Wealth Management

the Navigator

INVESTMENT, TAX AND LIFESTYLE PERSPECTIVES FROM RBC WEALTH MANAGEMENT SERVICES

Transferring securities in a loss position to and from your corporation

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When you and your corporation transfer or sell property to each other, the transfer or sale may give rise to a capital loss. There are tax rules, known as the "stop-loss" rules (which include the "superficial loss" rules) that can prevent you or your corporation from claiming this capital loss. These rules apply when the transfer is considered to be made without any real intention of disposing of the property. The purpose of this article is to provide a general overview of the stop-loss rules so you are aware of the limitations of transferring or selling property at a loss between you and your corporation.

For the purposes of this article, any reference to a spouse includes a common-law partner.

Superficial loss rules

The superficial loss rules apply when you or an affiliated person transfer property (for example, shares of a corporation or mutual funds) in a loss position to a corporation that you control. Affiliated persons include you, your spouse, a corporation controlled by you and/or your spouse, and a trust where you and/or your spouse are majority interest beneficiaries. The rules prohibit you from claiming a capital loss where all of the following occurs:

- You dispose of your property;
- Your corporation acquires the same property or an identical property (either one referred to as "substituted property") during the period that begins 30 calendar days before and ends 30 calendar days after your disposition; and
- Your corporation owns or has a right to buy the substituted property on the 30th calendar day after the disposition.

If the superficial loss rules apply, your capital loss is denied and is added to the adjusted cost base (ACB) of the substituted property owned by your corporation. When your corporation eventually disposes of the substituted property to a non-affiliated person, it will realize a smaller capital gain or larger capital loss due to the increased ACB. P

If your corporation has realized capital gains, you may want to take advantage of the superficial loss rules in order to transfer capital losses to your corporation and use them to offset the realized gains. For example: Suppose you previously acquired XYZ shares for $100. The shares are now worth $75 and you decide to transfer these shares to your corporation. If your corporation holds the XYZ shares for 30 days, the $25 capital loss realized when you transferred these shares to your corporation will be denied under the superficial loss rules and instead added to the corporation's ACB of these shares. This will result in an ACB of $100 ($75 + $25). If your corporation then sells the XYZ shares on the open market for $75, your corporation will realize a $25 capital loss. Your corporation can then use this capital loss to offset any capital gains it has realized in the current tax year. Unused capital losses can be carried back three years or carried forward indefinitely if not used in the current tax year.

For more information on the superficial loss rules, please ask your RBC advisor for the article on that topic.

Stop-loss rules

The stop-loss rules apply when your corporation transfers property in a loss position to you, the controlling shareholder, or to an affiliated person, and you or the affiliated person hold the substituted property on the 30th calendar day after the transfer. If the stop-loss rules apply, instead of adding the corporation's denied loss to the ACB of the substituted property, the loss is suspended (unavailable for use) in the corporation until the time you or the affiliated person dispose of the substituted property to a non-affiliated party. (This assumes neither you, nor an affiliated person acquires the substituted property in the 30 calendar days before and after the disposition and still holds the substituted property on the 30th day after the disposition.) At that time, your corporation will realize the loss. It is important to note that neither you nor the affiliated person can claim this loss. Only your corporation can claim the loss.

Example

Suppose your corporation previously acquired XYZ shares for $100. The shares are now worth $75 and your corporation transfers the XYZ shares to you, the controlling shareholder. If you hold onto these shares for 30 calendar days, your corporation is not permitted to claim the $25 capital loss at the time of the transfer; the loss is suspended in the corporation. If you later dispose of the XYZ shares on the open market for $90, you will realize a capital gain of $15 ($90 – $75). At that time, your corporation can realize the suspended capital loss of $25 ($100 – $75).

Conclusion

If it makes sense for you to trigger capital losses by transferring property between you and your corporation, it is crucial to ensure you are aware of the superficial and stop-loss rules that might prevent you from claiming the tax benefit associated with the loss. If you have any questions or require clarification of these rules, speak to a qualified tax advisor.

This article may contain strategies, not all of which will apply to your particular financial circumstances. The information in this article is not intended to provide legal, tax or insurance advice. To ensure that your own circumstances have been properly considered and that action is taken based on the latest information available, you should obtain professional advice from a qualified tax, legal and/or insurance advisor before acting on any of the information in this article.

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