Revenue Canada Taxation

Revenu Canada Impôt

**Supplementary Guide**

# Capital Gains Tax Guide

1992

Your Guide

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# What You Need to Know Before You Start

## Is this guide for you?

This guide is for you if you had a capital gain or a capital loss in 1992. You generally have a capital gain or loss whenever you dispose of capital property. Capital property is defined in Chapter 1 on page 7. This guide will show you how to calculate this type of gain or loss. It will also show you how to calculate your capital gains deduction.

Use Schedule 3, *Summary of Dispositions of Capital Property in 1992*, to record your capital gain or capital loss. This schedule is included with your *General Tax Guide* and return package.

## Do you need any other forms or publications?

This guide has copies of some of the forms you may have to complete. You can find them at the back of this guide. We also refer to other forms and publications that give you more detailed information on different subjects. As you read this guide, list the forms and publications you need on the order form on the back cover. Then take or mail the form to your district taxation office. You can also call the "Request for Forms" telephone number that was included with your *General Tax Guide*. When requesting a publication, always ask for the most current version.

## Do you need to read all of this guide?

You may not need to read all of this guide to report your capital gains and capital losses. You should look through the table of contents before you start filling in your return. It will help you choose the chapters or sections that apply to your tax situation. In addition, refer to Chapter 1 for the definitions of terms used in this guide.

# What's New for 1992?

Outlined below are the major changes we have made to this guide. For more details on all changes for 1992, see the areas highlighted in yellow.

## Form T657, *Calculation of Capital Gains Deduction for 1992 on All Capital Property*

If you disposed of qualified farm property or qualified small business corporation shares in 1992 or a prior year, you are eligible to claim a lifetime capital gains deduction of $500,000. To calculate your deduction, you need to complete form T657. We no longer include this form with this guide. If you disposed of this type of property, you can get this form from your district office. It has the information you need to calculate your deduction.

## Capital gains deduction

We have made it simpler for certain individuals to claim the capital gains deduction. You may be able to claim this deduction without completing any forms at all. Please refer to line 254 in your *General Tax Guide* for more information.

## Proposed changes

This guide includes tax changes announced by the Minister of Finance. These had not become law at the time of printing. However, we are getting ready to apply them.

**Capital gains deduction** — Legislation is proposed to exclude all or part of a capital gain or loss that results from the disposition of real estate from the calculation of the capital gains deduction. This change applies to certain real estate disposed of after February 1992. This change will also affect the calculation of your cumulative net investment loss. For more details, see Chapter 5 in this guide.

This guide uses plain language to explain the most common tax situations. If you need more help after reading this guide, please contact your district taxation office.

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# Introduction

This section has general information you need to know before you start to calculate your capital gain or capital loss.

## Did you sell personal-use property or your home?

Most people are not affected by capital gains rules because the property they own is for their own personal use or enjoyment. When you sell personal-use property such as cars and boats, generally you do not end up with a capital gain because this type of property usually does not increase in value over the years. As a result, you may end up with a loss. Although you have to report a gain on the sale of personal-use property, generally you are not allowed to claim a loss. The rules for personal-use property are explained on page 14 in Chapter 2 of this guide.

If you sell your home for more than what it cost you, you generally do not have to report the sale on your tax return or pay tax on any gain as long as:

- your home is your principal residence; and
- you did not designate any other house as your principal residence while you owned your home. For more information, see Chapter 7.

## Do you have a capital transaction or an income transaction?

**You have to know the answer to this question before you can continue in this guide.** If you sell a property and end up with a gain or a loss, it may be taxed in one of two ways:

- as a **capital** gain or loss (capital transaction); or
- as an **income** gain or loss (income transaction).

If you dispose of a property, you need to find out if the transaction is a capital transaction or an income transaction. The facts surrounding the transaction determine the nature of the gain or loss.

If you would like more information on the difference between capital and income transactions, get a copy of the following Interpretation Bulletins:

- IT-459, *Adventure or Concern in the Nature of Trade*
- IT-218, *Profit, Capital Gains and Losses from the Sale of Real Estate, Including Farmland and Inherited Land and Conversion of Real Estate from Capital Property to Inventory and Vice Versa*
- IT-479 and Special Release, *Transactions in Securities*

The information in the rest of this guide deals with capital transactions. Therefore, if you have an income transaction, you **do not** have to read any further in this guide. If you have an income transaction, get a copy of the *Business and Professional Income Tax Guide*.

## When do you have a capital gain or a capital loss?

Usually, you have a capital gain or capital loss when you sell or are considered to have sold a capital property. The following are examples of cases where you are considered to have sold capital property:

- you exchange one property for another;
- you give property (other than cash) as a gift;
- you convert shares or other securities in your name;
- you settle or cancel a debt owed to you;
- you transfer certain property to a trust;
- your property is expropriated;
- your property is stolen;
- your property is destroyed;
- an option that you hold to buy or sell property expires;
- a corporation redeems or cancels shares or other securities that you hold.*

* If a corporation redeems shares that you hold, you will usually have a deemed dividend. The amount of the dividend will be shown on a T5 slip.

There are other situations when you are considered to have sold a capital property even though there is no change in the property's ownership. This can happen if:

- you change the property's use (see Chapter 7);
- you leave Canada (see Chapter 8); or
- the owner dies (see the *Guide for Preparing T1 Returns for Deceased Persons*).

## When do you report a capital gain or a capital loss?

When you sell or are considered to have sold a capital property, you have to report the sale in the year that it takes place.

You may not have to pay tax for 1992, however, you still have to file a return:

- when you sell, or are considered to have sold, any capital property in 1992 (whether or not the sale results in a capital gain or capital loss); or
- to report the taxable part of any capital gains reserve you deducted in 1991 (see Chapter 6).

**Tax Tip**

If you want to claim the capital gains deduction, you must file your 1992 return on or before April 30, 1994. For more information about the capital gains deduction, see Chapter 5.

### Do you own a business?

If you own a business that has a fiscal year-end other than December 31, you still report the sale of a capital property in the calendar year the sale takes place.

**Example**

Nadia owns a construction firm. The fiscal year-end for her business is June 30, 1992. In November of 1992, she sold a capital property that she used in her business. As a result of the sale, she had a capital gain. Nadia has to report the capital gain on her income tax return for 1992. She does this even though the sale took place after her business' fiscal year-end date of June 30.

### Are you a member of a partnership?

If you are, it is possible that your partnership has a fiscal year-end other than December 31. If the partnership sells capital property during its fiscal year, report your share of any capital gain or capital loss in the year in which the partnership's fiscal year ends. Do not report the gain or loss in the calendar year the sale took place.

## How do you calculate a capital gain or a capital loss?

If you sold capital property in 1992, you will need to know the following three amounts to calculate any capital gain or capital loss:

- the proceeds of disposition;
- the adjusted cost base (ACB); and
- the outlays and expenses you incurred when selling your property.

To calculate your capital gain, subtract the ACB of your property from the proceeds of disposition. From this new amount, subtract any outlays and expenses not already included in your ACB.

## How do you report a capital gain or a capital loss?

Use Schedule 3, *Summary of Dispositions of Capital Property in 1992*, to calculate and report all of your taxable capital gains or allowable capital losses. Do not include any capital gains or capital losses in your business or property income, even if you used the property for your business. See Chapters 2 and 3 for information on how to complete Schedule 3.

You may have deducted a reserve in an earlier year, or you may be deducting a reserve in 1992. If either one of these apply to you, fill in Form T2017, *Summary of Reserves on Dispositions of Capital Property*. For more information on reserves, see Chapter 6.

## Did you sell capital property in 1992 that you owned before 1972?

If you did, you have to apply a special set of rules when calculating your capital gain or capital loss. You have to use these special rules because you did not have to pay tax on capital gains before 1972. If you would like more information, you can get the following Interpretation Bulletins (ITs):

- **Shares** — IT-78, *Capital Property Owned on December 31, 1971 — Identical Properties*
- **Median rule** — IT-84, *Capital Property Owned on December 31, 1971 — Median Rule (Tax-Free Zone)*
- **Election** — IT-139, *Capital Property Owned on December 31, 1971 — Fair Market Value*
- **Special situations** — IT-217 and Special Release, *Capital Property Owned on December 31, 1971 — Depreciable Property*

## What forms are in this guide?

Besides Schedule 3, there are several other forms that you may need. This guide has two copies of each form listed in the following section. Use one as a working copy and keep it for your records. Include the other form with your return.

- **Form T1A — *Request for Loss Carry-Back*** — Use this form to request a loss carry-back. See Chapter 4 for more information.
- **Form T657A — *Calculation of Capital Gains Deduction for 1992 on Other Capital Property*** — This form will help you calculate your capital gains deduction. See Chapter 5 for information on how to fill in this form.
- **Form T936 — *Calculation of Cumulative Net Investment Loss (CNIL) to December 31, 1992*** — Use this form to calculate your CNIL to December 31, 1992. See Chapter 5 for more information.
- **Form T2017 — *Summary of Reserves on Dispositions of Capital Property*** — Use this form to deduct a capital gains reserve in 1992. You also use it to include a reserve deducted in 1991 in your capital gains for 1992. See Chapter 6 for more information.

## What records do you have to keep?

You will need the information from your records or vouchers to calculate your capital gains or capital losses for the year. You do not need to include these documents with your return as proof of any sale or purchase of capital property. However, it is important that you keep these documents in case we ask to see them later.

If you have investment income or expenses, make sure you keep a record of these amounts. You will need them to calculate your CNIL when you calculate your capital gains deduction. We explain the CNIL in Chapter 5.

In addition, it is a good idea to keep a record of the fair market value of the property on the date you:

- inherit it;
- receive it as a gift; or
- change its use.

If you need more detailed information on keeping records, get Information Circular 78-10, *Books and Records Retention/Destruction*.

# Chapter 1
# Definitions

**Adjusted cost base** — This is usually the cost of your property plus any expenses you incurred to acquire it. These expenses may include commissions and legal fees. The cost of a capital property is its actual or deemed cost depending on the type of property and how you acquired it.

You have to adjust the cost of your property to include capital expenditures such as the cost of additions and improvements to the property. You cannot add current expenses such as maintenance and repair costs to the cost base of a property. If you would like more detailed information on the difference between capital expenditures and current expenses, get Interpretation Bulletin IT-128, *Capital Cost Allowance — Depreciable Property*. For more information on additions to, and deductions from, the cost of a property, get Interpretation Bulletin IT-456 and Special Release, *Capital Property — Some Adjustments to Cost Base*.

In some cases, special rules may apply so that the cost of a property is considered to be an amount other than its actual cost. For instance, when you inherit or receive property as a gift, you are considered to have acquired the property at its fair market value on the date you acquired it. Similarly, when you win property as a prize from a lottery scheme, you are considered to have acquired the prize at its fair market value at that time. If you would like more information, get Interpretation Bulletin IT-213, *Prizes from Lottery Schemes, Pool System Betting and Giveaway Contests*.

**Allowable capital loss** — This is the amount of your capital loss that you are entitled to deduct. For 1987 and previous taxation years, the allowable portion was **one-half** of your capital loss. For 1988 and 1989, the allowable portion was **two-thirds**. For 1990, 1991 and 1992 the allowable portion is **three-quarters**.

**Arm's length transaction** — This is a term used to describe a transaction between unrelated parties. Each party acts in his or her own self interest. Related persons are not considered to deal with each other at arm's length. Related persons include individuals connected by blood relationship, marriage, or adoption, such as a husband and wife, or a father and son. Also, a corporation and a shareholder who controls the corporation are related.

Unrelated parties may not be dealing with each other at arm's length if, for instance, one is under the influence or control of the other. If you would like more information on this, see Interpretation Bulletin IT-419 and Special Release, *Meaning of Arm's Length*.

**Business investment loss** — This is a capital loss that results from the actual or deemed disposition of certain capital properties. It can happen when you sell one of the following to a person you deal with at arm's length:

- a share of a **small business corporation**; or
- a debt owed to you by a **small business corporation**.

For business investment loss purposes, a small business corporation includes a corporation that was a small business corporation at any time during the 12 months before the disposition.

You may incur such a loss if you are deemed to have disposed of, for nil proceeds of disposition, a debt or share of a small business corporation under any of the following circumstances:

- A small business corporation owes you a debt (other than a debt from the sale of personal-use property), that is considered to be a bad debt at the end of the year.
- You own a share (other than a share for personal-use property) of a small business corporation that at the end of the year:
  - has gone bankrupt in the year;
  - is insolvent and a winding-up order has been made under the *Winding-up Act*; or
  - is insolvent at the end of the year and neither the corporation, nor a corporation it controls, carries on a business. Also, at that time, the shares in the corporation have a fair market value of zero, and it is reasonable to expect that the corporation will be dissolved or wound-up and will not commence to carry on business. You must elect in your return to be deemed to have sold the shares in the corporation for nil proceeds of disposition, and to have reacquired the shares immediately thereafter at a cost equal to nil.

You or a person that you do not deal with at arm's length will be deemed to have realized an offsetting capital gain if the corporation, or a corporation it controls, carries on business within 24 months following the end of the year in which the disposition occurred. You report the capital gain in the taxation year the corporation commences to carry on business. The above applies if you or the person own the shares in the corporation at the time the business is commenced.

If you would like more information about business investment losses, see page 20 in Chapter 4. You can also get Interpretation Bulletin IT-484, *Business Investment Losses*.

**Canadian-controlled private corporation** — This is a private Canadian corporation that is not controlled directly or indirectly in any way by:

- one or more non-resident persons;
- one or more public corporations (other than a prescribed venture capital corporation); or
- any combination of the above.

For more information, get Interpretation Bulletin IT-458, *Canadian-Controlled Private Corporation*.

**Canadian security** — A Canadian security is:

- a share of a corporation that is resident in Canada; or
- a unit of a mutual fund trust, or a bond, debenture, bill, note, mortgage, or similar obligation issued by a person resident in Canada.

Prescribed securities are not considered to be Canadian securities.

**Capital cost allowance** — This is a tax term for depreciation. In the year you buy a depreciable property, such as a building, you cannot deduct the full cost. However, since this type of property wears out or becomes obsolete over time, you can deduct a part of its cost each year, for a period of several years. The deduction for this is referred to as capital cost allowance.

**Capital gain** — You have a capital gain when you sell, or are considered to have sold, a capital property for **more** than its adjusted cost base plus the expenses or outlays incurred to sell the property. A capital gain is the difference between your proceeds of disposition and its adjusted cost base less the expenses or outlays incurred to sell the property.

**Capital loss** — You have a capital loss when you sell, or are considered to have sold, a capital property for **less** than its adjusted cost base and the expenses or outlays of selling the property. The capital loss is the difference between the adjusted cost base of the property before you sold it, and your proceeds of disposition less any expenses or outlays of selling the property.

**Capital property** — This is any property which, if sold, would result in a capital gain or capital loss and includes depreciable property. You usually buy it for investment purposes or to earn income. Some common types of capital property include:

- your cottage;
- securities, such as stocks and bonds; or
- land, buildings, and equipment that you use in a business or a rental operation.

Capital property **does not** include the trading assets of a business, such as stock or inventory.

Special rules apply when you sell certain types of property. These types of property include:

- insurance policies;
- Canadian resource properties;
- cultural properties given to designated institutions (see page 19 in Chapter 3);
- eligible capital properties (see page 17 in Chapter 3);
- foreign resource properties;
- depreciable properties sold at a loss (see page 11 in Chapter 2); and
- timber resource properties.

If you would like detailed information on resource properties, get Interpretation Bulletin IT-125, *Dispositions of Resource Properties*.

**Cumulative net investment loss (CNIL)** — This is an amount by which:

- the total of your investment expenses for each year after 1987; is more than
- the total of your investment income for each year after 1987.

You use your CNIL when you calculate your capital gains deduction. See Chapter 5 for more information.

**Deemed acquisition** — This term is used when you are considered to have acquired property, even though you did not actually buy it.

**Deemed disposition** — This term is used when you are considered to have disposed of property, even though you did not actually sell it.

**Deemed proceeds of disposition** — This term is used when you are considered to have received an amount for property, even though you did not actually receive any funds.

**Depreciable property** — This is usually capital property used to earn income from a business or property. The cost can be written off as capital cost allowance over a number of years. Capital cost allowance is defined on this page.

**Disposition (dispose of)** — This is usually an event or transaction where you give up possession, control, and all other aspects of property ownership.

**Employees' stock options** — This is an option that a corporation grants to an employee. By using this option, the employee can buy the corporation's shares, or the shares of a corporation with which it does not deal at arm's length, for a price that may be less than the fair market value.

**Fair market value** — This is the highest dollar value that you can get for your property in an open and unrestricted market.

**Listed personal property** — This refers to the following personal-use properties that normally increase in value:

- prints, etchings, drawings, paintings, sculptures, or other similar works of art;
- jewellery;
- rare folios, rare manuscripts, or rare books;
- stamps; or
- coins.

You can determine the value of many of these items by consulting with art, coin, jewellery, and stamp dealers. You can also refer to these dealers' catalogues. All or any part of such property, any interest in it, or any right to it, is considered to be listed personal property.

