

Accounting and Tax for Agriculture – How to Get the Best Bang for Your Buck!

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INTRODUCTION

Accounting and tax for agricultural operations is an ever changing and dynamic field where planning can not only achieve a more static and consistent tax bill and operational picture, but can often leave you wondering where you left your crystal ball. The environment in which agriculture plays in is no doubt one of the most volatile industries in the world. As advisors, we daily try to help our clients plan for a change in commodity prices, the weather, the world market, but even more important, their own operations' future. We are asking if any of your kids are interested in joining the operation, if you trust that they have learned enough over the years that they can handle the job, if you're ready to retire, and if so, do you have enough cash saved up to do so. We are asking not only how your operation did this year, but what do you expect to change in the future? Can your answers help us to keep your tax bill from making your heart race as much as that hail cloud a week before harvest or that snow storm right before calving?

The intent of this discussion is to provide the reader with some additional insight into common accounting and tax applications that we as business advisors often look at in terms of proactive planning, which may not be as common to the general producer.

ACCOUNTING

When we record income for accounting purposes, we generally try to match it to the relating expense in order to get a true picture of the operation. We often do this by recording accrual adjustments such as prepaid expenses, accounts receivable, and accounts payable. This is known as accrual accounting. Farmers and fishermen have an exemption where they are allowed to file their tax returns on a cash basis , thus being given the advantage to defer income to the subsequent year in order to stay into a desired tax bracket, or purchase subsequent year inputs before year-end to help manage tax liabilities. Essentially recording income and expenses when cash is received and paid.

Income

The income that one would record in their records and tax returns would at first glance expect to be self explanatory, but there are some items that may surprise you:

- If you have a company that holds your operations, inventory, and machinery, but the land is owned personally in order to be able to use the capital gains exemption on sale or death, surface lease, pipeline, windmill, and power line income should really be recorded on your personal tax return.
- Often grain farmers look at deferring grain cheques into the new year in order to help manage their current year tax, but many livestock producers think that the same thing can apply to them by simply asking the auction mart to send them their calf cheque after year-

end. Unfortunately the Income Tax Act is quite clear on the fact that a dealer is an agent of the seller and as a result the rancher must include the sale in income when the purchaser pays the dealer. This is when the risks and rewards of ownership of the cattle have transferred from the seller to the purchaser. (*Income Tax Rulings 2000-0005677 – Sale of Cattle at Auction – 28(1)*)

- Cash advances in the eyes of CRA are considered to be loans, and thus the revenue does not need to be reported until the commodity is actually sold. At that time, the net cheque plus the amount of the advance repaid must be included in income.

Expenses

A few items with respect to agricultural expenses seem to be at the top of auditor and producer minds alike. Some examples follow:

- It's common for farm families to all work together, and a common question that often comes up is how much can I pay my kids or spouse? (*2014 Edition for 2013 Returns Preparing Your Income Tax Returns, Wolters Kluwer Ltd. CCH S1710*) states that payments can be made if the following provisions are met:
 - They were actually paid during the year;
 - They were for services necessary to earn income from the business; and
 - The amount is reasonable, considering the age of the child and the amount you would pay to an outside employee for the same work

It's noted that income tax and CPP remittances and the filing of a T4 information return should be considered. It has been a common audit area for CRA to challenge if deductions are not remitted, even if the child or spouse reports the income on a business schedule.

- Many producers like to think of their workers as casual labourers, but to determine if CRA would see it the same way, if your workers would be considered employees and source deductions required, or contractors under CRA's *Guide, RC4110* www.cra-arc.gc.ca/E/pub/tg/rc4110/rc4110-13e.pdf its often helpful to think of how you would treat your plumber (contractor);
 - How much control do you have over your worker? If a plumber was called they would tell you what day they would be at your house and at what time. The customer does not cover their sick days or medical benefits.
 - Who owns the tools? A plumber would generally bring their own.
 - How much chance of profit and risk of loss do they have? Plumbers cover their own operating costs and live with the fact that there may not be steady income month to month. If they can't make it to an appointment on a specific day they may also send someone else to take their place.