- your grandchild or great-grandchild
- your child's spouse or common-law partner
- another person who is wholly dependent on you for support and who is, or was immediately before the age of 19, in your custody and under your control

The following types of property qualify for this transfer:

- farmland
- depreciable property, including buildings
- eligible capital property

Furthermore, a share of the capital stock of a family-farm corporation and an interest in a family-farm partnership also qualify for this transfer if your child is a resident of Canada just before the transfer.

For most property, the transfer price can be any amount between the adjusted cost base (ACB) and its fair market value (FMV). For depreciable property, the transfer price can be any amount between its undepreciated capital cost (UCC) and FMV. For eligible capital property, the transfer price can be any amount between:

- its FMV; and
- $4/3 \times$ your cumulative eligible capital property from the farming business \times $\frac{\text{FMV of the property}}{\text{FMV of all your eligible capital property from the farming business}}$

Example

Wade wants to transfer these farm properties to Vicky, his 19-year-old daughter.

Land

ACB	\$ 85,000
FMV at the time of transfer	\$ 100,000

Combine

FMV	\$ 9,000
UCC at the time of transfer	\$ 7,840

Therefore, Wade can transfer:

- the land at any amount between \$85,000 (ACB) and \$100,000 (FMV); and
- the combine at any amount between \$7,840 (UCC) and \$9,000 (FMV).

If Wade chooses to transfer the land at its ACB and the combine at its UCC, he postpones any taxable capital gain and any recapture of CCA. Also, if he does this, we consider that Vicky acquires the land at \$85,000 and the combine at \$7,840. When Vicky disposes of the land and the combine, she includes in her income any taxable capital gain and recapture that Wade postpones.

For more details and information about transfers of eligible capital property, see Interpretation Bulletin IT-268, *Inter Vivos Transfer of Farm Property to Child*, and its Special Release.

Transfer of farm property to a child if a parent dies in the year

We allow a tax-free transfer of a deceased taxpayer's Canadian farm property to a child if **all** of these conditions are met:

- The child was resident in Canada just before the parent's death.
- The property was used mainly in a farming business on a regular and ongoing basis by the deceased, the deceased's spouse or common-law partner, or any of the children before the parent's death.
- The property was transferred to the child no later than 36 months after the parent's death. In some cases, we may allow the transfer even if it took place later than 36 months after the parent's death.

The following types of farm property qualify for this transfer:

- land and buildings, or other depreciable property used in a farming business; and
- a share of the capital stock of a family-farm corporation, and an interest in a family-farm partnership, if the child was resident in Canada just before the parent's death and the property transfers to the child no later than 36 months after the parent's death. In some cases, we may allow the transfer even if it took place later than 36 months after the parent's death.

For most property, the transfer price can be any amount between the ACB and its FMV.

For depreciable property, the transfer price can be an amount between the property's FMV and a special amount. For more information, see Chapter 4, "Deemed Disposition of Property," in the *Preparing Returns for Deceased Persons* guide.

The deceased's legal representative will choose the amount in the year of death. We consider the child to acquire these properties at the amount chosen.

Similar rules also apply for property that a deceased person leased to the family-farm corporation or partnership.

If a child gets a farm from a parent and the child later dies, the property can be transferred to the surviving parent based on the same rules.

Shares or other property of a family-farm holding corporation can also be transferred, based on the same rules, from a spouse or common-law partner trust to a child of the settlor. The settlor is the person who sets up a trust, or the person who transfers property to a trust.

For more details on these transfers, see Interpretation Bulletin IT-349, *Intergenerational Transfers of Farm Property on Death*.

Transfer of farm property to a spouse or common-law partner

A farmer can transfer farm property to a spouse or common-law partner or to a spousal or common-law partner trust during the farmer's lifetime. At the time of the transfer, the farmer can postpone any taxable capital gain or recapture of CCA.