**Net capital loss** — If your allowable capital loss is more than your taxable capital gain, the difference between the two is your net capital loss for the year. How net capital losses are applied is explained in more detail in Chapter 4 on page 23.

**Non-arm's length transaction** — This is a transaction between people who were not dealing with each other at arm's length at the time of the transaction. Please see the definition of "arm's length transaction" earlier in this chapter.

**Outlays and expenses** — These are amounts that you incurred to sell a capital property. You can deduct outlays and expenses from your proceeds of disposition. These types of expenses include:

- fixing-up expenses
- finders' fees
- commissions

- brokers' fees
- surveyors' fees
- legal fees
- transfer taxes
- advertising costs

You cannot reduce your other income by claiming a deduction for these outlays and expenses. Instead, use them to reduce your capital gain or increase your capital loss.

**Personal-use property** — This refers to items that you own primarily for the personal use or enjoyment of your family and yourself. It includes all personal and household items such as furniture, automobiles, boats, and other similar properties.

**Prescribed security** — This is not considered to be a Canadian security. A prescribed security generally includes:

- a share of a corporation (other than a public corporation) whose value, at the time you dispose of it, comes mainly from real estate, resource properties, or both;
- a bond, debenture, bill, note, mortgage, hypothec, or similar obligation of a corporation (other than a public corporation) that you do not deal with at arm's length at any time before you dispose of the security;
- a share, bond, debenture, bill, note, mortgage, hypothec, or similar obligation you acquire from a person with whom you do not deal at arm's length.

**Proceeds of disposition** — This is usually the amount that you received or will receive for your property. In most cases, it refers to the sale price of the property. This could include compensation you received for property that has been destroyed, expropriated, or stolen.

**Qualified farm property** — This is property that you or your spouse own. It is also a family farm partnership in which you or your spouse hold an interest. Qualified farm property includes:

- A share of the capital stock of a family farm corporation.
- An interest in a family farm partnership.
- Real property such as land and buildings.
- Eligible capital property such as milk and egg quotas.

Real property or eligible capital property is qualified farm property only if it is used to carry on a farm business in Canada by any **one** of the following:

- You, your spouse, any of your parents or children. We define children below.
- A family farm corporation where any of the above individuals own a share of the corporation.
- A family farm partnership where any of the above individuals own an interest in the partnership.

Your children include:

- your natural child, adopted child, or step-child;
- your grandchild or great-grandchild;
- your son-in-law or daughter-in-law; or
- a person who, while under 19, was in your custody and control and was wholly dependent on you for support.

You may have bought eligible capital property before June 18, 1987. We will consider that you are using this property to carry on a farm business in Canada as long as **one** of these conditions are met:

- In the year you sell the property, either you, a partnership, or a family farm corporation used the property, or any replacement property, to carry on a farm business in Canada.
- Either you or a family farm partnership referred to above owned the property and used it to carry on a farm business in Canada for at least five years.

If you buy real or eligible capital property at any time, we will consider that you are using the property to carry on a farm business in Canada, as long as certain conditions are met. If throughout the 24 months before the sale, the property is owned by you, your spouse, any of your children, parents, or a family farm partnership in which any of these individuals owned an interest, and:

- the individual referred to above used the property or a replacement property in a farm business in Canada, and in at least two years the individual's gross income from the farm business was larger than the individual's income from all other sources in the year; or
- a family farm partnership or family farm corporation used the property to carry on a farm business in Canada throughout a period of at least 24 months, and during this time any individual referred to above was actively engaged in the farm business.

**Qualified small business corporation shares** — See the definition for "Small business corporation" in this chapter.

**Real property** — This is property that cannot be moved, such as land or buildings. We commonly refer to such property as real estate.

**Small business corporation** — This is a Canadian-controlled private corporation in which the fair market value of all or most (90% or more) of its assets are:

- used mainly in an active business, carried on primarily in Canada by the corporation or by a related corporation;
- shares or debts of connected corporations that were small business corporations; or
- a combination of these two types of assets.

A share of a corporation is considered to be a **qualified small business corporation share** if:

- at the time of sale, it was a share of the capital stock of a small business corporation, and it was owned by you, your spouse, or a partnership of which you were a member;
- throughout the 24 months immediately before the share was disposed of, no one other than you, a partnership of which you were a member, or a person related to you, owned the share*; and
- throughout that part of the 24 months immediately before the share was disposed of, while the share was owned by you, a partnership of which you were a member, or a person related to you, it was a share of a Canadian-controlled private corporation of which the fair market value of more than 50% of the assets were:

- used mainly in an active business carried on primarily in Canada by the Canadian-controlled private corporation, or by a related corporation;
- certain shares or debts of connected corporations; or
- a combination of these two types of assets.

* As a general rule, when a corporation issues shares to a person, or a partnership related to that person after June 13, 1988, a special situation exists. We consider the shares to have been owned, immediately before they were issued, by a person who was **not** related to the individual or the partnership. As a result, to meet the holding-period requirement, the individual, or a person or partnership related to the individual cannot dispose of the shares for 24 months after they were issued. However, this rule does not apply to shares issued:

- as payment for other shares; or
- in connection with a property that a person or the members of that partnership disposed of to a corporation. The property disposed of has to consist of either:
  - all or most (90% or more) of the assets used in an active business operated by that person or by the members of that partnership; or
  - an interest in a partnership where all or most (90% or more) of the partnership's assets were used in an active business operated by the members of the partnership.

**Taxable capital gain** — This is the amount of your capital gain that you have to report as income on your return. For 1987 and previous taxation years, the taxable part of a capital gain was **one-half**. For 1988 and 1989, the taxable part was **two-thirds**. For 1990, 1991 and 1992, the taxable part is **three-quarters**.

**Terminal loss** — This type of loss occurs when you have an undepreciated balance in a class of depreciable property at the end of the taxation year or fiscal year-end, and you no longer own any property in that class. You can deduct the terminal loss when you calculate your income for the year.

**Undepreciated capital cost** — Generally, it is equal to the total capital cost of all the property of a class, less the proceeds of disposition when the property is disposed of, minus the total deductions for capital cost allowance claimed in prior years.

# Chapter 2
# Common Transactions

This chapter gives you information about some of the most common capital gains transactions. It also provides information about where you should report the sale of a capital property on Schedule 3, *Summary of Dispositions of Capital Property in 1992*. You can find this schedule in your *General Tax Guide* and return package.

## Information slips

### T3 slip

**Box 21 — Capital Gains** — You may receive a T3 information slip with an amount in this box. If there is no asterisk (*) in this box, enter the amount on line 533 of Schedule 3.

If there is an asterisk in this box, you should have received instructions with your slip, telling you where to report the amount on Schedule 3. You either enter the amount on line 513, qualified small business corporation shares, or on line 516, qualified farm property. The reason for this, is that these types of property are eligible for a higher capital gains deduction. We explain the capital gains deduction in Chapter 5.

**Box 30 — Capital Gains Eligible for Deduction** — If there is an amount in box 21, there must also be an amount in this box. If the amount is not the same as the amount in box 21, you have to enter the difference on line 536 of Schedule 3. This will help you calculate your capital gains deduction and your cumulative net investment loss. We explain this later in Chapter 5.

**Example**
Janet received a T3 slip with $500 in box 21 and $300 in box 30. Since there was no asterisk in box 21, she entered $500 on line 533 of Schedule 3. Because the amount in box 30 was less than the amount in box 21, she entered the difference between the two amounts ($200) on line 536 of Schedule 3.

**Note**
If box 30 has "nil", a zero, or a dash (–), no amount of your capital gain is eligible for the deduction. If there is no entry in box 30, contact the issuer for an amended slip.

**Box 37 — Insurance Segregated Fund Losses** — If there is an amount in this box, enter it on line 533 of Schedule 3. This amount is a loss, so if it is your only entry, put brackets around the amount. If it is not your only entry, subtract the amount in this box from the total of the amounts indicated on your other slips.

### T4PS slip

**Box 34 — Capital gains (or losses)** — Enter this amount on line 533. If this amount has brackets around it, it is a capital loss. If this is your only entry, put brackets around the amount on line 533. If it is not your only entry, subtract the amount in this box from the total of the amounts indicated on your other slips.

**Box 38 — Foreign capital gains (or losses)** — Do not include this amount on your Schedule 3. It is already included in box 34 of your T4PS slip. You enter this amount on line 508 of your Schedule 1 and use it to calculate your foreign tax credit.

**Box 40 — Non-eligible capital gains** — If there is an amount in this box, enter it on line 536 of Schedule 3. This is the amount of your capital gain that is not eligible for the capital gains deduction. You will use this amount to calculate your capital gains deduction and your cumulative net investment loss. We explain this later in Chapter 5. Do not subtract this amount from the amount you have already entered on line 533.

### T5 slip

**Box 18 — Capital Gains Dividends** — Enter this amount on line 533 of Schedule 3.

**Box 24 — Non-eligible portion of box 18** — If there is an amount in this box, enter it on line 536 of Schedule 3. This is the amount of your capital gain that is not eligible for the capital gains deduction. You will use this amount to calculate your capital gains deduction and your cumulative net investment loss. We explain this later in Chapter 5. Do not subtract this amount from the amount you have already entered on line 533.

### T5013 slip

**Box 27 — Capital gains (losses)** — Enter this amount on line 533 of Schedule 3 unless you have received additional details. For instance, the details area of your slip may indicate that your gain is for qualified farm property or qualified small business corporation shares. If this is the case, enter your gain on line 513 or line 516 of Schedule 3.

The details area of your slip could also identify amounts included in box 27 that are not eligible for the capital gains deduction. If this is the case, enter the amount that is not eligible on line 536 of Schedule 3. This will help you calculate your capital gains deduction and cumulative net investment loss. We explain this in Chapter 5.

**Box 28 — Capital gains reserve** — Enter this amount in the appropriate area on Form T2017, *Summary of Reserves on Dispositions of Capital Property*.

You can use Form T2089, *Capital Dispositions Supplementary Schedule Re: Information Slips*, to calculate your gain or loss.

## Real estate and depreciable property

If you sold real estate or depreciable property in 1992, you have to report your capital gain or loss in the section called "Real estate and depreciable property" on Schedule 3.

If you sold real estate after February 1992, there are changes to the way the capital gains deduction is calculated. We explain this in the section "Property disposed of after February 1992" on page 27 in Chapter 5.

### Real estate

A real estate transaction includes the sale of:

- vacant land;

- rental properties — both land and buildings;
- farm property — both land and buildings (other than qualified farm property — see page 18 in Chapter 3); and
- commercial and industrial land and buildings.

Do not use this section of Schedule 3 to report the sale of personal-use property, or the sale of mortgages and other similar debt obligations on real property. You have to report this information on Schedule 3 under "Personal use property," and "Bonds, debentures, promissory notes and other properties."

If you sold real property in 1992 that includes land and a building, you:

- first calculate how much of the selling price is for the land, and how much is for the building; then
- report the sale of your land and building separately on Schedule 3.

If you dispose of a building and end up with a loss, a special rule may apply. Under the rule, you may have to consider your proceeds from the building as an amount other than the actual proceeds. For more information, see the section called "Selling a building in 1992" in this chapter.

To help you calculate your gains or losses from real estate, use Form T2083, *Capital Dispositions Supplementary Schedule Re: Real Estate*. However, do not use this form for your principal residence, depreciable property, or other personal-use property.

### Depreciable property

When you dispose of depreciable property, you may end up with a capital gain or a loss. The loss on the sale of a depreciable property is not considered to be a capital loss. Instead, you may be entitled to claim a terminal loss if you no longer own any property in that class at the end of your fiscal period. Unlike a capital loss, you can deduct the full amount of the terminal loss from your income.

For capital cost allowance (CCA) purposes, depreciable properties are grouped into classes. There are a number of classes for a wide range of depreciable properties. For example, computer hardware and systems software, some automobiles, and certain portable tools are grouped together in Class 10. If you want to know what class your property is in, call your district office.

The beginning undepreciated capital cost (UCC) for a class is the capital cost of the depreciable properties in that class. From this amount you deduct:

- any proceeds that you received from selling property in that class; and
- the CCA deducted over the years.

The remaining amount is your ending UCC. This amount becomes your beginning UCC for the following year.

You subtract from the UCC of the property in that class the lesser of the following two amounts:

- the proceeds of disposition of the property minus the related outlays and expenses; and
- the capital cost of the property.

When you sell a depreciable property for **less** than its original capital cost, but for more than the UCC in the class, you do not have a capital gain. However, if the UCC of a class has a negative balance at the end of the year, the negative balance is considered to be a recapture of CCA. You have to include this recapture in income for that year.

If the UCC of a class has a positive balance at the end of the year, and you do not have any properties left in that class, the positive balance is considered to be a terminal loss. You can deduct the terminal loss from income in that year. However, if the balance for the UCC of a class is zero at the end of the year, then you have neither a recapture of CCA, nor a terminal loss.

The rules for recapture and terminal loss do not apply to passenger vehicles that you included in Class 10.1.

**Example**

In 1986, Stefan bought a piece of machinery for $20,000 for his business. It is the only property in its class at the beginning of 1992. The class has a UCC of $11,000. He sold the piece of machinery in 1992 and purchased no other property in that class. The following chart gives you three different selling prices to show you how Stefan would handle a variety of situations.

| | A | B | C |
|---|---|---|---|
| Cost of properties acquired: | $20,000 | $20,000 | $20,000 |
| **Minus:** CCA 1986-1991: | 9,000 | 9,000 | 9,000 |
| UCC at beginning of 1992: | $11,000 | $11,000 | $11,000 |
| **Minus the lesser of:** | | | |
| - cost — $20,000; and | | | |
| - proceeds of: (A) $ 8,000 | | | |
| (B) $16,000 | | | |
| (C) $24,000 | 8,000 | 16,000 | 20,000 |
| | $ 3,000 | $(5,000) | $(9,000) |
| | **Terminal loss** | **Recapture** | **Recapture** |

In addition to a recapture of $9,000 in example C, there is a capital gain of $4,000.

If you need more information about the recapture of CCA and terminal losses, get Interpretation Bulletin IT-478, *Capital Cost Allowance — Recapture and Terminal Loss*. You can also get the *Business and Professional Income Tax Guide*, or the *Rental Income Tax Guide*.

### Selling a building in 1992

If you sold a building in 1992, and it was the only property in the class, the UCC of the class before the sale is considered to be its **cost amount**.

If there is more than one property in the same class, you have to calculate the cost amount of each building as follows:

$$\frac{\text{Capital cost of the building}}{\text{Capital cost of all properties in the class}} \times \text{UCC of the class} = \text{Cost amount of the building}$$

In certain situations, special rules apply that make the selling price an amount other than the actual selling price. This happens when you meet **both** of the following conditions:

- you, or a person with whom you do not deal at arm's length, own the land on which the building is located, **or** the land adjoining the building, if you need the land so that the building can be used; and
- you sell the building for an amount that is less than both its cost amount (as calculated in the previous formula), and its capital cost to you.

If you sold a building under these conditions the terminal loss on the building would be restricted but the capital gain on the land would be reduced. If you would like more detailed information, get Interpretation Bulletin IT-220, *Capital Cost Allowance — Proceeds of Disposition of Depreciable Property.*

You can use Form T2085, *Capital Dispositions Supplementary Schedule Re: Depreciable Property*, to calculate any capital gain or loss you have when you sell depreciable property.

### Selling part of a property

When you sell only part of a property, you have to divide the adjusted cost base (ACB) of the property between the part you sell and the part you keep.

**Example**
Sophia owns 100 hectares of vacant land. The land is all of equal quality. She decides to sell 25 hectares of this land. Since 25 is one-quarter of 100, Sophia calculates one-quarter of the total ACB as follows:

| | |
|---|---|
| The total ACB ...................... | $100,000 |
| **Minus:** The ACB of the part she sold ... | 25,000 |
| **Equals:** The ACB of the part she kept ... | $ 75,000 |

Sophia then calculates any capital gain or loss using an ACB of $25,000 for the 25 hectares she sold.

If you would like more information, get Interpretation Bulletin IT-264 and Special Release, *Part Dispositions*.

## Canadian securities

You report a disposal of Canadian securities or prescribed securities on Schedule 3 at:

- Line 513 — Qualified small business corporation shares
- Line 516 — Qualified farm property
- Line 520 — Shares
- Line 528 — Bonds, debentures, promissory notes and other properties

Read the information under the applicable headings on pages 12, 14, 17 and 18 to determine where you should report your disposition. Chapter 1 contains the definitions of Canadian securities, prescribed securities, qualified small business corporation shares and qualified farm property.

If you disposed of Canadian securities, there is a special election available to you. You may actually have an **income** gain or loss from the sale of a Canadian security. The special election is available in the year that you dispose of a Canadian security. This election is not available to traders or dealers in securities, or to anyone who was a non-resident of Canada when the security was sold.

You can elect to report your gain or loss as a **capital** gain or loss even though it is actually an income gain or loss. However, from the time you make the election, we will consider all your Canadian securities to be capital properties.

