Tax Planning in a Down Market – Seize the Opportunities

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In these difficult times, where asset values may be depressed, there may be some planning opportunities that you can take advantage of in order to free up some cash flow or reduce future taxes payable.

A. Crystallize (Not Cut!) Your Losses

Consider triggering unrealized capital losses to recover tax paid on capital gains in the three previous taxation years. This can be accomplished by selling the assets within the family group if you still want to own the asset. Alternatively, you can sell assets (like securities) in the market and reinvest the proceeds in other securities that you feel may be a bargain. Any loss not used in the current year can be carried back up to three taxation years (it can be carried forward too) to reduce or eliminate previously realized gains and net you a refund of previously paid tax. Anti-avoidance rules can apply to this strategy so if you are considering triggering losses, please contact a member of our Tax Group or your accountant. If your loss is in a corporation, you may want to pay out previously undistributed realized capital gains (e.g. capital dividends) before you trigger your capital loss. We can also provide guidance if you have gains in one corporation in your group and losses in another.

B. Freeze (or Re-Freeze!)

The recent decline in asset values may have widened the window of opportunity to effect a freeze or re-freeze. A freeze is usually done to reduce taxes owing at death or multiply the lifetime capital gains exemption. A freeze shifts the *future* growth in value of an asset you own to another person or group of persons, like family members. The family business is the most common candidate, but most any valuable asset can be frozen. The value of your interest is “frozen” as at the time of the freeze so that any future increase in value accrues to the other person or group of persons, often through a trust. If you have already completed a freeze, then you may wish to revisit the current value of your frozen interest – it may be *less* than its stated value. In that case, you might “re-freeze” the asset so as to reset its value down to current levels.

C. Purifications May Be Inexpensive

The lifetime capital gains exemption exempts from tax approximately $866,000 of a capital gain realized by an individual on the sale of shares of a qualifying small business corporation. A number of conditions must be met. One of those conditions is that 90% or more of the corporation’s assets at the time of the sale must be attributable to assets used principally in an active business carried on primarily in Canada (active business assets). Securities, passive rental properties, cash (other than cash needed for working capital or to meet debt covenants, etc.), do not generally qualify as active business assets. Since this 90% test must be met at the time of sale, you can take steps to extract non-qualifying assets (or “purify” the corporation) in anticipation of a sale. Consider whether it might be a good time to effect a purification on a pre-emptive basis while asset values (and the tax cost associated with the purification) might be low.

For further information regarding any of the foregoing strategies, please contact a member of our Tax Group.

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