If the spouse or common-law partner later disposes of the property, the farmer generally has to report any taxable capital gain, not the spouse or common-law partner. This rule applies to transfers made after 1971 where the farmer is living at the time the spouse or common-law partner sells the property. However, there are exceptions to this rule. For more details, see Interpretation Bulletin IT-511, *Interspousal and Certain Other Transfers and Loans of Property*.

A transfer of farm property can also occur after the farmer dies. For more information, see Chapter 4, "Deemed Disposition of Property" in the *Preparing Returns for Deceased Persons* guide.

The rollover provisions available for farm property are now extended to land and depreciable property used principally in a woodlot farming business. They will apply where the deceased, the deceased's spouse or common-law partner, or any of the deceased's children was engaged in the woodlot operation as required by a **prescribed forest management plan** in respect of the woodlot. These provisions apply to transfers of property that occur after December 10, 2001.

Other special rules

You may also be able to postpone paying tax on capital gains in the following situations.

Reserves

When you dispose of a capital property, you usually receive full payment at that time. However, sometimes you receive the amount over a number of years. Generally, a reserve allows you to defer reporting part of the capital gain to the year in which you receive the proceeds. For example, you may sell a capital property for \$50,000 and receive \$10,000 at the time of the sale. You receive the remaining \$40,000 over four years. In this situation, you can claim a reserve. However, there is a limit to the number of years you can do this. For more information on reserves, see the *Capital Gains* guide and Form T2017, *Summary of Reserves on Dispositions of Capital Property*.

Exchanges or expropriations of property

There are special rules that apply when you dispose of a property and replace it with a similar one, or when someone expropriates your property. For more details, see Interpretation Bulletin IT-259, *Exchanges of Property*. You may also want to see Interpretation Bulletin IT-491, *Former Business Property*, and its Special Release.

Capital Cost Allowance (CCA) Rates

In this list, you will find the more common depreciable properties a farming business may use. The CCA rates appear at the end of the list. For details on the CCA rates for classes 13, 14, 34, 43.1, and Part XVII of the *Income Tax Act*, call us at 1-800-959-5525.

Depreciable property	Class No.	Depreciable property	Class No.
Aircraft – Acquired before May 26, 1976	16	Harrows.....	8
Aircraft – Acquired after May 25, 1976	9	Hay balers and stookers	
Automobiles	10	Drawn	8
Bee equipment	8	Self-propelled	10
Boats and component parts	7	Hay loaders.....	8
Breakwaters		Ice machines.....	8
Cement or stone.....	3	Incubators.....	8
Wood	6	Irrigation equipment – Overhead	8
Brooders.....	8	Irrigation ponds	6
Buildings and component parts		Leasehold interest.....	13
Wood, galvanized, or portable.....	6	Manure spreaders.....	8
Other:		Milking machines	8
Acquired after 1978 and before 1988*	3	Mixers	8
Acquired after 1987	1	Mowers.....	8
Fruit and vegetable storage (after Feb. 19, 1973).....	8	Nets	8
Casing, cribwork for waterwells.....	8	Office equipment	8
Chain-saws	10	Outboard motors	10
Cleaners – grain or seed	8	Passenger vehicles (see Chapter 3)	10 or 10.1
Combines		Piping – Permanent	2
Drawn.....	8	Planters – All types.....	8
Self-propelled.....	10	Ploughs	8
Computer hardware and systems software.....	10	Pumps.....	8
Coolers – Milk	8	Rakes.....	8
Cream separators.....	8	Roads or other surface areas – Paved or concrete.....	17
Cultivators	8	Silo fillers.....	8
Dams		Silos	8
Cement, stone, wood, or earth	1	Sleighs.....	10
Diggers – All types	8	Sprayers.....	8
Discs.....	8	Stable cleaners	8
Docks	3	Stalk cutters.....	8
Drills – All types	8	Swathers	
Dugouts, dikes, and lagoons	6	Drawn	8
Electric-generating equipment - portable		Self-propelled	10
Acquired after May 25, 1976.....	8	Threshers.....	8
Electric motors	8	Tile or concrete drainage system – Acquired before 1965	13
Elevators	8	Tillers – All types	8
Engines – Stationary	8	Tools	
Fences – All types.....	6	Less than \$200.....	12
Forage harvesters		\$200 and more	8
Drawn.....	8	Tractors.....	10
Self-propelled.....	10	Trailers.....	10
Graders – Fruit or vegetable.....	8	Trucks	10
Grain-drying equipment.....	8	Trucks (freight).....	16
Grain loaders	8	Wagons.....	10
Grain separators	8	Water towers	6
Grain-storage building		Weeders.....	8
Wood, galvanized steel	6	Welding equipment.....	8
Other.....	1	Well equipment	8
Greenhouses (all except as noted below)	6	Wharves	
Greenhouses of rigid frames covered with replaceable		Cement, steel, or stone	3
flexible plastic (this applies to taxation years after		Wood.....	6
1988 for greenhouses acquired after 1987).....	8	Windchargers	8
Grinder.....	8	Wind-energy conversion equipment	
Harness.....	10	acquired before February 22, 1994	34
		acquired after February 21, 1994	43.1