If you are a member of a partnership, and the partnership owns Canadian securities, each partner is treated as owning the security. When the partnership disposes of the security, each partner may elect to treat the security as capital property. An election by one partner will not result in each member of the partnership being treated as having made the election.

If you would like to make this election, fill in Form T123, *Election on Disposition of Canadian Securities*, and attach it to your 1992 return. Please remember that once you make this election, you cannot reverse your decision.

For more information on Canadian securities, get Interpretation Bulletin IT-479 and Special Release, *Transactions in Securities*.

## Other securities and properties

This includes shares, bonds, debentures, promissory notes, and other such properties. If you sold any of these items in 1992, you will receive a T5008, *Statement of Securities Transactions* or an account statement. Report any capital gains and capital losses in the section "Other securities and properties" on Schedule 3. This section is broken down into several subsections so that you can report different securities and properties separately.

### Shares

Use this section to report a gain or loss when you sell shares or securities that are **not** described in any other section of Schedule 3. This includes:

- publicly traded shares;
- shares that qualify as Canadian securities or prescribed securities if they are not qualified small business corporation shares or qualified family farm corporation shares;
- shares issued by foreign corporations; and
- the sale of a unit in a mutual fund trust.

The following section has two examples. They share some common information. They show you two different situations and how you would fill in this part of Schedule 3 for each situation.

## Example 1

In 1992, Franco sold 100 shares of ABC Public Corporation of Canada for $8,500. He received the full proceeds at the time of the sale. He paid brokerage fees of $500. When he bought the shares in 1985 for $3,800, Franco paid brokerage fees of $200.

To fill in Schedule 3, Franco needs to find out three things:

- his proceeds of disposition;
- his adjusted cost base; and
- the amount of any outlays and expenses that relate to the sale.

After he finds out these three amounts, Franco calculates his taxable capital gain as follows:

| | | | |
|---|---|---|---|
| Proceeds of disposition | | | $8,500 |
| **Minus:** The ACB | | | |
| – original cost | $3,800 | | |
| – brokerage fees on purchase | $ 200 | $4,000 | |
| Outlays and expenses (brokerage fees on the sale) | | $ 500 | $4,500 |
| Capital gain | | | $4,000 |
| Taxable capital gain (3/4 × $4,000) | | | $3,000 |

Franco reports the sale under "Shares" in the section "Other securities and properties." He reports his total proceeds on line 519, and his capital gain on line 520.

**Other securities and properties**
Shares

| No. of shares | Name of corporation and class of shares | | | | | | | | Gain (or loss) | |
|---|---|---|---|---|---|---|---|---|---|---|
| *100* | *ABC Public Corporation* | *1985* | *8,500* | *00* | *4,000* | *00* | *500* | *00* | *4,000* | *00* |
| | *of Canada* | | | | | | | | | |
| | | Total proceeds **519** | *8,500* | *00* | | | | Gain (or loss) **520** | *4,000* | *00* |

If Franco has no other capital gains or capital losses in the year, he reports $3,000 (3/4 × $4,000) as his total taxable capital gains amount. He fills in this amount at the bottom of Schedule 3, and again on line 127 of his return. Franco may also be entitled to the capital gains deduction. If you would like more information about this deduction, see Chapter 5.

## Example 2

Using the same situation in Example 1, assume that Franco had sold his shares for only $3,700. As you can see below, Franco ends up with a capital loss of $800. He could use the loss to offset any capital gains he had in 1992. If his capital losses were more than his capital gains in that year, his net capital loss for 1992 would be three-quarters of the difference between the two amounts. For more information about capital losses, see the section "1992 Capital losses" on page 20 in Chapter 4.

**Other securities and properties**
Shares

| No. of shares | Name of corporation and class of shares | | | | | | | | Gain (or loss) | |
|---|---|---|---|---|---|---|---|---|---|---|
| *100* | *ABC Public Corporation* | *1985* | *3,700* | *00* | *4,000* | *00* | *500* | *00* | *(800* | *00)* |
| | *of Canada* | | | | | | | | | |
| | | Total proceeds **519** | *3,700* | *00* | | | | Gain (or loss) **520** | *(800* | *00)* |

You can use Form T2082, *Capital Dispositions Supplementary Schedule Re: Shares*, to help you calculate any gains or losses from the sale of shares.

### Bonds, debentures, promissory notes, and other properties

If you sell any of these types of properties, report the sale on Schedule 3 in the section "Bonds, debentures, promissory notes and other properties." Report the following capital gains and capital losses in this section:

- **Options** — If you would like information on disposing of options to sell or buy shares, get Interpretation Bulletins IT-96, *Options Granted by Corporations to Acquire Shares, Bonds or Debentures*, and IT-479 and Special Release, *Transactions in Securities*;
- **Discounts, premiums, and bonuses** — If, in 1992, you received any of these amounts for investments that you have, you can get Interpretation Bulletin IT-114, *Discounts, Premiums and Bonuses on Debt Obligations*.

You can use Form T2084, *Capital Dispositions Supplementary Schedule Re: Bonds and Other Obligations*, to help you calculate your gains or losses from disposing of bonds, debentures, and promissory notes.

## Treasury bills (T-Bills)

You will receive a T5008, *Statement of Securities Transactions* or an account statement for transactions that took place in 1992. When a T-Bill is issued at a discount and you keep it until it matures, the interest deemed to accrue to you is the difference between the issue price and the amount you cash it in for. However, you may sell the T-Bill before it matures. In this case, in addition to the interest accrued at that time, you may have a capital gain or capital loss.

**Example**
Ralph purchased a T-Bill on December 1, 1991 for $49,000. The date of maturity was March 1, 1992. However, he sold it on February 4, 1992 for $49,500. The effective yield rate was 5.36%.

Ralph calculates interest on the T-Bill as follows:

$$\text{Effective yield rate} \times \frac{\text{Number of days T-Bill held}}{\text{Number of days in the year sold}} \times \text{Purchase price} = \text{Interest to be included in income}$$

$$5.36\% \times \frac{66}{366} \times \$49{,}000 = \$473$$

Ralph calculates his capital gain as follows:

| | |
|---|---|
| Proceeds | $49,500 |
| **Minus:** Interest | $ 473 |
| Net proceeds | $49,027 |
| Adjusted cost base | $49,000 |
| Capital gain | $ 27 |

## Identical properties

Properties of a group are considered to be identical if each property in the group is the same as all the others. The most common example of this is when you have shares of the same class of the capital stock of a corporation.

### Average cost calculation

You may buy and sell several identical properties at different prices over a period of time. If you do this, you have to figure out the average cost of each property in the group at the time of each purchase. This allows you to determine your ACB. You need to know this amount before you can calculate any capital gain or loss.

**Example**
Blake owns 100 common shares of a corporation. He bought these shares for $15 each. He later bought another 150 shares of the same class of that corporation for $20 each. In 1992, he sold 200 of these shares for $24 each.

| | | |
|---|---|---|
| Previously purchased shares: | 100 × $15 = | $1,500 |
| Newly purchased shares: | 150 × $20 = | $3,000 |
| **Total shares:** | 250 **Total cost:** | $4,500 |
| Average cost of each share: | $4,500 ÷ 250 = | $ 18 |
| **Calculation of capital gain** | | |
| Selling price: | (200 × $24) = | $4,800 |
| **Minus:** ACB of shares sold: | (200 × $18) = | $3,600 |
| Capital gain: | | $1,200 |
| Taxable capital gain: | ($1,200 × 3/4) | $ 900 |

You have to calculate the average cost each time you buy another identical property.

**Example**
After selling 200 shares in the corporation, Blake had 50 left (250 − 200). He then bought 350 more shares (which were identical properties) at $21 each. He has to recalculate the average cost of the shares as follows:

| | | |
|---|---|---|
| Cost of previously purchased shares: | 50 × $18 = | $ 900.00 |
| Cost of newly purchased shares: | 350 × $21 = | $7,350.00 |
| **Total shares:** | 400 **Total cost:** | $8,250.00 |
| Average cost of each share (recalculated amount): | $8,250 ÷ 400 = | $ 20.63 |

You should use this same method to calculate the average cost for identical bonds or debentures that you bought after 1971. However, the average cost is based on the principal amount for each identical property.

A bond, debenture, or similar debt obligation that a debtor issues is considered to be identical to another if:

- they are both issued by the same debtor; and
- all the attached rights are the same.

You cannot take the principal amount of individual debt obligations into account when you are figuring out if these properties are identical.

## Personal-use property

When you dispose of a personal-use property, you will end up with a capital gain or a capital loss. To calculate this amount, follow these rules:

- if the ACB of the property is less than $1,000, its ACB is considered to be $1,000;
- if the proceeds of disposition are less than $1,000, the proceeds of disposition are considered to be $1,000; and

- if both the ACB and the proceeds of disposition are $1,000 or less, you do not have a capital gain or capital loss. Do not report the sale on Schedule 3 when you file your return.

When you dispose of personal-use property that has an ACB and proceeds of disposition **over $1,000**, you have to report any capital gain in the section called "Personal-use property" on Schedule 3. However, if you end up with a capital loss, you usually **cannot** deduct that loss when you calculate your income for the year. In addition, you cannot use the loss to decrease capital gains on other personal-use property. However, these restrictions **do not** apply:

- to a bad debt owed to you by a person with whom you deal at arm's length for the sale of personal-use property. For more information, see the section called "Bad debts" on page 17 in Chapter 3; **or**
- if you disposed of listed personal property. Listed personal property is described on page 18 in Chapter 3.

## You were asking...?

Q. In 1992, I sold an old china cabinet for $900. The cabinet didn't cost me anything because my grandmother gave it to me 10 years ago. She had a dealer appraise it at the time, and the cabinet was valued at $500. Do I have to report the gain on my income tax return?

A. No. Since the china cabinet is considered to be a personal-use property, the ACB and the proceeds of disposition are both considered to be $1,000. Therefore, for income tax purposes, there is no gain or loss on the sale of the china cabinet.

### Example

Samir sold his motorcycle in 1992 for $1,200. He bought it in 1983 for $850. The only expense he had in selling the motorcycle was $15 for advertising. Since the ACB of the motorcycle is less than $1,000 ($850), it is considered to have an ACB of $1,000. Although Samir actually had a gain of $335 ($1,200 minus $850 minus $15), the capital gain that he reports is only $185 ($1,200 minus $1,000 minus $15).

**Personal-use property** (full description)

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| *Motorcycle* | *1983* | *1,200* | *00* | *1,000* | *00* | *15* | *00* | *185* | *00* |
| | | | | | | | Gain only **530** | *185* | *00* |

### Example

In 1992, Chelsea sold her lakefront property and cottage to a developer for $100,000. She bought the property in 1981 for $49,000, and built a cottage on it for $30,000 in 1990. Chelsea incurred expenses of $1,000 in connection with the sale of the land and cottage. She paid $9,000 in interest and property taxes during the period she owned the property. In addition, she paid interest on the money she borrowed to buy the property and build the cottage.

When calculating her capital gain on the property and cottage, Chelsea can deduct the $1,000 selling expenses. However, the $9,000 in interest and property taxes is considered to be a personal expense since she was not using the property or cottage to earn income. As a result, Chelsea cannot deduct the $9,000 from her income for any taxation year. She also cannot use it to reduce her capital gain in 1992. In addition, when she calculates the ACB of the property, she cannot add the $9,000 to her original cost of $49,000 for the land.

Therefore, Chelsea has to show the sale of the property in the section called "Personal-use property" on Schedule 3. She uses this schedule to report her capital gain of $20,000 ($100,000 − $49,000 − $30,000 − $1,000 = $20,000).

If Chelsea had designated her cottage as her principal residence, all or part of the capital gain may have been exempted from tax. For more information on designating your principal residence, see Chapter 7.

**Personal-use property** (full description)

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| *Lot 119 – 120, Plan 2750* | *1981* | *100,000* | *00* | *79,000* | *00* | *1,000* | *00* | *20,000* | *00* |
| *City, Province, Country* | | | | | | | Gain only **530** | *20,000* | *00* |

Remember, if you sell personal-use property that is real property, you have to read Chapter 5 to figure out what portion of your gain is not eligible for the capital gains deduction.

If you want information on selling part of a personal-use property or sets of personal-use property, get Interpretation Bulletin IT-332, *Personal-Use Property*.

You can use Form T2080, *Capital Dispositions Supplementary Schedule Re: Personal-Use Property (other than listed personal property and principal residence)*, to calculate any gains or losses you have when you dispose of personal-use property.

## Employees' stock options

When your employer grants you a stock option, there is no immediate effect on your tax situation. A stock option is an **opportunity** to buy stock at a certain price. It only affects your tax situation if you sell the option or exercise that option and actually buy stocks. If you decide to buy stocks, and you buy them at **less-than-market value**, you will have a taxable benefit. The taxable benefit is the difference between what you paid for the stocks, and the higher fair market value at the time you exercised your option. This difference is a taxable benefit received through employment.

You have to include this taxable benefit in your income in the year you acquire the shares. Please note, however, that the amount of the benefit can be reduced by any amount you paid to acquire the stock option. Your employer includes this taxable benefit in boxes 14 and 38 on your T4 Supplementary.

However, if you buy stocks through an employee stock option granted to you by a Canadian-controlled private corporation with which you deal at arm's length, the situation is different. You **do not** include the taxable benefit in your income in the year you acquire the stocks. You wait until the year you **sell** the stocks.

If you meet certain conditions, you may be entitled to claim a special deduction. This deduction is equal to one-quarter of the taxable employee stock option benefit included in your employment income. The amount of the benefit that qualifies for this deduction is shown in the "footnotes" area of your T4 slip. For more information about this deduction, see line 249, "Stock option and shares deductions," in the *General Tax Guide*.

To calculate the ACB of your stocks, add the following two amounts:

- any amount included in your income as an employee stock option benefit; and
- the actual purchase price.

You have to do this even if you claimed a stock option deduction for these stocks.

The taxable benefit included in your income as an employee stock option benefit is **not** eligible for the capital gains deduction.

In the year you exchange or sell the shares that you bought through an employee stock option agreement, report the capital gain or loss on Schedule 3. Depending on your situation, you can either use the section called "Qualified small business corporation shares," or the one called "Other securities and properties." In addition, you may be eligible to claim a capital gains deduction for part, or all, of any taxable capital gain.

For more detailed information, get Interpretation Bulletin IT-113, *Benefits to Employees — Stock Options*.

# Chapter 3
# Other Transactions

We explain some less common capital gains transactions in this chapter. We also explain the special rules for calculating your capital gain or capital loss and where to report the result on your Schedule 3.

## Eligible capital property

If you operate a business, you may buy a property that does not physically exist. Examples of this kind of property are goodwill, customer lists, trademarks, and milk quotas. This kind of property is called eligible capital property.

If you have these types of properties, you may have a taxable capital gain when you dispose of them. Details on what amount will be a capital gain are provided in the:

- *Business and Professional Income Tax Guide;*
- *Farming Income Tax Guide*; or
- *Fishing Income Tax Guide.*

Read the chapter "Eligible Capital Expenditures" in the guide that applies to your type of business. You may also want to read Interpretation Bulletin IT-123, *Disposition of and Transactions Involving Eligible Capital Property.*

A taxable capital gain on eligible capital property that is qualified farm property goes on line 543 of Schedule 3. A taxable capital gain on all other types of eligible capital property goes on line 544 of Schedule 3.

## Mortgages

The person who holds a mortgage on a property is the **mortgagee**. The person who owes the money is the **mortgagor**.

If you are the mortgagee, you may repossess a property when the mortgagor does not pay you the money owed under the terms of the mortgage. If this happens, you are considered to have repurchased the property.

If you are the mortgagor, your property may be repossessed. If this happens, you will be considered to have sold the property.

If you need information on this subject, get Interpretation Bulletin IT-505, *Mortgage Foreclosures and Conditional Sales Repossessions.*

You report any capital gain or capital loss on Schedule 3 in the section called "Bonds, debentures, promissory notes and other properties".

## Bad debts

If a debt is owed to you (other than a debt under a mortgage, or a debt resulting from a conditional sales agreement), and it remains unpaid after you have exhausted all means to collect it, it becomes a bad debt. The debt will be a capital loss if it was incurred:

- to earn income from a business or property; or
- as consideration or payment for the sale of capital property in an arm's length situation.

This loss is equal to the adjusted cost base of the property.

If the amount that you are still owed is from the sale of personal-use property to a person with whom you deal at arm's length, the situation is different. You can claim the capital loss in the year that the debt becomes a bad debt. However, the capital loss cannot be more than the capital gain previously reported on the sale of the property.

There are times when a bad debt involves a **small business corporation**. We explain what to do in this situation under "Allowable business investment losses (ABIL)" on page 20 in Chapter 4.

If you need more detailed information about bad debts, you can get Interpretation Bulletins IT-159, *Capital Debts Established to be Bad Debts*, and IT-239, *Deductibility of Capital Losses from Guaranteeing Loans for Inadequate Consideration and from Loaning Funds at less than a Reasonable Rate of Interest in Non-arm's Length Circumstances.*

## Foreign exchange gains and losses

Foreign exchange gains or losses from capital transactions in foreign currencies are considered to be capital gains or capital losses. However, you only report the amount of your net gain or loss for the year that is **more than $200**. Report this amount on line 528 of Schedule 3. If the net amount is **$200 or less**:

- there is no capital gain or capital loss; and
- you do not have to report it on your tax return.

