

# 'Tis the Season to Review your Tax Strategy

By Tyler Simms  
Investment Associate

As the end of 2011 draws near, we remind investors to consider any tax-loss strategies in their portfolios. To ensure any loss is available for use now, trade settlement must take place in 2011, meaning trades must be effected no later than December 23rd.

While hardly festive, tax-loss selling is always a popular activity leading up to the holiday season. Here, we share the key considerations for investors when contemplating tax loss selling.

## The Rules

### *No Capital Gains on Tax-Deferred Investments*

Investors typically invest in stocks, bonds, and mutual funds across several types of accounts including tax sheltered accounts such as RRSPs, LIRAs, RRIFs and TFSAs. As a reminder, taxable gains – and tax deductible losses – apply only to holdings in taxable investment accounts and therefore tax sheltered accounts are not affected.

### *Using Realized Losses*

The Canada Revenue Agency (CRA) rules provides for flexible usage of tax losses. Capital losses may be applied to offset both concurrent gains, as well as those incurred in three preceding years (ie. 2008, 2009, 2010). Capital losses can also be carried forward indefinitely providing for future buffer against taxable gains. It should be noted that losses must first be used against gains in the current tax year before they can be carried back or forward.

When it comes to tax loss strategies, good recordkeeping is always beneficial particularly for investors holding investments across multiple accounts and with various financial institutions. By maintaining a record of portfolio transactions you will be better positioned to employ tax loss strategies in a timely fashion across your different accounts each year.

### *The ‘Superficial Loss’ Rule*

There are certain nuances to CRA rules that taxpayers will want to be aware of. A “superficial loss” is deemed to occur if, during the thirty days prior to, or after the disposition date, the taxpayer or related party purchases the same asset. In other words, during the 30 day period preceding the tax loss sale, and for the following 30 day period (a period of 61 days in total), the sold security cannot be purchased. In such instances, the loss would be deemed superficial and not allowed for tax loss purposes. Additionally, the taxpayer (or related party) cannot own a right to acquire the security (ie. call option) at the end of the sixty one day period for the purposes of the superficial loss rule.

### *Transfers to Tax Sheltered Accounts*

While it may seem convenient to simply transfer an investment with an accrued loss to your RRSP or TFSA and realize a capital loss, this is specifically not allowed under CRA rules without actually selling the investment.

Instead, investors can simply sell the investment and realize the accrued loss and contribute the cash proceeds into an RRSP or TFSA. Once the thirty day superficial loss period has expired, you can then reacquire the investment.

### *Working Around the ‘Superficial Loss’ Rule*

Investors may want to crystallize losses on their investments but aren't willing to lose market exposure for 30 days as a consequence of the superficial loss rule. One strategy for consideration is to reinvest the proceeds of a capital loss sale into a highly correlated asset with similar underlying risk characteristics. For example, selling Royal Bank of Canada and concurrently buying Bank of Nova Scotia would allow for you to claim the loss and maintain the desired market exposure. Alternatively, Exchange Traded Funds (ETFs) can be

employed in a similar fashion - the iShares Financials Index ETF, of which RBC makes up nearly 20% of the index, would be an easy way to regain exposure to the Canadian Banking sector.

### ***Bottom Line***

As a principle, tax efficiency should come second to investment strategy when contemplating significant changes to your portfolio. In other words, we don't advise selling securities in loss positions simply for the benefit of a tax benefit. Rather, investors should consider the investment's fundamentals, the impact on their asset allocation and portfolio risk profile before pulling the trigger on a sale.

If you're interested in discussing tax loss strategies for your portfolio, we extend an invitation to you to consult with one of our Portfolio Managers, at no obligation. We would be happy to assist you at 403-234-6118 or [ctsang@mcleanpartners.com](mailto:ctsang@mcleanpartners.com).

---

*McLean & Partners provides independent research and advice to its clients on a fee for service basis. The company is not engaged in any investment banking, underwriting, consulting or financial services activities on behalf of any companies. McLean & Partners' research reports are for the sole purpose of managing client portfolios on a managed and non-managed basis. The company may engage in proprietary trading to invest surplus corporate cash balances. The opinions expressed herein are those of the author and do not necessarily represent those of McLean & Partners Wealth Management Ltd. The information contained in this report has been obtained from sources believed to be reliable, however, we cannot represent that it is accurate or complete. McLean & Partners Wealth Management Ltd. is a member of the Canadian Investor Protection Fund and the Investment Industry Regulatory Organization of Canada.*