* You may add to or alter a class 3 building after 1987. In this case, there is a limit on the amount you can include in class 3. The most you can include in class 3 is the lower of \$500,000 or 25% of the building's cost on December 31, 1987. In class 1, include any costs you incur that are over this limit.

Rates	
Class 1	4%
Class 2	6%
Class 3	5%
Class 6	10%
Class 7	15%
Class 8	20%
Class 9	25%

Rates	
Class 10	30%
Class 10.1	30%
Class 12	100%
Class 16	40%
Class 17	8%
Class 45	45%
Class 46	30%

How to Calculate the Mandatory Inventory Adjustment (MIA)

For instructions on how to complete the following charts, see page 24 and Chapter 2.

Chart 1	
Cash cost of purchased inventory	
Enter the amount you paid by the end of the 2004 fiscal period for the specified animals you bought:	
Fiscal period	Cash cost
■ in your 2004 fiscal period	\$ _____ A
■ in your 2003 fiscal period	\$ _____ B
■ in your 2002 fiscal period	\$ _____ C
■ in your 2001 fiscal period	\$ _____ D
■ before your 2001 fiscal period	\$ _____ E
Enter the amount you paid by the end of your 2004 fiscal period for all other inventory you bought:	
■ in your 2004 fiscal period	\$ _____ F
■ in your 2003 fiscal period	\$ _____ G
■ in your 2002 fiscal period	\$ _____ H
■ in your 2001 fiscal period	\$ _____ I
■ before your 2001 fiscal period	\$ _____ J

Chart 3	
Value of purchased inventory for all other inventory	
Inventory bought in your 2004 fiscal period	
Enter the amount on line F or the fair market value, whichever is less.	\$ _____ P
Inventory bought in your 2003 fiscal period	
Enter the amount on line G or the fair market value, whichever is less.	\$ _____ Q
Inventory bought in your 2002 fiscal period	
Enter the amount on line H or the fair market value, whichever is less.	\$ _____ R
Inventory bought in your 2001 fiscal period	
Enter the amount on line I or the fair market value, whichever is less.	\$ _____ S
Inventory bought before your 2001 fiscal period	
Enter the amount on line J or the fair market value, whichever is less.	\$ _____ T

Chart 2	
Value of purchased inventory for specified animals	
Inventory bought in your 2004 fiscal period	
Enter an amount that is not more than the amount on line A, but not less than 70% of this amount.	\$ _____ K
Inventory bought in your 2003 fiscal period	
Enter an amount that is not more than the amount on line B, but not less than 70% of the total of the value at the end of your 2003 fiscal period plus any amounts you paid in your 2004 fiscal period toward the purchase price.	\$ _____ L
Inventory bought in your 2002 fiscal period	
Enter an amount that is not more than the amount on line C, but not less than 70% of the total of the value at the end of your 2003 fiscal period plus any amounts you paid in your 2004 fiscal period toward the purchase price.	\$ _____ M
Inventory bought in your 2001 fiscal period	
Enter an amount that is not more than the amount on line D, but not less than 70% of the total of the value at the end of your 2003 fiscal period plus any amounts you paid in your 2004 fiscal period toward the purchase price.	\$ _____ N
Inventory bought before your 2001 fiscal period	
Enter an amount that is not more than the amount on line E, but not less than 70% of the total of the value at the end of your 2003 fiscal period plus any amounts you paid in your 2004 fiscal period toward the purchase price.	\$ _____ O