You can use Form T2087, *Capital Dispositions Supplementary Schedule Re: Foreign Exchange Transactions*, to help you calculate your capital gain or capital loss. If you need more detailed information, get Interpretation Bulletin IT-95, *Foreign Exchange Gains and Losses.*

## Qualified small business corporation shares

If you sell qualified small business corporation shares, report the sale on Schedule 3 in the section, "Qualified small business corporation shares."

**Do not** report the following transactions in this section:

- the sale of other shares such as publicly traded shares, or shares of a foreign corporation; and
- losses you have when you sell any shares of small business corporations to a person with whom you deal at arm's length.

For more information on losses you may have when selling these type of shares, see "Allowable business investment losses (ABIL)" on page 20 in Chapter 4.

If you have a capital gain when you sell qualified small business corporation shares, you are eligible for the $500,000 capital gains deduction. To calculate this deduction, get form T657 from your district office.

## Qualified farm property

Generally, when you dispose of qualified farm property, you report any capital gain or capital loss on Schedule 3 in the section, "Qualified farm property." However, if you have a taxable capital gain from selling eligible capital property that is also qualified farm property, report the gain on line 543 of Schedule 3. For more information, see "Eligible capital property" at the beginning of this chapter.

If you have a capital gain when you sell qualified farm property, you are eligible for the $500,000 capital gains deduction. To calculate this deduction, get form T657 from your district office.

If you dispose of **non-qualified** farm property, report it on Schedule 3 in the section, "Real estate and depreciable property." You can find more details about this section on page 10 in Chapter 2.

## Inheriting property

Generally, when you inherit property from a person, the property's cost to you is the fair market value on the date of that person's death. When you sell the property, you may have a capital gain or capital loss. Property that you inherit as a result of your spouse's death may not be affected by this rule. If you would like more information, see the *Guide for Preparing T1 Returns for Deceased Persons*.

## Listed personal property (LPP)

LPP (defined in Chapter 1) is a type of personal-use property. Therefore, the $1,000 minimum proceeds of disposition and adjusted cost base rules apply. For more information about these rules, see the section called "Personal-use property" on page 14 in Chapter 2.

You report the sale of LPP on Schedule 3 only if you had a capital gain from the sale. If you have LPP losses from a previous year to apply against your 1992 LPP gain, refer to page 21 in Chapter 4 to see how to apply them.

## Common transfers of property

### To persons other than your spouse

If you give capital property as a gift, you are considered to have sold it at its fair market value (FMV) at the time you give the gift. You include any taxable capital gain or allowable capital loss in your income for the year that you gave the gift.

If you receive capital property as a gift, you are considered to have purchased it at its FMV at the time you received it. If you sell the property later, this same purchase price will be your cost when you calculate any capital gain or capital loss for the year.

### To your spouse or a trust for your spouse

If you give capital property to your spouse, or to a trust for your spouse, you generally do not have a capital gain or capital loss at that time. At the time you give the gift, depending on the type of property you give, you are considered to receive an amount equal to:

- the undepreciated capital cost for depreciable property; or
- the adjusted cost base for other types of capital property.

Your spouse, or the trust for your spouse, is considered to have bought the capital property for the same amount that you are considered to have sold it for. If your spouse, or the trust, sells the property during your lifetime, you generally have to report any capital gain or capital loss from the sale.

You will not have to report the capital gain or capital loss when your spouse sells the property if:

- you are not a resident of Canada; or
- you are divorced from your spouse.

If you are living apart because of a marriage breakdown, you may not have to report the capital gain or capital loss when your spouse sells the property. To do this, you must file an election with your tax return.

For transfers of property made after May 22, 1985, you can file this election with your income tax return for any taxation year ending after the time you separated. However, in order for the election to be valid, it must be filed no later than the year your spouse disposes of the property.

For transfers of property made before May 23, 1985, the election must be filed with your income tax return for the taxation year in which the separation occurred.

In both cases, the election must state that you do not want section 74.2 of the *Income Tax Act* to apply. Both you and your spouse must sign the election.

If you sold the property to your spouse or trust, and you were paid an amount equal to the FMV, there is another way to report the sale. You can list the sale at the property's FMV, and report any capital gain or capital loss for the year that you sold the property. You also have to attach a note to your tax return. The note should say that you are reporting the property as being sold to your spouse at FMV.

If your spouse or the trust later sells the property, your spouse or trust has to report any capital gain or loss from the sale.

A special situation exists if all of the following apply to you:

- You owned capital property (other than depreciable property or a partnership interest) on June 18, 1971.
- You give it to your spouse after 1971.
- Your spouse later sells the property.

If you would like information about this situation, get Interpretation Bulletin IT-209, *Inter-Vivos Gifts of Capital Property to Individuals Directly or Through Trusts*.

If you need more detailed information about transferring property to your spouse, get Interpretation Bulletins IT-511, *Interspousal Transfers and Loans of Property made after May 22, 1985*, and IT-258 and Special Release, *Transfer of Property to a Spouse*.

**Tax Tip**

As you read about transfers, remember the capital gains deduction that is explained in Chapter 5. The deduction may be more useful in your situation than any of these transfers.

## Other transfers

If you **sell** property to someone with whom you do not deal at arm's length, and the selling price is **less** than its FMV, your selling price is considered to be the FMV.

Similarly, if you **buy** property from someone with whom you do not deal at arm's length, and the purchase price is **more** than the FMV, your purchase price is considered to be the FMV.

If you would like more detailed information, get Interpretation Bulletin IT-405, *Inadequate Considerations — Acquisitions and Dispositions.*

There are special rules that allow you to transfer property at an amount other than the property's FMV. If these rules apply to your situation, you may be able to postpone paying tax on any capital gains that you realize from the transfer.

### Farms

When you sell or transfer farm property, you may end up with a capital gain. There are many special rules for these types of capital gains. In certain situations, you can transfer farm property to a spouse or child. If you would like more information about these types of transfers, and other rules that apply to farm property, get the *Farming Income Tax Guide.*

### Elections

If you have a capital gain, you may elect to postpone reporting it when you transfer property:

- **from** an individual **to** a corporation (use Form T2057, *Election on Disposition of Property by a Taxpayer to a Taxable Canadian Corporation)*;
- **from** a partnership **to** a corporation (use Form T2058, *Election on Disposition of Property by a Partnership to a Taxable Canadian Corporation)*; or
- **from** an individual **to** a Canadian partnership (use Form T2059, *Election on Disposition of Property by a Taxpayer to a Canadian Partnership).*

If you would like information on making a transfer to a corporation, get Information Circular 76-19, *Transfer of Property to a Corporation under Section 85*, and Interpretation Bulletin IT-291, *Transfer of Property to a Corporation under Subsection 85(1).*

For information on a transfer to a Canadian partnership, get Interpretation Bulletin IT-413, *Election By Members of a Partnership under subsection 97(2).*

## Selling or donating certified Canadian cultural property

You do not have to report a capital gain that you have when you sell or donate Canadian cultural property (national treasures) to an institution or public authority designated by Communications Canada. The Canadian Cultural Property Export Review Board, which operates under Communications Canada, certifies this property as being cultural property and provides certificates for tax purposes.

If you sell or donate certified cultural property to a designated institution, and end up with a capital loss, you can deduct the loss. Please see Chapter 4 for details on how to deduct a capital loss.

If you would like more information, get Interpretation Bulletin IT-407, *Disposition after 1987 of Canadian Cultural Property.*

# Chapter 4
# Capital Losses

## Who should read this chapter?

You should read this chapter if you sold or disposed of any capital property in 1992 or a prior year, and ended up with a capital loss.

## When do you have a capital loss?

You generally have a capital loss when you sell, or are considered to have sold, a capital property for **less** than what it cost you. However, you **cannot** have a capital loss when you dispose of:

- depreciable property (see Chapter 2); or
- personal-use property (see Chapter 2).

If you sold listed personal property and ended up with a loss, see the section called "Listed personal property (LPP) losses" later in this chapter.

## 1992 Capital losses

You can only apply a capital loss against a capital gain. This means that if you had a capital gain in 1992, you can use your capital loss to reduce the amount of the gain.

The amount of your capital loss is further reduced to what we call your **allowable capital loss**. An allowable capital loss is three-quarters of your capital loss.

When your allowable capital losses in 1992 are greater than your taxable capital gains, the difference between the two is your **net capital loss** for 1992. Always report your loss on Schedule 3 and file it with your 1992 return. This is to ensure your losses are on our records should you want to apply the losses to other years.

You can carry your 1992 net capital loss back three years and apply it against your taxable capital gains in any of the those years. For details, see the section "How do you apply a 1992 net capital loss to previous years?" on page 26 in this chapter.

You can also apply your net capital loss against a taxable capital gain in any future year. If you are going to do this, make sure you keep a record of the amount you have available to carry forward. We explain how to apply these losses in the section "How do you apply net capital losses of other years to 1992?" on page 23 in this chapter.

**Example**

In 1992, Sylvana sold some securities that she owned. As a result, she had a capital loss of $800, and a capital gain of $400.

| | |
|---|---|
| Capital loss | $(800) |
| Capital gain | $ 400 |
| Total capital loss | $(400) |
| Allowable capital loss (3/4 × $400) | $(300) |

In Sylvana's case, her allowable capital loss will be her net capital loss. She may apply her net capital loss of $300 against taxable capital gains that she had in any of the three previous years, or in any future year.

**You were asking...?**

Q. I owned some shares in a Canadian public corporation and sold them in 1992 at a loss. I had no capital gains in 1992. How do I show my capital loss on my tax return?

A. You report this loss on Schedule 3. Enter the proceeds of disposition on line 519 of Schedule 3, and enter your capital loss on line 520. Three-quarters of your capital loss is your allowable capital loss for 1992. Since you have no taxable capital gains in 1992, your allowable capital loss becomes a net capital loss for 1992. You cannot deduct the net capital loss in 1992 because you did not have any taxable capital gains. You can, however, carry the loss back three years, or forward to any future year, and apply it against taxable capital gains. Make sure you attach Schedule 3 to your income tax return for 1992, so that we have a record of your loss.

## Allowable business investment loss (ABIL)

If you had a business investment loss (defined in Chapter 1) in 1992, you can deduct three-quarters of the loss from income. We call this amount your ABIL.

You have to reduce your business investment loss by any capital gains deduction you claimed in a previous year. We explain this in the next section, "Reduction in business investment loss."

You can deduct your ABIL from your other sources of income for the year. If your ABIL is more than your other sources of income for the year, include the difference as part of your non-capital loss for 1992. You can carry back a non-capital loss three years and forward seven years.

To carry back a non-capital loss to 1989, 1990 or 1991, complete form T1A and file it with your income tax return for 1992. Do not file an amended income tax return for the year you want the loss applied to. If you want more information on non-capital losses, get Interpretation Bulletin IT-232, *Non-Capital Losses, Net Capital Losses, Restricted Farm Losses, Farm Losses and Limited Partnership Losses — Their Composition and Deductibility in Computing Taxable Income*.

You may not be able to deduct your ABIL as a non-capital loss within the allowed time-frame. The unapplied part becomes a net capital loss in the eighth year. You can then use it to reduce your taxable capital gains in the eighth year or any year after.

For example, let's say you had an ABIL in 1984 that became a non-capital loss. You could not deduct it in the three years before 1984 or the seven years after 1984. The loss then becomes a net capital loss in 1992. You can now use it to reduce your taxable capital gains in 1992 or any year after.

To claim your ABIL, enter the amount of your loss on line 217 of your tax return, and attach a note that states the:

- name of the small business corporation;

- number and class of shares, or the type of debt you disposed of;
- insolvency, bankruptcy, or wind-up date;
- date that you bought the shares, or the date that you acquired the debt;
- amount of the proceeds of disposition;
- adjusted cost base of the shares or debt;
- outlays or expenses on the disposition; and
- amount of the loss.

Any ABIL that you claim for 1992 will reduce the capital gains deduction you are eligible to claim in 1992 and in future years. See Chapter 5 for more information.

### Reduction in business investment loss

If you claimed a capital gains deduction in a previous year, you have to reduce your business investment loss in 1992.

The following chart will help you calculate the reduction. If you had more than one business investment loss in 1992, make sure you calculate each one separately.

Looking at the chart, you will notice that we adjust the amount of the capital gains deductions that you claimed in previous years. We do this because capital gains were included in income at different rates in those years.

| | | | | |
|---|---|---|---|---|
| Total capital gains deductions claimed in 1985, 1986, or 1987 (from line 254 of your 1985, 1986, and 1987 returns) | ________ | × 2 = | ________ | (1) |
| Capital gains deduction claimed in 1988 and 1989 | ________ | × 3/2 = | ________ | (2) |
| Capital gains deduction claimed in 1990 and 1991 | ________ | × 4/3 = | ________ | (3) |
| Line 1 plus lines 2 and 3 | | | ________ | (4) |
| Total amount you used to reduce your business investment losses in 1986 to 1991 (from line 535 of Schedule 3 of your 1986 to 1991 returns) | ________ | (5) | | |
| Total amount already used to reduce any **other** business investment loss in 1992 | ________ | (6) | | |
| Line 5 plus line 6 | | | ________ | (7) |
| Line 4 minus line 7 | | | ________ | (8) |
| Business investment loss for 1992 (before reducing this loss) | | | ________ | (9) |
| **Reduction in a business investment loss for 1992:** Line 8 or line 9, whichever amount is less | | | ________ | (10) |
| **Business investment loss for 1992:** Line 9 minus line 10 | | | ________ | (11) |

The amount from line 10 becomes a capital loss for 1992. Enter this amount on line 535 of Schedule 3. The amount on line 11 is your business investment loss for 1992. Three-quarters of this amount is your ABIL for 1992. Enter this reduced amount on line 217 of your tax return.

## Applying listed personal property (LPP) losses

If you dispose of LPP in 1992, you need to read this section because applying a LPP loss is not the same as applying other capital losses. This is because:

- you can only deduct this loss from any gains you had from selling other LPP;
- the total amount of LPP losses that you deduct in the year cannot be more than the total LPP gains for that year; and
- you cannot use this loss to reduce any capital gains you had from selling other types of property.

To figure out how much of a LPP loss you can apply, you have to calculate each LPP disposition separately.

First, determine if you have any LPP gains in 1992. If you do, check your records to see if you have any unapplied LPP losses from 1985 and later years. If you do, use these losses to reduce your LPP gain in 1992. Do not put these losses on line 253 of your return. Instead, reduce your LPP gain by the amount of the loss. If you have reduced your LPP gain to zero, any loss that is left that has not expired can be carried forward. A LPP loss expires when it is not used in the seventh year after it was incurred.

Now, determine if you have any LPP losses in 1992. If you do, and you still have a LPP gain, use your 1992 LPP losses to reduce as much of your gain as you can. If you have not reduced your gain to zero, enter the remaining gain on line 531 of Schedule 3.

If you still have a 1992 LPP loss left, you can apply this loss against any LPP gain you had in 1989, 1990, or 1991. If you are going to do this, complete form T1A. File one copy with your 1992 tax return. Do not file an amended return for the year you would like the loss applied to.

Remember, only complete the "Listed personal property" area of Schedule 3 if you end up with a gain in 1992. If you do not have a gain, keep a record of your LPP losses so that you can apply these losses against future LPP gains.

**Example**
Marina bought some jewellery in 1981 for $5,800. In 1992, she sold it for $6,000. She ended up with a gain of $200. She also sold a coin collection for $2,000 in 1992. Marina had originally bought this collection in 1985 for $1,700. She ended up with a gain of $300 when she sold the coin collection. In addition, she sold a painting in 1992 for $8,000. However, Marina bought the painting in 1980 for $12,000. Therefore, she had a loss of $4,000. She had no outlays or expenses for these three transactions.

Marina's loss from selling LPP in 1992 was more than her gain: her loss was $4,000, her total gain was $500 ($200 + $300). As a result, her net loss was $3,500 ($4,000 − $500). She cannot use the difference to offset her capital gain on the sale of a property other than on LPP in the year. Nor can she offset any income she had from other sources. However, she can apply her LPP loss against her LPP gains in any of the three previous years, or the seven years following 1992.

To calculate her gains or losses from LPP for 1992, Marina uses Form T2081, *Capital Dispositions Supplementary Schedule Re: Listed Personal Property*. She keeps this form for her own records and she does not complete a Schedule 3 for 1992.

## Superficial losses

A superficial loss can occur when you dispose of capital property and, during the period starting 30 days before the sale, and ending 30 days after the sale, you, your spouse, or a corporation you control directly or indirectly:

- buys the same or identical property (called "substituted property"); and
- still owns the substituted property 30 days after the sale.

If you have a superficial loss in 1992, you cannot deduct it when you calculate your income for the year. However, you may be the person who acquires the substituted property. In this case, you can add the amount of the superficial loss to the adjusted cost base of the substituted property. This will either decrease your capital gain, or increase your capital loss, when you sell the substituted property.

