

Family Farms

Changes are proposed to broaden the special rules that permit the tax to be deferred on a transfer of farm property by a farmer to his children. This is generally referred to as a tax-free rollover and now applies only to the transfer of farmland and depreciable farm property owned by a farmer. It will be made to apply to an incorporated family farm effective immediately.

The rollover will cover transfers to children of shares in qualifying farm corporations and of interests in qualifying farm partnerships. To qualify, the farm corporation or partnership must be carrying on a farming business in Canada, substantially all of its assets must be used in the business and one or more members of the farmer's family must be actively engaged in running the farm. The rollover will also be extended to cover transfers of agricultural quotas.

Family Law Reform

Several provinces are enacting important basic changes in their laws relating to the division of certain properties between parties to a marriage. In some provinces the new laws for the division of property will apply to all married couples, while in others they will relate to property division only in the case of a marriage breakdown.

Although property law is a field entirely within provincial jurisdiction, these changes affecting marital properties give rise to a problem in the application of federal Income Tax Act provisions relating to capital gains.

Technical changes will be made to the Income Tax Act to facilitate the division of property between spouses without incurring a capital gains tax liability. No tax would arise on the original transfer. On a subsequent sale of the property, each spouse would report an equal share of any capital gain.

An example would be a cottage (other than a principal residence) originally bought by a husband in Ontario for \$10,000 and valued at \$25,000 at the time of a divorce or legal separation. Under the existing Income Tax Act, the husband would be deemed to have disposed of a one-half interest in the property. The difference between the fair market value of his half-interest (\$12,500) and his cost thereof (\$5,000) would represent a capital gain of \$7,500 and the husband would be liable to tax on half of that amount. Since the taxpayer's wife would not have paid anything for her interest in the property, she would have no cost. This means that on a later sale of the property, she would be required to treat her full share of the proceeds as a capital gain and would be required to bring one-half the proceeds into her income.

The change proposed ensures that a capital gain will not arise on the division of the property. The husband will be deemed to transfer his half-interest in the cottage for \$5,000. On any subsequent sale of the property, both the husband and wife would include one-half the gain in income.