Chart 4	
Calculation of MIA	
Enter the amount of your net loss from line 9899 of Form T2042.	\$ _____ U
Enter the value of your inventory from Chart 2 and Chart 3:	
■ the amount on line K	\$ _____
■ the amount on line L	\$ _____
■ the amount on line M	\$ _____
■ the amount on line N	\$ _____
■ the amount on line O	\$ _____
■ the amount on line P	\$ _____
■ the amount on line Q	\$ _____
■ the amount on line R	\$ _____
■ the amount on line S	\$ _____
■ the amount on line T	\$ _____
Total value of inventory	\$ _____ \$ _____ V
MIA – enter the amount on line U or line V, whichever is less.	\$ _____ W

GST/HST Rates

Farm goods and services **taxable** at 7% GST or 15% HST include:

- crop dusting;
- contract work, including field clearing, tilling, and harvesting done by one farmer on behalf of another;
- road-clearing services;
- stud or artificial insemination services;
- storing goods (for example, storing grain in a grain elevator);
- beeswax;
- maple sugar candy;
- canary seed, lawn seed, and flower seed;
- bedding plants, sod, cut flowers, living trees, and firewood;
- furs, animal hides, and dead animals not suitable for human consumption;
- fertilizer in bulk quantities of less than 500 kilograms, or any quantities of soil or soil mixture whether or not they contain fertilizer;
- gravel, stones, rock, soil, and soil additives;
- livestock or poultry not normally raised as food or to produce food for human consumption (for example, horses, mules, rabbits, exhibition poultry, and mink); and
- processed wool, feathers, and down.

Many farm products and purchases, such as milk sales and feeder-cattle purchases, are taxable, but at 0%. We refer to these as zero-rated goods. You do not pay GST/HST when you buy these products and you do not charge GST/HST when you sell them to your customers.

Zero-rated farm products are:

- fruit and vegetables;
- grains or seeds in their natural state, treated for seeding purposes or irradiated for storage purposes, and hay or silage, or other fodder crops, when they are sold in quantities larger than ordinarily offered for sale to consumers, **except** grains and seeds sold to use as feed for wild birds or pet food;
- feed sold by a feedlot operator, as long as the price is separately identified on the invoice or written agreement;
- hops, barley, flax seed, straw, sugar cane, or sugar beets;
- livestock such as cattle, hogs, poultry, bees or sheep that are raised or kept to produce food, or to be used as food, for human consumption, or to produce wool;
- poultry or fish eggs that are produced for hatching;
- rabbits, except those that are to be sold as pets;
- fertilizer sold in individual bags of at least 25 kg when the total quantity is at least 500 kg;
- wool that is not further processed than washed; and

- tobacco leaves that are not further processed than dried and sorted.

Zero-rated farm purchases are:

- large farm tractors (60 PTO horsepower and over);
- pull and self-propelled combines, swathers, and wind-rowers;
- headers for combines, forage harvesters, swathers or wind-rowers;
- combine or forage harvester pickups;
- forage harvesters, and self-propelled, tractor-mounted, or pull-type mechanical fruit or vegetable pickers or harvesters;
- mouldboard and disc ploughs (3 or more furrows), and chisel ploughs and subsoil chisels (at least 8 feet or 2.44 metres);
- discers, rod weeders, or bean rods (at least 8 feet or 2.44 metres);
- field and row crop cultivators (at least 8 feet or 2.44 metres);
- combination discer-cultivators (at least 8 feet or 2.44 metres);
- rototillers and rotavators (at least 6 feet or 1.83 metres);
- harrows sold in complete units and pulverizers (at least 8 feet or 2.44 metres);
- land packers, mulchers, and rotary hoes (at least 8 feet or 2.44 metres);
- airflow seeders, grain and seed drills (at least 8 feet or 2.44 metres), and farm-type row-crop or toolbar seeders or planters designed to seed two or more rows at a time;
- mower conditioners, hay balers, hay cubers, hay rakes, hay conditioners, hay crushers, hay crimpers, hay tedders, swath turners, and wind-row turners;
- bale throwers, elevators, or conveyors, silage baggers, and round bale wrapping machines;
- grain bins or tanks with capacity of 181 m³ or less (5,000 bushels);
- transportable grain augers, utility augers, elevators, and transportable conveyors with belts less than 76.2 cm (30 inches) wide and 0.48 cm (3/16 inch) thick;
- bin sweep or cleaner attachments for portable grain augers;
- tractor-powered pneumatic grain conveyors;
- feed mills, including roller mills and hammer mills;
- feed mixers, grinders, grinder mixers, and tub grinders;
- ensilage mixers and self-propelled feed or ensilage carts;
- grain toasters to use in livestock feed production;
- grain dryers;

- farm bulk milk coolers;
- assembled and fully operational milking systems or individual components of these systems;
- automated and computerized farm livestock or poultry feeding systems, or individual components of these systems;
- self-propelled, tractor-mounted, or pull-type agricultural wagons or trailers designed for off-road handling and transporting of grain, forage, livestock feed, or fertilizer, and to be used at speeds not exceeding 40 km per hour;
- mechanical rock or stone pickers, rock or root rakes, and rock or root wind-rowers, forage blowers, silo unloaders, and shredders with an operational width of at least 3.66 m or 12 feet;
- tractor-mounted, self-propelled, or pull-type field sprayers with tank capacities of at least 300 litres or 66 gallons;
- granular fertilizer or pesticide applicators with operational capacity of at least 0.2265 m³ or 8 cubic feet;
- liquid box, tank, or flail manure spreaders, and injection systems for liquid manure spreaders;
- leaf-cutter bees;
- complete feeds, supplements, micro-premixes, macro-premixes, and mineral feeds other than trace mineral salt feeds, labelled in accordance with the *Feeds Regulations*, and designed for rabbits or a specific type of farm livestock, fish, or poultry ordinarily raised or kept for human consumption or to produce wool, and sold in 20 kg or more bulk quantities or bags;
- feed sold in 20 kg or more bulk quantities or bags designed for ostriches, rheas, emus, or bees;

- food processing by-products sold in 20 kg or more bulk quantities or bags used as feed or as ingredients in feed for farm livestock, fish, or poultry that is ordinarily raised or kept for human consumption or to produce wool, or for rabbits, ostriches, rheas, emus, or bees;
- pesticides used for agricultural purposes labelled by the *Pest Control Products Regulations* and not designed for domestic use;
- sales of quotas between farmers for zero-rated products (including dairy, turkey, chicken, eggs, and tobacco leaves); and
- farmland rented to a registrant under a sharecropping arrangement where a share of the production that is zero-rated is part of the price (any other extra payments are taxable).

GST/HST registrants can claim an **input tax credit** for the GST/HST they paid or owe for expenses used to provide taxable goods and services at the rates of 0%, 7%, and 15%.

A limited number of goods and services you purchase are exempt from GST/HST. Because you do not pay GST/HST on these goods and services, there is no input tax credit to claim.

Examples of **exempt** goods and services include:

- insurance services sold by insurance companies, agents, or brokers;
- most services provided by financial institutions, such as arranging loans or mortgages; and
- most health, medical, and dental services.

For more information about GST/HST, see our guide called *General Information for GST/HST Registrants*.

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Your opinion counts!

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