However, this rule **does not apply** if:

- you are considered to have sold the capital property because you ceased to be a resident of Canada;
- the property is considered to have been sold because the owner died;
- the disposition results from the expiry of an option; or
- you are considered to have sold the property because you changed its use.

## Restricted farm losses

You may have restricted farm losses (RFLs) that you incurred in your farming operation that you could not deduct when you calculated your income for previous years. You can apply part of these RFLs against any capital gain that you may have when you sell your farmland. The amount you can apply cannot be more than the total of the property taxes and the interest on money borrowed to buy the farmland. Reduce your capital gain by adding these amounts to the adjusted cost base (ACB) of your farmland. Also reduce your RFL balance by these amounts.

You can only use RFLs to reduce your capital gain to zero. You cannot use this type of loss to create or increase a capital loss from selling farmland.

**Example**
Bob sold his farmland in 1992 for $200,000. The ACB of the property was $160,000. Bob has an unapplied RFL of $20,000 from 1991. This amount includes $5,000 for property taxes, $5,000 for interest, and $10,000 for other expenses.

Bob wants to reduce his capital gain from selling his farmland by applying his RFLs against the capital gain. He calculates his capital gain as follows:

| | | |
|---|---|---|
| Proceeds of disposition: | | $200,000 |
| ACB: | $160,000 | |
| **Plus:** Property taxes: | $ 5,000 | |
| Interest: | $ 5,000 | $170,000 |
| Capital gain: | | $ 30,000 |
| Taxable capital gain ($30,000 × 3/4): | | $ 22,500 |

Bob can only apply the portion of his RFLs that relate to property taxes and interest on the money borrowed to buy the farmland.

If you would like more information, get Interpretation Bulletin IT-232, *Non-Capital Losses, Net Capital Losses, Restricted Farm Losses, Farm Losses and Limited Partnership Losses — Their Composition and Deductibility in Computing Taxable Income*.

## Net capital losses of other years, line 253 — T1 return

Generally, when your allowable capital losses are **more** than your taxable capital gains for a year, the difference is your **net capital loss**. You can carry your net capital loss back three years, and apply it against your net taxable capital gains for those years. You can also carry it forward indefinitely to a future year, and apply it against your taxable capital gains.

**Tax Tip**
If you had a taxable capital gain in 1992, you may decide to take advantage of the capital gains deduction. You can do this instead of using your net capital losses from another year. See Chapter 5 for more information about the capital gains deduction.

The taxable part of a capital gain, and the allowable part of a capital loss, is not the same for every year. We refer to these amounts as their inclusion rate. The inclusion rates are as follows:

- **one-half** for 1987 and years before that;
- **two-thirds** for 1988 and 1989; and
- **three-quarters** for 1990, 1991 and 1992.

Since there are different inclusion rates for certain years, you may have to adjust your net capital loss. You have to adjust your net capital loss when you apply it against a taxable capital gain in a year that has a different inclusion rate.

The following information and charts will help you calculate the adjustment to your net capital loss. You do the adjustment before you apply the loss against your taxable capital gains. Depending on your own individual tax situation, you may or may not have to use all the information and charts.

## How do you apply net capital losses of other years to 1992?

**Make sure you apply net capital losses of earlier years before you apply net capital losses of later years.** For instance, if you have a net capital loss in 1987 and in 1991, and you would like to apply these losses against your taxable capital gains in 1992, you must follow a certain order. First, you apply your 1987 net capital loss against your taxable capital gain, then you apply your 1991 net capital loss against it.

## Applying net capital losses incurred before 1988 to 1992

You may have unapplied net capital losses from before 1988 to apply against your 1992 capital gains. If you do, you have to separate your losses that occurred before May 23, 1985 from your losses that occurred after May 22, 1985. You have to do this because the way you apply these losses is different.

### Net capital losses incurred prior to May 23, 1985

This includes losses incurred after May 22, 1985, according to an agreement you entered into before May 23, 1985. We call this your pre-1986 loss balance.

You can apply your pre-1986 loss balance against all sources of income. Once you have applied your net capital losses against taxable capital gains, you can use the excess to offset other income up to $2,000.

Your **pre-1986 capital loss balance** available for 1992 is:

- the balance of your total **unapplied** net capital losses that you had at any time before May 23, 1985; **minus**
- the total adjusted amount of capital gains deductions that you claimed before 1992.

When you calculate the balance of your unapplied pre-May 23, 1985 net capital losses, remember to reduce the balance by the amount you applied to years before 1992.

If you claimed a capital gains deduction in 1988 and 1989, you have to adjust the deduction to reflect the lower rate for years before 1988.

Use the following chart to calculate your pre-1986 capital loss balance for 1992.

You can use these charts only if you are using your maximum deduction for pre-1986 net capital losses.

**Pre-1986 capital loss balance available for 1992**

Balance of unapplied net capital losses you had before May 23, 1985 . . . $ ______ (1)

Capital gains deductions you claimed:

| | | | |
|---|---|---|---|
| Before 1988 | | | $ ______ |
| In 1988 and 1989 | $ ______ | × 3/4 = | $ ______ |
| In 1990 and 1991 | $ ______ | × 2/3 = | $ ______ |

Total capital gains deductions after adjustment . . . $ ______ (2)

Pre-1986 capital loss balance for 1992: line 1 minus line 2 . . . $ ______ (3)

If you had a net capital loss during the period January 1, 1985 to May 22, 1985, and you had capital gains later in 1985, your capital gains will reduce your pre-1986 capital loss balance. If you would like more information, get Interpretation Bulletin IT-232, *Non-Capital Losses, Net Capital Losses, Restricted Farm Losses, Farm Losses and Limited Partnership Losses — Their Composition and Deductibility in Computing Taxable Income.*

Before you can figure out the amount of your pre-1986 net capital losses that you can apply in 1992, you have to adjust your losses to reflect the higher inclusion rate.

**Pre-1986 adjusted net capital loss balance for 1992**

Unapplied net capital loss from line 1 . . . $ ______ (4)

Adjustment factor . . . × 3/2

Adjusted pre-1986 net capital loss amount . . . $ ______ (5)

Once you have completed these calculations, you can calculate your maximum 1992 deduction. To do this, use the following chart to calculate your maximum 1992 deduction for pre-1986 net capital losses of other years.

**Pre-1986 net capital loss applied in 1992**

Taxable capital gain reported on line 127 . . . $ ______ (6)

Adjusted net capital loss amount from line 5 . . . $ ______ (7)

Line 6 or line 7, whichever is less . . . $ ______ (8)

Pre-1986 deductible amount . . . $ 2,000 (9)

Amount from line 3 . . . $ ______ (10)

Amount from line 1 . . . $ ______

Minus: line 8 $ ______ × 2/3 = . . . $ ______ $ ______ (11)

Line 9, 10, or 11, whichever is less . . . $ ______ (12)

Maximum deduction for pre-1986 net capital losses: line 8 plus line 12 . . . $ ______ (13)

You can claim all, or any part, of your maximum deduction for your pre-1986 net capital losses. Enter the amount you want to claim on line 253 of your 1992 tax return.

Use the following chart to calculate your remaining unapplied balance of pre-1986 net capital losses.

**Pre-1986 net capital loss available for carry-forward**

Amount from line 1 . . . $ ______ (14)

Amount from line 8 : $ ______ × 2/3 = . . . $ ______ (15)

Amount from line 12 . . . $ ______ (16)

Total of line 15 plus line 16 . . . $ ______ (17)

Balance available for carry forward to a future year: line 14 minus line 17 . . . $ ______ (18)

## Example

Allan has a pre-1986 unapplied net capital loss of $1,800. He claimed a capital gains deduction of $800 in 1986 and $800 in 1989. In 1992, Allan reported a taxable capital gain of $1,000 on line 127 of his 1992 return. He uses the following chart to calculate the maximum deduction for his pre-1986 net capital loss, and the loss balance that is available for him to carry forward to a future year.

We calculated Allan's carry forward of $1,800 using the chart in the 1991 *Capital Gains Tax Guide*. If you claimed any portion of your pre-1986 capital losses in 1989, 1990, or 1991, you should follow this chart to recalculate your carry forward.

**Pre-1986 capital loss balance for 1992**

| | | | |
|---|---|---|---|
| Unapplied net capital losses before May 23, 1985 | | $ 1,800 | (1) |
| Capital gains deductions claimed: | | | |
| Before 1988 | $ 800 | | |
| In 1988 and 1989 $ 800 × 3/4 = | $ 600 | | |
| In 1990 and 1991 $____ × 2/3 = | $____ | | |
| Total capital gains deductions after adjustment | | $ 1,400 | (2) |
| Pre-1986 capital loss balance for 1992: line 1 minus line 2 | | $ 400 | (3) |

**Pre-1986 adjusted net capital loss balance for 1992**

| | | | |
|---|---|---|---|
| Unapplied net capital loss from line 1 | | $ 1,800 | (4) |
| Adjustment factor | | × 3/2 | |
| Adjusted pre-1986 net capital loss amount | | $ 2,700 | (5) |

**Pre-1986 net capital loss applied in 1992**

| | | | |
|---|---|---|---|
| Taxable capital gain reported on line 127 | | $ 1,000 | (6) |
| Adjusted net capital loss amount from line 5 | | $ 2,700 | (7) |
| Line 6 or line 7, whichever is less | | $ 1,000 | (8) |
| Pre-1986 deductible amount | | $ 2,000 | (9) |
| Amount from line 3 | | $ 400 | (10) |
| Amount from line 1 | $ 1,800 | | |
| Minus line 8 $1,000 × 2/3 = | $ 666 | $ 1,134 | (11) |
| Line 9, 10, or 11, whichever is less | | $ 400 | (12) |
| Maximum deduction for pre-1986 net capital losses: line 8 plus line 12 | | $ 1,400 | (13) |

**Pre-1986 net capital loss available for carry-forward**

| | | | |
|---|---|---|---|
| Amount from line 1 | | $ 1,800 | (14) |
| Amount from line 8 $1,000 × 2/3 = | $ 666 (15) | | |
| Amount from line 12 | $ 400 (16) | | |
| Total of line 15 plus line 16 | | $ 1,066 | (17) |
| Balance available for carry forward to a future year: line 14 minus line 17 | | $ 734 | (18) |

The maximum deduction that Allan can claim on line 253 for pre-1986 net capital losses in 1992 is $1,400. His pre-1986 net capital loss balance that he can carry-forward to a future year is $734.

### Net capital losses incurred after May 22, 1985 and before 1988

You can only apply allowable capital losses you incurred between these two dates against taxable capital gains.

If you want to apply these losses against your 1992 capital gains, use the following chart. It will help you calculate your maximum deduction.

Balance of unapplied net capital losses after May 22, 1985 and before 1988 .................. $ ______ (1)
**Adjusted net capital loss amount:**
Line 1 .................. $ ______ × 3/2 .......... $ ______ (2)
Taxable capital gains reported on line 127 of your 1992 return .................. $ ______ (3)
**Maximum deduction in 1992 for net capital losses after May 22, 1985 and before 1988:**
Line 2 or line 3, whichever is less .................. $ ______ (4)

On line 253 of your tax return, you can claim all or a part of the amount on line 4 as a net capital loss after 1985 and before 1988.

You may still have a balance of **unapplied net capital losses** after you have applied these losses to your 1992 taxable capital gains. If this is the case, use the following chart to calculate this balance. Remember that you are adjusting the amount you applied to 1992 to reflect the lower inclusion rate **before** you deduct it from the balance of your unapplied net capital losses.

Total unapplied net capital losses after May 22, 1985 before 1988 at the beginning of 1992 .................. $ ______ (1)
Amount claimed on line 253 of your 1992 return for these losses .......... $______ × 2/3 = .......... $ ______ (2)
**Balance of net capital losses after May 22, 1985 and before 1988 available to carry forward to a future year:**
Line 1 minus line 2 .................. $ ______ (3)

## Applying 1988 and 1989 net capital losses to 1992

Since there was a lower inclusion rate for 1988 and 1989, you have to adjust your net capital losses for those years before you apply them against your taxable capital gains in 1992.

To apply these net capital losses against your 1992 taxable capital gains, use the following chart.

Balance of unapplied net capital losses for 1988 and 1989 .................. $ ______ (1)
**Adjusted net capital loss amount:**
Line 1 .................. $ ______ × 9/8 .......... $ ______ (2)
Taxable capital gains reported on line 127 of your 1992 return .................. $ ______ (3)
**Maximum deduction in 1992 for net capital losses for 1988 and 1989:** Line 2 or line 3, whichever is less .... $ ______ (4)

On line 253 of your return you can claim all or a part of the amount on line 4 as net capital losses of other years.

After you claim your deduction, you may have a remaining balance of unapplied net capital losses for these years. Use the following chart to calculate this balance. Please note that you are adjusting back the amount applied to 1992 to reflect the lower inclusion rate, before you deduct it from the balance of your unapplied net capital losses.

Total unapplied net capital losses from 1988 and 1989 at the beginning of 1992 .................. $ ______ (1)
Amount claimed on line 253 of your 1992 return for 1988 and 1989 losses .... $ ______ × 8/9 = .......... $ ______ (2)
**Balance of net capital losses in 1988 and 1989 available to carry forward to a future year:**
Line 1 minus line 2 .................. $ ______ (3)

### Example

Dexter had the following capital gains and losses:

| | | |
|---|---|---|
| **1988** | Capital loss | $ (700) |
| | Capital gain | $ 100 |
| | Net capital loss | $ (600) |
| | Allowable capital loss (2/3 × $600) | $ (400) |
| **1989** | Capital loss | $ (2,100) |
| | Capital gain | $ 1,200 |
| | Net capital loss | $ (900) |
| | Allowable capital loss (2/3 × $900) | $ (600) |
| **1992** | Capital gain | $ 1,467 |
| | Taxable capital gain (3/4 ×$1,467) | $ 1,100 |

Since Dexter could not apply his 1988 and 1989 allowable capital losses in those years, these amounts became unapplied net capital losses for 1988 and 1989. For 1992, Dexter wants to reduce his taxable capital gain of $1,100 by claiming net capital losses of other years. He wants to use his losses from 1988 and 1989. To do this, he completes the following chart as shown:

Unapplied net capital losses for 1988 and 1989 ($400 + $600) .................. $ 1,000 (1)
Adjusted net capital loss amount line 1 .................. $1,000 × 9/8 .......... $ 1,125 (2)
Taxable capital gain reported on line 127 of his 1992 return .................. $ 1,100 (3)
Maximum deduction in 1992 for net capital losses for 1988 and 1989:
Line 2 or line 3, whichever is less: .................. $ 1,100 (4)

On line 253 of his tax return, Dexter can claim all or part of the amount on line 4 as net capital losses of other years. He claims the entire amount of $1,100. To determine his remaining balance, he completes the following chart as shown.

Total unapplied net capital losses from 1988 and 1989 at the beginning of 1992 .................. $ 1,000 (1)
Amount claimed on line 253 of his 1992 return for 1988 and 1989 losses ...... $1,100 × 8/9 = .......... $ 978 (2)
Balance of net capital losses in 1988 and 1989 available to carry forward to a future year:
Line 1 minus line 2 .................. $ 22 (3)

## Applying 1990 and 1991 net capital losses to 1992

If you would like to apply your 1990 and 1991 net capital losses against taxable capital gains you had in 1992, you do not have to make an adjustment. This is because the inclusion rate for all years is the same. To make this claim, enter the amount of your 1990 and 1991 net capital losses on line 253 of your return. The amount you can claim cannot be more than the taxable capital gains you had in 1992.

Use the following chart to calculate your remaining balance of these losses:

Unapplied 1990 and 1991 net capital losses at the beginning of 1992 ....... $ ________ (1)
Amount claimed on line 253 of your 1992 return for 1990 and 1991 losses ........................... $ ________ (2)
Balance of 1990 and 1991 net capital loss available for carry forward to a future year: line 1 minus line 2 ....... $ ________ (3)

## How do you apply a 1992 net capital loss to previous years?

You can carry a 1992 net capital loss back three years, and use it to reduce your taxable capital gains. When you carry back your net capital loss, you can choose to which year you want to apply the loss.

To apply a 1992 net capital loss to 1989, 1990 or 1991, complete Form T1A, Area III — Net capital loss for carry-back. It will show you how to adjust the inclusion rates for each year, and will determine the amount you have left to carry forward to future years.

To help you keep accurate records, make sure you keep separate balances of unapplied net capital losses for each year.

**Example**

Usha reported taxable capital gains totalling $1,500 in 1989, $1,000 in 1990, and $2,000 in 1991. She claimed a capital gains deduction of $1,000 in 1990. In 1992, Usha had a net capital loss of $8,000. She would like to use her 1992 net capital loss to completely offset her taxable capital gains in 1989 and 1991. As a result, Usha decides to first apply her net capital loss to 1989.

