

Capitalizing on capital losses

If you or your spouse has realized capital gains in the last three years, consider selling an investment that has dropped in value to recover the taxes paid on those gains.

Stock market declines and volatility experienced during the past couple of years have caused investors to worry about their investments. Many want to take action and reorganize their portfolios, despite being in a loss position. Once the decision is made to crystallize losses, our capitalizing on capital losses strategy can be used to gain maximum tax benefit on portfolio losses. This strategy is based on carrying back any losses that exceed current year capital gains, to a previous year with net capital gains.

An in-depth look at the issue ... and the opportunities

The Income Tax Act requires capital losses to be first applied against capital gains realized in the current year. If there is any remaining balance, the net capital losses can be used to either reduce taxable capital gains in any of the three preceding years, or in any other future year. The best strategy is to carry the losses back to the earliest year in which you have capital gains before it falls out of the three year window. For example, the earliest date allowed to carry back 2004 losses is 2001.

Transferring capital losses between spouses

If you don't have capital gains this year or the previous three years, but your spouse or common-law partner does, it is possible to transfer capital losses to these individuals. First, the investment is sold to crystallize the capital loss. Immediately afterwards the spouse or common-law partner buys the exact same amount of the identical investment. The spouse or common-law partner then sells the investment after waiting at least 31 days. The capital loss realized on your sale will be denied under the superficial loss rules and instead added to your spouse or common-law partner's adjusted cost base, thereby transferring the capital loss.

Tip

Property that sold for a loss cannot be repurchased within 30 days. Where this occurs, the loss will be denied under the superficial loss rules.

John has a net capital loss of \$20,000 realized this year that he either carries back to a previous year or transfers to his spouse. Here's how the tax savings stack up.

Type of Income	(50% inclusion rate)
Loss amount	\$20,000
Tax savings at a 46% marginal tax rate (loss amount X inclusion rate X .46)	\$4,600

Carrying back John's loss to a previous year or transferring them to his spouse results in a recovery of \$4,600 in taxes previously paid.

Investment options with Manulife investments

Manulife and its subsidiaries provide a range of investments and services including:

- Manulife GIF & GIF *encore* funds combine the growth potential offered by over 60 top-ranked investment funds, with the unique wealth protection features of an insurance contract. Through Manulife GIF & GIF *encore*, investors can limit their exposure to risk through death and maturity guarantees, potential creditor protection features, and the estate planning benefits – all from a single investment. For conservative investors looking to grow their wealth but who are also concerned about minimizing risk, GIF & GIF *encore* provide an ideal solution.
- The Manulife Investments GIC offers competitive rates plus investment options that include Basic, Escalating Rate and Laddered GIC Accounts.

Ideal candidates

Investors who:

- Are selling their investments at a loss, and who have little or no capital gains in the current year, and
- Had capital gains, or their spouse or common-law partner had capital gains, in the past three years.

Take action

To apply for a loss carryback, investors need to:

- Complete Area III of Form T1A, Request for Loss Carryback, and
- Attach it to this year's return

Canada Revenue Agency (CRA) will then automatically apply the losses to the previous year(s) requested on the form.