1992 unapplied net capital loss .......... $ 8,000 (1)

1992 adjusted net capital loss amount available for carry-back to 1989:
Line 1 $8,000 × 8/9 = .......... $ 7,111 (2)
Amount applied to 1989 .......... $ 1,500 (3)
Balance of net capital loss:
Line 2 minus line 3 .......... $ 5,611 (4)

**Unapplied net capital loss available to carry back to 1991:**
Line 4 $5,611 × 9/8 = .......... $ 6,312 (5)

Amount applied to 1991 .......... $ 2,000 (6)
**Balance of 1992 net capital loss available to carry forward to a future year:**
Line 5 minus line 6 .......... $ 4,312 (7)

Usha fills in Form T1A, *Request for Loss Carry-Back*, and attaches it to her 1992 income tax return.

# Chapter 5
# Capital Gains Deduction

This chapter deals with the capital gains deduction as it applies to capital property other than qualified farm property or qualified small business corporation shares. In this chapter, we explain the proposed rules regarding property disposed of after February 1992. We will also show you how to complete Form T936, *Calculation of Cumulative Net Investment Loss (CNIL) to December 31, 1992*, and Form T657A, *Calculation of Capital Gains Deduction on Other Capital Property.*

If you disposed of qualified farm property or qualified small business corporation shares in 1992 or a prior year, use Form T657, *Calculation of Capital Gains Deduction on All Capital Property.* If you disposed of a combination of properties that includes these types of properties you should also use form T657. This form includes information that helps you calculate the deduction for these types of capital gains. You can get this form from your district office.

## What is a capital gains deduction?

It is a deduction that you can claim against taxable capital gains incurred from property disposed of after 1984. By claiming this deduction, you can reduce the amount of your taxable income.

Under proposed legislation, a capital gain incurred from certain property disposed of after February 1992 will not be eligible for the deduction. Only the portion of the gain accrued after February 1992 will not be eligible. If you disposed of capital property after February 1992, see the section "Property disposed of after February 1992" later in this chapter.

## When can you claim the capital gains deduction?

You can claim the capital gains deduction in a year that you have an eligible capital gain. Your claim cannot be more than your eligible capital gain. Claiming a capital gains deduction is not mandatory. In other words, you can claim any amount you want to in a year, from zero up to the maximum.

An eligible capital gain does not include reserves brought into income from capital property you disposed of before 1985. In addition, it does not include the portion of a capital gain accrued after February 1992 from the disposition of real property. We explain this in the section called "Non-qualifying real property" on this page.

**Tax Tip**

If you do not report your capital gain on your return for the year that you had the capital gain, you may not be allowed to claim the capital gains deduction.

## Who is eligible to claim the capital gains deduction?

Anyone who was a resident of Canada throughout 1992 is eligible. For purposes of this deduction, we will also consider you to be a resident throughout 1992 if:

- you were a resident of Canada for at least **part** of 1992; and
- you were a resident of Canada **throughout** 1991 or 1993.

Residents of Canada include "factual" and "deemed" residents. For a definition of these terms, see the heading "Before you start" under "General Information" in the *General Tax Guide*. If you were not a resident of Canada throughout 1992, see the section called "Are you entitled to claim the capital gains deduction?" on page 43 in Chapter 8. It will help you decide if you are eligible to claim this deduction.

## What is the capital gains deduction limit?

If you have an eligible capital gain in 1992, you can claim up to $100,000 in capital gains deductions. Since you only include 3/4 of a capital gain in your taxable income, your lifetime cumulative capital gains deduction limit is $75,000 (3/4 of $100,000). If you disposed of qualified farm property or qualified small business corporation shares, your lifetime cumulative capital gains deduction limit is $375,000 (3/4 of $500,000).

## Property disposed of after February 1992

Legislation is proposed that will exclude all or part of a capital gain from the disposition of real property and certain other capital property from the calculation of the capital gains deduction. The principal residence exemption remains the same and does not fall under these new rules.

You may have disposed of non-qualifying real property and ended up with a capital loss. If this is your only disposition of non-qualifying real property, there is no effect on your capital gains deduction and you do not have to read this section. You also do not have to read this section if you had more than one disposition of non-qualifying real property but the net effect of these dispositions is a capital loss.

This section will help you determine if all or a portion of your capital gain is eligible for the deduction. It will also help you to calculate the portion of your capital gain that is not eligible, and provide instructions to complete your Schedule 3.

### Non-qualifying real property

To determine if your capital gain is eligible for the capital gains deduction, you must determine if your property is non-qualifying real property. The portion of your gain accrued after February 1992, on the disposition of non-qualifying real property is not eligible.

Qualified farm property and qualified small business corporation shares are not included in the description of non-qualifying real property and remain eligible for the $500,000 capital gains deduction.

Generally, non-qualifying real property is real property that you or your partnership disposed of after February 1992. It also includes the following property, if the fair market

value is derived principally (more than 50%) from real property:

- a share of a capital stock of a corporation;
- an interest in a partnership;
- an interest in a trust; or
- interest or options in respect of such real property.

**The non-qualifying property we described above will be considered as eligible for the capital gains deduction if while you or your spouse owned it:**

- it was used principally in an active business at all times in the 24-month period before you disposed of it. If you or your spouse owned it for less than 24 months, that shorter period; or
- it was used principally in an active business throughout all or substantially all (90% or more) of the time before you disposed of it.

This last situation accommodates the sale of real property that may have been used for many years in an active business but lay idle for a period of time before you sold it.

In addition, the active business must have been carried on for the above-specified time period by:

- you, your spouse, child or parent; or
- a preferred beneficiary of a personal trust; or
- the spouse, child or parent of the preferred beneficiary of a personal trust; or
- a corporation, partnership or personal trust where 90% or more of the fair market value of their shares or interests are owned by one or more persons described in this list.

## What is an active business?

For the purposes of this deduction, an active business is:

- a business that does not derive its income principally from property; or
- any business that employs more than 5 persons on a full-time basis; or
- any business that has managerial, administrative, financial, maintenance or other similar services provided to it that would be equivalent to employing more than 5 persons on a full-time basis; or
- any business that leases property that is not real property.

## Calculating your eligible capital gains

If you disposed of any of the property we described as non-qualifying real property, you have to calculate the portion that is not eligible for the capital gains deduction. Even if you are not claiming a capital gains deduction this year, you should still do this calculation. The reason for this is that the taxable part of your capital gain that is not eligible for the deduction becomes investment income for the purposes of calculating your cumulative net investment loss.

To calculate the portion that is not eligible for the deduction, you use a formula. The formula is:

$$A \times B/C$$

In this formula:

A = Your capital gain.

B = The number of months you owned the property after February 1992. You start counting with March 1992 and you include the month you disposed of the property.

C = The number of months you owned the property. If you owned the property before January 1972, you start counting with that month. Otherwise, start counting with the month you purchased the property and include the month you disposed of the property.

You may have disposed of non-qualifying real property that was originally transferred to you. In this case, you have to consider the factors of the transfer to determine the amount to use for "C" in the formula.

If the property was transferred to you for an amount not more than the adjusted cost base to the person who transferred it to you (the transferor), you will be considered as having purchased the property when the transferor purchased it.

If the property was transferred to you for more than the adjusted cost base to the transferor, you will be considered to have purchased the property at the time the property was transferred to you. This will usually happen when the transferor elects to report all or part of the gain on the property at the time of the transfer.

You may have disposed of a property that was used as your principal residence for part of the time that you owned it. In this case, do not include any months that the property was used as your principal residence when determining the numbers to use in "B" or "C" of the formula. If you need more information on principal residence, see Chapter 7.

When you record your disposition on Schedule 3, you enter the total gain at the line that describes the property you disposed of. For example, if you disposed of a rental property, you enter the gain at line 522. If you disposed of a share of the capital stock of a corporation that you determined was non-qualifying real property, you enter your gain at line 520. If you disposed of a cottage that was not your principal residence, you enter the gain at line 530. You then use the formula to determine the amount of your gain that is not eligible for the capital gains deduction. You enter this amount at line 536 of Schedule 3.

### Example

Jackie owned a cottage that was not her principal residence. She bought it in 1969 for $5,000. In November 1992, she sold it for $70,000. After subtracting her adjusted cost base and the outlays and expenses, she ended up with a capital gain of $40,000. She calculated her portion of the gain that was not eligible for the capital gains deduction as follows:

A = $40,000

B = 9 (March 1992 – November 1992)

C = 251 (January 1972 – November 1992)

$40,000 × 9/251 = $1,434.26

On her Schedule 3 for 1992, Jackie enters $40,000 at line 530. She does this because her cottage is real estate that is classified as personal-use property. She then enters $1,434.26 at line 536. This is the portion of her gain that is not eligible for the capital gains deduction. The eligible portion of her capital gain is $38,565.74. This is the amount she uses to calculate her capital gains deduction.

You may have two dispositions of non-qualifying real property. One is a capital gain and the other is a capital loss. If the net effect of these two dispositions is a capital gain, you also have to determine the non-eligible portion of your capital loss. You do this because the non-eligible portion of your capital loss should be applied against the non-eligible portion of your capital gain. This will allow you to have a larger capital gains deduction. Once you have done this calculation, you enter the net amount of the non-eligible capital gain at line 536 of your Schedule 3.

**Example**

Tim had the following capital gains and capital losses in 1992.

| | |
|---|---|
| Loss on the sale of shares — line 520 | $ (400) |
| Gain on the sale of real estate — line 522 | $ 800 |
| Gain on the sale of bonds — line 528 | $1,200 |

Both the shares and the real estate are non-qualifying real property. He bought the shares in July 1991 and sold them in April 1992. He bought the real estate in January 1992 and sold it in April 1992.

Tim calculated the non-eligible portion of his capital loss and capital gain as follows:

| | | |
|---|---|---|
| Shares | $(400) × 2/10 = | $ (80) |
| Real estate | $800 × 2/4 = | $400 |
| Total | | $320 |

Tim entered $320 on line 536 of Schedule 3. Three-quarters of this capital gain ($240) will become investment income. This will reduce Tim's cumulative net investment loss for 1992.

## How do you calculate your capital gains deduction?

To calculate your capital gains deduction for 1992, you need to know the following amounts:

- your **cumulative net investment loss** (CNIL) for 1992;
- your **annual gains limit** for 1992;
- your **cumulative gains limit** for 1992;
- your **eligible capital gains** in 1992; and
- the total of all **capital gains deductions** you claimed in previous years.

There are five steps for you to complete to figure out your capital gains deduction for 1992. The following sections will help you complete each step.

### Step 1 — Calculating your CNIL

The first step in calculating your capital gains deduction is to figure out your CNIL for 1992. If you have a CNIL in 1992, it will reduce the amount of your capital gains deduction.

Your CNIL is the total of:

- your **investment expenses** for each year after 1987; minus
- your **investment income** for each year after 1987.

Under proposed legislation, the amount of net capital losses of other years (line 253 on your return) that is used to reduce any taxable capital gains that are not eligible for the capital gains deduction, will become an investment expense. You will use this amount when you calculate your CNIL. In addition, a taxable capital gain that is not eligible for the capital gains deduction becomes investment income. You will also use this amount when you calculate your CNIL.

Your CNIL will not necessarily reduce your lifetime capital gains deduction. Since the balance in your CNIL account varies each year, you could still end up claiming the maximum lifetime capital gains deduction if your CNIL is offset by investment income you earn in a future year.

To figure out your CNIL for 1992, complete form T936.

**Tax Tip**

Even if you do not claim a capital gains deduction in 1992, you should still complete form T936 and keep it for your own records. Since the balance in your CNIL account is a cumulative total, you may need this information in the future.

The following example will show you how to calculate a CNIL.

## Example

Jim had the following types of income and expenses for 1991 and 1992 on his income tax return. Prior to 1991, Jim did not have any investment income or expenses:

| | 1991 | 1992 |
|---|---|---|
| Line 120: Taxable dividends | $ 100 | $ 100 |
| Line 121: Interest income | $ 575 | $ 500 |
| Line 126: Net rental income (loss) | $(1,000) | $(2,000) |
| Line 127: Taxable capital gains | | * $ 3,750 |
| Line 221: Carrying charges | $ 1,125 | $ 600 |

* Jim had a $5,000 capital gain from the disposal of real estate in 1992. Of the $5,000, he calculated that $2,000 was not eligible for the capital gains deduction. He entered this amount at line 536 of his Schedule 3. The taxable portion of his capital gain not eligible for the deduction is $1,500 and the taxable portion of his capital gain eligible for the deduction is $2,250.

He calculated his CNIL for 1991 and 1992 by completing forms T936 as follows. Due to space limitations, we have not reproduced form T936 in its entirety.

**PART 1 — CUMULATIVE INVESTMENT EXPENSES**

Investment expenses claimed on your 1991 return.

| | Line | Amount | Line | Total |
|---|---|---|---|---|
| **ADD:** Carrying charges and interest expenses (from line 221) | (1) | 1,125 00 | | |
| Net rental loss (from line 126 and/or related schedules or statements) | (2) | 1,000 00 | | |
| Limited or non-active partnership loss (from line 122) other than allowable capital losses | (3) | | | |
| Limited partnership losses of other years after 1985 (from line 251) other than allowable capital losses | (4) | | | |
| 50% of exploration and development expenses (from line 224) | (5) | | | |
| Any other expenses claimed in 1991 to earn property income (from line 232)* | (6) | | | |
| Total Investment Expenses claimed in 1991 (add lines (1) to (6) inclusive) | | 2,125 00 | ▶ (7) | 2,125 00 |
| **ADD:** Investment Expenses claimed in prior years (after 1987) (Enter the amount from line (A) of your 1990 form T936. If you did not complete a form T936 for 1990, report the total expense amounts as described in lines (1) to (6) above, as claimed on your 1988, 1989 and 1990 returns.) | | | (8) | |
| Cumulative Investment Expenses (add lines (7) and (8)) | | | | 2,125 00 (A) |

**PART 2 — CUMULATIVE INVESTMENT INCOME**

Investment Income reported on your 1991 return.

| | Line | Amount | Line | Total |
|---|---|---|---|---|
| **ADD:** Investment Income (from lines 120 and 121) | (9) | 675 00 | | |
| Net rental income, including recaptured depreciation (from line 126) | (10) | | | |
| Net income from limited or non-active partnership (from line 122) other than taxable capital gains | (11) | | | |
| 50% of income from the recovery of exploration and development expenses (from line 130) | (12) | | | |
| Any other property income reported in 1991 (from line 130)** | (13) | | | |
| Annuity payments taxable under paragraph 56(1)(d) less the capital portion deductible under paragraph 60(a) | (14) | | | |
| Total Investment Income reported in 1991 (add lines (9) to (14) inclusive) | | 675 00 | ▶ (15) | 675 00 |
| **ADD:** Total Investment Income reported in prior years (after 1987) (Enter the amount from line (B) of your 1990 form T936. If you did not complete a form T936 for 1990, report the total income amounts described in lines (9) to (14) above, as reported on your 1988, 1989 and 1990 returns.) | | | (16) | -0- |
| Cumulative Investment Income (add lines (15) and (16)) | | | | 675 00 (B) |

**PART 3 — CUMULATIVE NET INVESTMENT LOSS**

| | Total |
|---|---|
| Cumulative Investment Expenses (line (A) of Part 1) minus Cumulative Investment Income (line (B) of part 2): If negative (i.e. income is more than expenses), enter zero. This amount has to be entered on line 15 of form T657A or form T657(E), if you are claiming a capital gains deduction on your 1991 return | 1,450 00 (C) |

Jim calculated his CNIL to the end of 1991 even though he did not have any taxable capital gains in 1991. By doing so, it was easier for him to calculate his CNIL in 1992.

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## CALCULATION OF CUMULATIVE NET INVESTMENT LOSS (CNIL) TO DECEMBER 31, 1992

- Use this form if you had any "investment income" or "investment expenses" for 1992 or in any year after 1987.
- Your CNIL reduces the amount of your cumulative gains limit for the year and may affect the allowable amount of your capital gains deduction.
- Even if you are not claiming a capital gains deduction in 1992, you should still complete this form for your own records because the balance in your CNIL account is a cumulative total. You may need this information in a future year.
- If you need more information, refer to the *Capital Gains Tax Guide* or contact your district taxation office.

If you have capital gains in 1992 that are not eligible for the capital gains deduction, you may have additional investment income to include when you calculate your CNIL. If you do, complete Parts A and B below. Otherwise, start at Part 1. Capital gains that are not eligible include reserves claimed for property you disposed of prior to 1985 and certain other capital property you disposed of after February 1992. See Chapter 5 in the *Capital Gains Tax Guide* for details.

### Part A – Taxable Capital Gains Not Eligible for the Capital Gains Deduction

| | Line | Amount | Line | Amount |
|---|---|---|---|---|
| Enter the amount from line 536 on schedule 3 | (a) | 2,000 00 | | |
| Enter the amount from line 397 on form T2017 | (b) | | | |
| Subtotal: Line (a) minus line (b) | | 2,000 00 | ▶ (c) | 2,000 00 |
| Enter the amount from line 395 on form T2017 | | | (d) | |
| Total : Line (c) plus line (d) | | | (e) | 2,000 00 |
| **Taxable capital gains not eligible for the capital gains deduction:** Enter 3/4 of line (e) | | | (f) | 1,500 00 |

### Part B – Additional Investment Income

- If you included an amount from a T3 slip on line 536 of schedule 3, complete all steps in this part.
- Otherwise, enter the amount from line (f) in Part A, on line (l) in this part.

| | Line | Amount | Line | Amount |
|---|---|---|---|---|
| Enter the amount from line (f) above | | | (g) | |
| Enter the amount from box 21 of all 1992 T3 slips | (h) | | | |
| Enter the amount from box 30 of all 1992 T3 slips | (i) | | | |
| Total: Line (h) minus line (i) | (j) | | | |
| Enter 3/4 of line (j) | | | (k) | |
| **Additional investment income**: Line (g) minus line (k) | | | (l) | 1,500 00 |

### Part 1 – Cumulative Investment Expenses

| | Line | Amount | Line | Amount |
|---|---|---|---|---|
| Investment expenses claimed on your 1992 return: | | | | |
| Carrying charges and interest expenses (from line 221) | (1) | 600 00 | | |
| Net rental loss (from line 126 and/or related schedules or statements) | (2) | 2,000 00 | | |
| Limited or non-active partnership losses (from line 122) other than allowable capital losses | (3) | | | |
| Limited partnership losses of other years after 1985 (from line 251) other than allowable capital losses | (4) | | | |
| 50% of exploration and development expenses (from line 224) | (5) | | | |
| Any other expenses claimed in 1992 to earn property income (from line 232)* | (6) | | | |
| Additional investment expenses: If you did not complete Parts A and B above, enter zero. Otherwise, enter the lesser of line (l) in Part B above, or the amount you claimed on line 253 of your return | (7) | 0 | | |
| Total investment expenses claimed in 1992 (add lines 1 to 7 inclusive) | | 2,600 00 | ▶ (8) | 2,600 00 |
| Investment expenses claimed in prior years (after 1987): Enter the amount from line A on your 1991 form T936. If you did not complete form T936 for 1991, report the total expense amounts as described in lines 1 to 6 above, as claimed on your 1988, 1989, 1990 and 1991 returns | | | (9) | 2,125 00 |
| Cumulative investment expenses (add lines 8 and 9) | | | | 4,725 00 (A) |

* Refer to the list "Other Investment Expenses" on the other side of this form.

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See reverse

### Other Investment Expenses

**Other expenses include** • repayments of inducements • repayments of refund interest • the uncollectible portion of proceeds from disposition of depreciable property (except passenger vehicles that cost more than $24,000) • sale of agreement for sale or mortgage included in proceeds of disposition in a previous year under subsection 20(5) • foreign non-business tax under subsections 20(11) and 20(12) • life insurance premiums deducted from property income • capital cost allowance claimed on certified films and videotapes.

**Do not include** • expenses incurred to earn business income • interest paid on money borrowed to: • buy an income averaging annuity contract • pay a premium under a registered retirement savings plan • make a contribution to a registered pension fund or plan • make a contribution to a deferred profit sharing plan.

### Part 2 – Cumulative Investment Income

Investment income reported on your 1992 return:

| | Line | Amount | | Line | Amount | |
|---|---|---|---|---|---|---|
| Investment income (from lines 120 and 121) | (10) | *600 00* | | | | |
| Net rental income, including recaptured depreciation (from line 126) | (11) | | | | | |
| Net income from limited or non-active partnership (from line 122) other than taxable capital gains | (12) | | | | | |
| 50% of income from the recovery of exploration and development expenses (from line 130) | (13) | | | | | |
| Any other property income reported in 1992 (from line 130)* * | (14) | | | | | |
| Annuity payments taxable under paragraph 56(1)(d.1) or 56(1)(d) less the capital portion deductible under paragraph 60(a) | (15) | | | | | |
| Additional investment income: Enter the amount from line (l) in Part B on the other side of this form | (16) | *1,500 00* | | | | |
| Total investment income reported in 1992 (add lines 10 to 16 inclusive) | | *2,100 00* | ▶ | (17) | *2,100 00* | |
| Total investment income reported in prior years (after 1987): Enter the amount from line B of your 1991 form T936. If you did not complete a form T936 for 1991, report the total income amounts described in lines 10 to 15 above, as reported on your 1988, 1989, 1990 and 1991 returns | | | | (18) | *675 00* | |
| Cumulative investment income (add lines 17 and 18) | | | | | *2,775 00* | (B) |

### Other Property Income

* * **Other property income includes** • amounts from insurance proceeds in respect of recaptured depreciable property (other than amounts already included in line 11) • home insulation or energy conversion grants under paragraph 12(1)(u)• • payments received as an inducement or reimbursement • income from the appropriation of property • other income from a trust.

**Do not include income amounts** • that relate to business income • payments received from an income averaging annuity contract • payments received from an annuity contract bought pursuant to a deferred profit sharing plan.

### Part 3 – Cumulative Net Investment Loss

| | Line | Amount | |
|---|---|---|---|
| Cumulative investment expenses (line A of Part 1) | (19) | *4,725 00* | |
| Cumulative investment income (line B of Part 2) | (20) | *2,775 00* | |
| Cumulative net investment loss (line 19 minus line 20, if negative, enter zero) | | *1,950 00* | (C) |

If you are claiming a capital gains deduction on your 1992 return, enter the amount from line C on line 15 of form T657A

### Step 2 — Calculating your annual gains limit

The second step in figuring out your capital gains deduction is to calculate your annual gains limit.

Your **annual gains limit** for 1992 is the total of:

- your net eligible taxable capital gains for the year; **minus**
- the total of any allowable business investment losses for the year; and
- net capital losses of other years used to reduce eligible taxable capital gains, that you reported in 1992.

Under proposed legislation, net capital losses of other years applied against taxable capital gains not eligible for the capital gains deduction will not reduce your annual gains limit in 1992. For this purpose, net capital losses of other years are first applied against taxable capital gains that are not eligible and then against eligible taxable capital gains.

To calculate your annual gains limit complete Part 1 of form T657A.

**Example**

Jim completed Part 1 of his T657A as follows:

**Part 1 – Calculation of Annual Gains Limit for 1992**

| | | | | |
|---|---|---|---|---|
| Taxable capital gain (loss) from lines 540 to 544 on schedule 3 | (1) | 3,750 00 | | |
| Taxable capital gains not eligible for the capital gains deduction (amount from line (f) on form T936) | (2) | 1,500 00 | | |
| Taxable capital gains eligible for the capital gains deduction (line 1 minus line 2) | | 2,250 00 ▶ | (3) | 2,250 00 |
| Net capital losses of other years (to calculate this amount, complete chart 1 on the other side of this form) | (4) | | | |
| Allowable business investment losses (line 217 of your 1992 return) | (5) | | | |
| Total of above losses (line 4 plus line 5) | | ▶ | (6) | Ø |
| Annual gains limit for 1992 (line 3 minus line 6: if negative, enter zero) | | | (7) | 2,250 00 |

### Step 3 — Calculating your cumulative gains limit

The third step in figuring out your capital gains deduction is to calculate your cumulative gains limit.

Your **cumulative gains limit** for 1992 is the total of your net eligible taxable capital gains from 1985 to 1992, **minus** the total of all of the following:

- any allowable capital loss you deducted from other income in 1985 (to a maximum of $2,000);
- all allowable business investment losses you claimed from 1985 to 1992;
- all net capital losses of other years you claimed from 1985 to 1987;
- all net capital losses of other years you claimed from 1988 to 1992 that you used to reduce eligible taxable capital gains in each of those years;
- your CNIL to December 31, 1992; and
- all capital gains deductions you claimed from 1985 to 1991.

Under proposed legislation, your cumulative gains limit will not be reduced by net capital losses of other years applied against taxable capital gains not eligible for the capital gains deduction in 1988 and following years.

To calculate your cumulative gains limit, complete Part 2 of form T657A.

### Example

Jim had a $700 taxable capital gain in 1987 but he did not claim a capital gains deduction. He completed Part 2 of form T657A as follows:

**Part 2 – Calculation of Cumulative Gains Limit for 1992**

| Description | Line | Amount | Line | Amount |
|---|---|---|---|---|
| Taxable capital gains reported after 1984 and before 1992 (do not include reserves reported before 1988) | (8) | 700 00 | | |
| 1992 taxable capital gains eligible for the capital gains deduction (from line 3 in Part 1 above) | (9) | 2,250 00 | | |
| Cumulative taxable capital gains eligible for the capital gains deduction (line 8 plus line 9) | | 2,950 00 | ▶ (10) | 2,950 00 |
| Allowable capital losses claimed in 1985 (from line 127 on your 1985 return; maximum of $2,000) | (11) | | | |
| Allowable business investment losses claimed after 1984 and before 1992 (from line 217 on your 1985 to 1991 returns) | (12) | | | |
| Net capital losses of other years claimed in 1985, 1986 and 1987 (from line 253 of your 1985, 1986 and 1987 returns and Form T1A, *Request for Loss Carry-Back* | (13) | | | |
| Net capital losses of other years claimed in 1988, 1989, 1990 and 1991 (to determine this amount, complete chart 2 on the other side of this form) | (14) | | | |
| Cumulative net investment loss (line C on form T936) | (15) | 1,950 00 | | |
| Total losses used to calculate your annual gains limit (line 6 of Part 1 above) | (16) | | | |
| Total capital gains deductions claimed after 1984 and before 1992 (from line 254 on your 1985 to 1991 returns) | (17) | -0- | | |
| Subtotal (add lines 11 to 17 inclusive) | | 1,950 00 | ▶ (18) | 1,950 00 |
| Cumulative gains limit for 1992 (line 10 minus line 18: if negative, enter zero) | | | (19) | 1,000 00 |

### Step 4 — Calculating your capital gains deduction available for 1992

The fourth step in figuring out your capital gains deduction is to calculate the balance of your lifetime capital gains deduction limit.

To do this, complete Part 3 of form T657A.

**Example**

Jim's completes Part 3 of form T657A as follows:

**Part 3 – Calculation of Capital Gains Deduction on Other Capital Property**

| Description | Line | Amount | Line | Amount |
|---|---|---|---|---|
| Maximum capital gains deduction for 1992 | | | (20) | $75,000 |
| Total capital gains deductions claimed after 1984 and before 1988 (from line 254 on your 1985 to 1987 returns) | (21) | Ø | | |
| Adjustment of pre-1988 capital gains deduction (1/2 of amount at line 21) | (22) | | | |
| Capital gains deductions claimed in 1988 and 1989 excluding "eligible capital property" (line 254 of your 1988 and 1989 returns less any amounts reported at line 544 on schedule 3 for 1988 and 1989; if negative, enter zero) | (23) | | | |
| Adjustment of 1988 and 1989 capital gains deductions (1/8 of amount at line 23) | (24) | | | |
| Capital gains deductions claimed in 1988 and 1989 for "eligible capital property" (not to exceed line 544 for 1988 and 1989; total of amounts at line 254 of your 1988 and 1989 returns less the amount at line 23 above) | (25) | | | |
| Total capital gains deductions claimed in 1990 and 1991 (from line 254 on your 1990 and 1991 returns) | (26) | | | |
| Subtotal (add lines 21 to 26 inclusive) | | Ø | ► (27) | Ø |
| Capital gains deduction available for 1992 (line 20 minus line 27: if negative, enter zero) | | | (28) | 75,000 00 |

### Step 5 — Figuring out your maximum claim

The final step is simple. The maximum amount you can claim is equal to the **lowest** of the following amounts:

- Line 7 of form T657A — your annual gains limit for 1992;
- Line 19 of form T657A — your cumulative gains limit at the end of 1992; or
- Line 28 of form T657A — your lifetime capital gains deduction limit available for 1992.

Remember, you do not have to claim the maximum amount. You can claim any amount, from zero to the maximum.

You enter the amount you want to claim on line 29 of form T657A. Then, enter the same amount at line 254 of your return.

**Example**

As we stated before, Jim decided to claim the maximum capital gains deduction, so he enters $1,000 on line 29 of form T657A and the same amount at line 254 on his 1992 return.

**Part 4 – Determination of 1992 Capital Gains Deduction on Other Capital Property**

| Description | Line | Amount |
|---|---|---|
| The maximum amount you can enter at line 29 is the least of lines 7, 19 and 28; however, you may enter an amount that is less than the maximum. Enter this amount on line 254 of your 1992 return | (29) | 1,000 00 |

# Chapter 6
# Reserves

In this chapter, we explain the capital gains rules when you sell property and only receive part of the selling price at the time of the sale. We also explain how to calculate the part of your reserve that is not eligible for the capital gains deduction.

## What is a reserve?

When you sell a capital property, you usually receive full payment at that time. However, this is not always the case. Sometimes the amount is spread over a number of years. For instance, you may sell a capital property for $50,000 and receive $10,000 at the time of the sale. You receive the remaining $40,000 over a period of four years. In this type of situation, you can claim a **reserve**.

If you decide to claim a reserve, you still need to calculate your capital gain for the year. You do this in the regular way (the proceeds of disposition **minus** the adjusted cost base and the selling expenses). From this amount, you have to deduct the amount of your reserve for the year. The figure that you end up with is the part of the capital gain that you have to report in the year of sale.

If you claimed a reserve in a **previous year**, include that reserve when you calculate your capital gains for the **current year**. For instance, if you claimed a reserve in 1991, you have to include this amount in your capital gains for 1992. If you still have a reserve for 1992, you have to calculate and deduct a new reserve, and include it for the following year — 1993. Keep doing this until you have received full payment for the property. However, there is a limit to the number of years that you can do this. It depends on the type of property that you sold.

A capital gain from a reserve qualifies for the **capital gains deduction** only if it is an eligible capital gain. Therefore, a reserve included in income from property you sold before 1985 is not eligible. Under proposed legislation, the portion of your reserve claimed in respect of a capital gain from the disposition of non-qualifying real property is not eligible for the capital gains deduction.

To deduct a reserve in any year, you have to fill in Form T2017, *Summary of Reserves on Dispositions of Capital Property*. You can find this form at the back of this guide.

## Who can claim a reserve?

Most people can claim a reserve when they sell a capital property. However, you **cannot** claim a reserve if you:

- were not a resident in Canada at the end of the taxation year, or at any time in the following year;
- were exempt from paying tax at the end of the taxation year or at any time in the following year; or
- sold a capital property to a corporation that you control in any way.

## How do you calculate a reserve?

There are two different ways to calculate a reserve. The one that you use depends on **when** you sold the property, and the type of property sold.

### Property sold on or before November 12, 1981

If you sold property on or before November 12, 1981, use the following formula to calculate your reserve:

(a) $$\frac{\text{Capital gain}}{\text{Proceeds of disposition}} \times \text{Amount not due until after the end of the year}$$

You also use this formula for property that you sold **after** November 12, 1981, if:

- the sale took place under the terms of an offer or an agreement in writing; and
- the offer or agreement was made, or entered into, on or before November 12, 1981.

### Property sold after November 12, 1981

If you sold property after November 12, 1981, the formula you use to calculate your maximum reserve depends on the type of property you sold. There are two formulas: one formula for when you sell **other property**, and one formula for when you sell **family farm property or small business corporation shares**.

You do not have to claim the maximum reserve in the taxation year. You may claim any amount up to the maximum. However, the amount of the reserve you claim in a later year for the disposition of a particular property may not be more than the amount you claimed for that property in the immediately preceding year.

### Other property

For all other property that you sell after November 12, 1981, you can spread the capital gain over a maximum of five years. Your reserve in each year cannot be more than the lesser of the following:

(a) $$\frac{\text{Capital gain}}{\text{Proceeds of disposition}} \times \text{Amount not due until after the end of the year}$$

**or**

(b) $$\frac{\text{Capital gain}}{\text{5 years}} \times (4 - X^*)$$

*X = the number of taxation years since the year of sale, but not including the year of sale.

By using this calculation, you end up reporting at least one-fifth of the capital gain each year until you have reported the entire amount.

### Family farm property or small business corporation shares

If you sell one of these two types of property after November 12, 1981, to your child (who lived in Canada at the time of the sale), you calculate your reserve in the following way. Remember that you can spread your capital gain over a maximum of 10 years. Also remember that your maximum reserve is the lesser of (a) or (b):

(a) $$\frac{\text{Capital gain}}{\text{Proceeds of disposition}} \times \text{Amount not due until after the end of the year}$$

**or**

(b) $$\frac{\text{Capital gain}}{\text{10 years}} \times (9 - X^{*})$$

*X = the number of taxation years since the year of sale, but **not** including the year of sale.

By using this calculation, you will end up reporting at least one-tenth of the capital gain each year until you have reported the entire amount.

Family farm property includes:

- shares of a family farm corporation;
- an interest in a family farm partnership; or
- land or depreciable property in Canada that you, your spouse, or any of your children, grandchildren, or great-grandchildren used in your farming business.

## Are you claiming a reserve for property disposed of after February 1992?

If you are claiming a reserve for non-qualifying real property (see page 27 in Chapter 5), you must calculate the portion of the reserve that is not eligible for the capital gains deduction.

To do this, you use the formula A × B/C. In this formula:

A = The capital gain you have determined is not eligible for the capital gains deduction (amount at line 536 on Schedule 3 for this property only).

B = The number of months you owned the property after February 1992. You start counting with March 1992 and you include the month you disposed of the property.

C = The number of months you owned the property. If you owned the property before January 1972, you start counting with that month. Otherwise, start counting with the month you purchased the property and include the month you disposed of the property.

### Example

Raju bought his cottage in January 1985. He sold it in December 1992 for $75,000. The adjusted cost base (ACB) of the cottage is $50,000, and his selling expenses were $5,000. Raju received a down payment of $30,000 at the time of sale. He will receive $5,000 a year for the following nine years.

Raju calculated his capital gain as follows:

| | | |
|---|---|---|
| Proceeds of disposition | | $75,000 |
| **Minus:** ACB | $50,000 | |
| Selling expenses | 5,000 | 55,000 |
| **Equals:** Capital gain | | $20,000 |

Once he determined his capital gain, he calculated the amount of the gain that was not eligible for the capital gains deduction as follows:

$20,000 × 10/96 = $2,083

He entered $2,083 on line 536 of Schedule 3. He also entered this amount on line (a) in Part A of Form T936, *Calculation of Cumulative Net Investment Loss (CNIL) to December 31, 1992.*

Since Raju did not receive full payment for the sale in the year he sold the cottage, he may claim a reserve. However, even though he will not receive the total selling price for nine years, he cannot spread the capital gain that he has to report over more than five years.

Raju's maximum reserve for 1992 is (a) or (b), **whichever is less**:

(a) $\frac{\$20,000}{\$75,000} \times \$45,000 = \$12,000$

**or**

(b) $\frac{\$20,000}{5} \times (4 - 0^{*}) = \$16,000$

* No taxation years have ended since the year of the sale. As a result, Raju does not have to reduce the number "4" in this calculation.

Raju entered the $12,000 reserve on line 388 of form T2017. In addition, just as he calculated the portion of his capital gain that was not eligible for the capital gains deduction, he also did the same for his reserve. To do this, he calculated the portion as follows:

$12,000 × 10/96 = $1,250

He entered $1,250 at line 397 of form T2017. He then entered this amount on line (b) in Part A of form T936. He completed Part A of form T936 as follows:

| | | |
|---|---|---|
| Line 536 (capital gain not eligible) | $2,083 | (a) |
| Minus: Line 397 (reserve not eligible) | $1,250 | (b) |
| Capital gain not eligible for the capital gains deduction | $ 833 | (c) |
| Taxable portion (3/4 × 833) | $ 625 | (f) |

When he completes Schedule 3, *Summary of Dispositions of Capital Property in 1992*, he enters the following amounts:

| | | |
|---|---|---|
| **Line 530 and 537** | — total capital gains | $20,000 |
| **Line 538** | — total amount of reserves on form T2017 | ($12,000) |
| **Line 539** | — total capital gain | $ 8,000 |
| **Line 540** | — taxable capital gain (3/4 of $8,000) | $ 6,000 |
| **Line 536** | — gains not eligible for the capital gains deduction | $ 2,083 |

Raju reports the taxable capital gain of $6,000 on line 127 of his tax return.

In 1993, Raju has to report his 1992 reserve of $12,000 as a capital gain. Since there will still be an amount due to him at the end of 1993, he may calculate a new reserve, and deduct it from the $12,000.

# Chapter 7
# Principal Residence

This chapter explains the meaning of a principal residence, how to designate it, and what happens when you sell it. It also explains what to do in other special tax situations.

## What is your principal residence?

It is the housing unit you normally live in. Your principal residence may be:

- a house;
- a cottage;
- a condominium;
- an apartment in an apartment building;
- an apartment in a duplex; or
- a trailer, mobile home, or houseboat.

A property qualifies as your principal residence, for any year, if it meets the following four conditions:

- It is a housing unit, a leasehold interest in a housing unit, or a share of the capital stock of a co-operative housing corporation.
- You own the property alone or jointly with another person.
- You, your spouse, your former spouse, or any of your children lived in it at some time during the year.
- You designate the property as your principal residence.

The land on which your home is located can be part of your principal residence. Usually, the amount of land that you can consider as part of your principal residence is limited to **one-half hectare** (approximately one acre). However, if you can show that you need more land to use and enjoy your home, you can consider more than this amount as part of your principal residence. For example, this may happen if the minimum lot size imposed by a municipality at the time you bought the property is larger than one-half hectare.

## How do you designate your home as your principal residence?

For each year that you own your home and use it as your principal residence, you can designate it as your principal residence. However, you do not have to designate it each year. You only have to do it in the year that you sell or are considered to have sold your principal residence. Refer to "Did you sell all or part of your principal residence?" in the next section.

**For 1982 and any years after**, you can designate only one home as your family's principal residence for each year.

For 1982 and any years after, during which you were married, or were 18 years of age or older, **a family includes**:

- you;
- a person who throughout the year was your spouse (unless you were separated for the entire year under the terms of a court order or a written agreement); or
- your child (other than a child who was married during the year, or who was 18 years of age or older).

For 1982 and any years after, during which you were **not** married, or 18 years of age or older, **a family includes:**

- your mother or father; or
- your brother or sister (who was not married during the year or who was 18 years of age or older).

**For years before 1982**, you can designate **more** than one home per family as a principal residence. As a result, it is possible for a husband and wife to designate different principal residences for these years. However, a special rule applies if members of a family designate more than one home as a principal residence for years before 1982. For more information, see Interpretation Bulletin IT-120, *Principal Residence*.

## Did you sell all or part of your principal residence?

When you sell your home or when you are considered to have sold your home, you usually do not have to pay tax on any gain from the sale. This is the case if it was your principal residence for every year you owned it. Also, you do not have to report the sale of your home on your tax return.

If it was not your principal residence for every year you owned it, there could be a capital gain that you have to include in your income. The gain will be on the part that does not qualify as your principal residence.

Form T2091(IND), *Designation of a Property as a Principal Residence by an Individual*, will help you calculate the part of the gain, if any, that is taxable. Complete form T2091(IND), if you:

- sold your principal residence, or any part of it;
- granted someone an option to buy your principal residence, or any part of it; or
- were considered to have sold your principal residence, or any part of it. For more information, see the next section in this chapter called "Special situations."

If your home **was not** your principal residence for every year that you owned it, form T2091(IND) will be able to determine:

- the number of years that you were entitled to designate your home as your principal residence; **and**
- the amount of capital gain that you have to report on your tax return.

You only have to include form T2091(IND) with your tax return if you have to report a capital gain. Report this amount on line 530 of Schedule 3. Also, your taxable capital gain may be eligible for the capital gains deduction. For more information about this deduction, see Chapter 5.

## Special situations

When you sell your principal residence, you may have a taxable capital gain if you:

- rented out part of the residence;
- used part of the residence to operate a business; or
- designated or chose another home as your principal residence.

### Changing your property's use to a rental or business operation

You may be living in a home that you have designated as your principal residence. However, you may decide that you would like to change the use of your home. You might want to rent it out, or use it to operate a business. If you do this, we would consider that you are no longer using your home for your own personal use or enjoyment. You would be using it to earn or produce income.

At the time you change the use of your property, two things happen. You are considered:

- to have sold the property at its fair market value (FMV); and
- to have immediately purchased the property for the same FMV.

By knowing the FMV, you will be able to tell if you have any capital gain on the property. However, if your home was your principal residence for every year you owned it before you changed its use, you do not have to pay tax on any gain when you changed its use.

If at some point, you stop using the property to earn income but do not actually sell it, you are considered to have sold it again. In this case, your capital gain would be the **increase** in the FMV during the time you used the property to earn income.

You have to report any capital gain that you make from the property on line 522 of Schedule 3. You usually have to do this in the calendar year that you changed the property's use.

### Elections

When you change your principal residence to a rental or business property, you can make a special election. With this election, you can choose **not** to be considered as having started to use your principal residence as a rental or business property. This means you **do not** have to report any capital gain when you change its use. However, you can only make this election if:

- you report the net rental or business income you earn;
- you do not claim capital cost allowance (CCA) on the property; and
- you do not designate any other property as your principal residence during this time.

You make this election by enclosing a signed letter with your tax return that:

- describes the property; and
- states that you are making your election under subsection 45(2) of the *Income Tax Act*.

You can designate the property to be your principal residence for up to four years while your election is in effect.

You can **extend** the four-year limit indefinitely if:

- you are absent from your principal residence because your employer, or your spouse's employer, wants you to relocate;
- you and your spouse are not related to the employer;
- you return to your original home while still with the same employer, or before the end of the year following the year in which this employment ends; **and**
- your original home is at least 40 kilometres farther than your temporary residence from your, or your spouse's, new place of employment.

If you started to use your principal residence as a rental or business property in the year, you may want information on reporting business or property income. If you do, get the *Business and Professional Income Tax Guide*, or the *Rental Income Tax Guide*.

### Using part of your principal residence for a rental or business operation

You are usually considered to have changed the use of part of your principal residence when you start to use that part for rental or business purposes. You are also considered to have sold that part at its FMV at that time. However, you are **not** considered to have changed its use if:

- the part you use for rental or business purposes is small in relation to the whole property;
- you do not make any major structural changes to the property to make it more suitable for rental or business purposes; **and**
- you do not deduct any CCA on the part you are using for rental or business purposes.

If you meet all of the above conditions, the whole property may qualify as your principal residence, even though you are using part of it for rental or business purposes.

If, before you changed its use, the property was your principal residence for every year since you owned it, there is no capital gain at the time you changed its use.

However, if all the previously mentioned conditions are not met, when you actually **sell** the property:

- you have to split the selling price and the adjusted cost base between the part used for the principal residence and the part used for the business. You can do this by using either square metres or the number of rooms, as long as the split is reasonable; and
- you do not have to report any capital gain for the part being used for the principal residence. Any capital gain on the part used for rental or business purposes may be eligible for the capital gains deduction. See Chapter 5 for more information.

### Changing your rental or business operation to a principal residence

If you buy a property to use as a rental or business property, and later begin to use it as your principal residence, you are considered to have sold the property at its FMV at the time you change its use.

You can elect to postpone reporting the disposition of your property until you actually sell the property. However, you **cannot** make this election if:

- you;
- your spouse; or
- a trust under which you or your spouse is a beneficiary;

has deducted CCA on the property for any taxation year after 1984, and on or before the day you change its use.

To make this election, you have to attach a signed note to your return that:

- describes the property; and
- states that you are making your election under subsection 45(3) of the *Income Tax Act*.

You have to make this election by the earlier of the following dates:

- 90 days after the date Revenue Canada, Taxation asks you to make the election; or
- April 30th following the year in which you actually sell the property.

If you make this election, you can designate the property as your principal residence for up to four years before you actually occupy it as your principal residence.

This election only applies to a capital gain. If you claimed CCA on the property before 1985, you have to include any recapture of CCA in your business or rental income. You include the income in the year you changed the use of the property. If you need more detailed information on the recapture of CCA, get the *Business and Professional Income Tax Guide*, or the *Rental Income Tax Guide*.

## Farms

If you are a farmer and you sell farmland in 1992 that includes your principal residence, you have a choice of two methods to calculate your capital gain. These two methods are explained in the *Farming Income Tax Guide*.

# Chapter 8
# Leaving or Entering Canada

## Who should read this chapter?

You should read this chapter if you:

- entered and became a resident of Canada (immigrated) in 1992; or
- left and ceased to be a resident of Canada (emigrated) in 1992.

## Did you leave Canada in 1992?

If you emigrated, you are considered to have sold all your capital property at the time you leave. However, this does not include taxable Canadian property.

Taxable Canadian property includes:

- real property located in Canada;
- shares of Canadian private corporations;
- capital property used in a business in Canada;
- certain shares of public corporations;
- a capital interest in a Canadian trust, except certain mutual fund trusts; and
- an interest in certain partnerships.

### Other capital property

At the time you emigrate, you are considered to have sold all other capital property at its fair market value (FMV). Examples of such property are publicly traded shares, listed personal property, and personal-use property. You have to report any capital gain or loss in the year that you emigrate.

When you sell capital property, you usually have to pay income tax on the sale. You have to pay your income tax by April 30 following the year you leave Canada. However, you can make certain elections on the tax you have to pay, and the capital property you are considered to have disposed of.

When you emigrate and sell your capital property, you can elect to pay any resulting tax in up to six yearly instalments. You can do this if you:

- provide acceptable security (for more information, contact the Collections Section at your district office); and
- file Form T2074, *Election Under Subsection 159(4) to Defer Payment of Income Tax on the Deemed Disposition of Property*. You have to file this form by the date your last income tax return (as a person residing in Canada) is due.

If you elect to make yearly instalments, we will charge you interest on the unpaid balance until you complete your payments.

### Options for disposing of property

If you are considered to have sold your capital property when you emigrate, you may want to consider the following two options.

#### Option 1

You may choose to be considered to have sold your taxable Canadian property immediately before you emigrate. This allows you to take advantage of the capital gains deduction if you are eligible to claim it. To do this, you have to:

- Report the sale of the property on Schedule 3, *Summary of Dispositions of Capital Property in 1992*. This schedule is in the *General Tax Guide* and return package.
- Fill in Form T657, *Calculation of Capital Gains Deduction for 1992 on All Capital Property*, or Form T657A, *Calculation of Capital Gains Deduction for 1992 on Other Capital Property*. You should also fill in Form T936, *Calculation of Cumulative Net Investment Loss (CNIL) to December 31, 1992*. Include these forms with your return for the year you emigrate.
- Fill in Form T2061A, *Election by an Emigrant to Report Deemed Dispositions of Taxable Canadian Property and Capital Gains and/or Losses Thereon*. You have to file this form by the date your last income tax return (as a person residing in Canada) is due.

#### Option 2

You may also choose to have some, or all, of your capital property considered as not having been sold. This property will then be considered to be taxable Canadian property. As a result, you will not have a capital gain or loss until you actually sell, or are considered to have sold, the property. To do this, you have to:

- Provide acceptable security for the payment of any tax you are postponing (for more information, contact the Collections Section at your district office).
- File Form T2061, *Election by an Emigrant to Defer Deemed Disposition of Property and Capital Gains Thereon*. This form is due by the date your last income tax return (as a person residing in Canada) is due.

If you choose to follow either of these options, we will limit the amount of allowable capital losses that you may deduct from the property you are considered to have sold. The amount you may deduct is limited to the **lesser** of:

- the total of the allowable capital losses from the deemed dispositions; and
- the taxable capital gains arising from the deemed dispositions of such property.

You may be eligible to claim the capital gains deduction. We explain when you can claim this deduction later in this chapter.

**Tax Tip**

Before you decide whether you would like to consider these options, you should carefully assess your situation. Consider your taxable capital gains, allowable capital losses, capital gains deduction, and your cumulative net investment loss.

## Did you enter Canada in 1992?

When you immigrate, you are considered to have bought all your capital property at its FMV at the time you enter Canada. However, this rule does not apply to:

- taxable Canadian property; and
- property that is considered to be taxable Canadian property because of an election you made when you left Canada.

As a result, when you enter Canada you have to:

- make a list of all the property you own; and
- note the FMV of each property at that time.

If you later decide to dispose of any of your property, remember that the cost of each property is its FMV at the time you entered Canada. You will need to know this amount when you calculate any capital gain or loss.

## Are you entitled to claim the capital gains deduction?

You cannot claim the capital gains deduction if you are not a resident in Canada at any time in 1992. You can claim this deduction if you resided in Canada for all of 1992. However, you are considered to be a resident of Canada for the entire year if you were resident in Canada at **any time in 1992** and:

- you were also resident in Canada for all of 1991; or
- you are resident in Canada for all of 1993.

The capital gains deduction applies to any eligible capital gains (see page 27 in Chapter 5) that you had on property you disposed of, or on property that is considered to have been disposed of.

If you emigrated or immigrated, there are several situations you may find yourself in. In each situation, you may or may not be entitled to claim the capital gains deduction.

**If you emigrated in 1992**, you can claim the capital gains deductions for 1992 if you resided in Canada:

- at any time in 1992; and
- for all of 1991.

**If you immigrated in 1992**, but did not reside in Canada for the entire year, you cannot claim the capital gains deduction for 1992 until you reside in Canada for all of 1993.

**If you immigrated in 1991**, and resided in Canada for all of 1992, you can claim the capital gains deduction for 1991. To do this, see the section called "Common questions and answers" in the *General Tax Guide*.

### You were asking...?

Q. I immigrated to Canada in May 1991. Later in 1991, I sold some shares and had a capital gain that I reported on my 1991 return. I knew that I was not eligible to claim the capital gains deduction at that time. However, I heard that I am now eligible for the deduction, and that I can have my 1991 return adjusted. Is this correct?

A. If you resided in Canada for all of 1992, you can claim the capital gains deduction for 1991.

For more information about the capital gains deduction, see Chapter 5.

If you would like more information about capital property and what happens to it when you leave or enter Canada, get the *Tax Guide for New Canadians*, or the *Tax Guide for Emigrants*. You can also get Interpretation Bulletin IT-451, *Deemed Disposition and Acquisition on Ceasing to be or Becoming Resident in Canada*.

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