Wealth Management

the Navigator

INVESTMENT, TAX AND LIFESTYLE PERSPECTIVES FROM RBC FAMILY OFFICE SERVICES

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Separating a joint account between you and your spouse

What happens when you have assets in a joint account with your spouse and together you decide to separate the assets into one or more individual accounts? This article discusses the tax consequences of separating the assets in a joint account under two different circumstances. It assumes that you and your spouse initially contributed equally to the joint account. ***Please note that any reference to a spouse in this article also refers to a common-law partner.***

The content of this article does not apply to the Joint – Gift of Beneficial Right of Survivorship (JGBRS) account (not available in Quebec).

Separating the joint account

Assume you and your spouse own a joint account that holds assets with a fair market value (FMV) of $100,000 and an adjusted cost base (ACB) of $30,000. When the account was created, you and your spouse equally contributed to the joint account. You and your spouse now decide you want to divide up the assets. Let's consider the tax implications that would result in each of the following two scenarios:

1. You transfer 100% of the assets to a sole account owned by your spouse.
2. You transfer 50% of the assets to your sole account and 50% to a sole account owned by your spouse.

Scenario 1: You transfer 100% of the assets to a sole account owned by your spouse

Generally, capital property, such as a passive investment portfolio, transfers automatically between spouses at cost. As such, if all the assets in your joint account are transferred to your spouse in-kind, it will be a tax-deferred transaction. Assuming you both contributed $15,000 to the joint account, you will dispose of your half of the securities for $15,000, resulting in no immediate tax consequences. The assets in your spouse's new account will have an ACB of $30,000 ($15,000 they originally contributed + $15,000 of investments transferred from you).

Tax consequences will arise when your spouse subsequently earns income or disposes of the investments you transferred to their sole name account. Any income earned on your share of the assets transferred to your spouse's sole name account will be attributed back to you. Similarly, when your spouse subsequently sells the assets you transferred to them, the resulting capital gain or loss relating to those assets will also be attributed back to you. This means that generally, 50% of the income and capital gains earned in your spouse's sole name account will attribute back to you and be taxable in your hands.

To avoid this attribution, your spouse must pay you $50,000 (i.e. 50% of the FMV of the account) with their own money. You must also file an election with your tax return to have the transfer take place at FMV and elect out of the spousal rollover provisions. You will have to report a capital gain of $35,000 ($50,000 proceeds – $15,000 ACB) on your tax return. Your spouse will then have a total ACB of $65,000 ($15,000 they originally contributed + $50,000 of investments purchased from you). If your spouse eventually sells the purchased assets, any gain or loss will be taxed in their hands.

This example describes a situation where you sell securities in a gain position to your spouse. If instead, you sell a security in a loss position to your spouse at FMV, and your spouse holds that security on the 30th day after the settlement date of the disposition, your loss will be denied under the superficial loss rules. If you would like to claim the capital loss on your tax return, consider selling the security on the open market and ensuring that neither you nor your spouse, nor any other affiliated person (which includes a trust of which you or your spouse are a majority interest beneficiary or a corporation controlled by you or your spouse), purchases the identical security in the 30 days before and 30 days after the settlement date of disposition and holds that security on the 30th day after the settlement date of the disposition.

Alternatively, you may want your spouse to benefit from a planning strategy that uses these superficial loss rules to transfer the capital loss to your spouse. This strategy involves first selling the securities in a loss position to your spouse at FMV. Your spouse will need to pay for the securities with their own money. Your spouse then holds the securities for at least 30 days. By doing so, your loss is denied under the superficial loss rules. The superficial loss rules also require your spouse to add your denied capital loss to the ACB of the security they purchased from you. This effectively allows your spouse to get the benefit of the capital loss when they eventually sell the security. Next, your spouse sells all of the securities on the market and realizes a capital gain or loss. Your spouse will benefit from a smaller capital gain or larger capital loss because of their higher ACB. Lastly, you will need to file an election with your tax return to have the initial transfer to your spouse take place at FMV, rather than at cost.

Tax consequences will arise when your spouse subsequently earns income or disposes of the investments you transferred to their sole name account.

Transferring capital losses to your spouse using this strategy can make sense in situations where you don't have offsetting capital gains but your spouse has taxable capital gains in the current year, or previous three years.

Scenario 2: You transfer 50% of the assets to your sole account and 50% to a sole account owned by your spouse

In this scenario, both your interest and your spouse's interest in the securities are transferred from the joint account to your own individual accounts. Each security held in the joint account is equally divided between you and your spouse. In such a case, there is no disposition for tax purposes. The resulting two individual accounts will each have securities with a FMV of $50,000 and an ACB of $15,000. The attribution rules should not apply on the income earned in the accounts or if either you or your spouse subsequently dispose of the assets in your respective accounts.

Unequal contributions

If you and your spouse initially made unequal contributions to the joint account, the resulting tax implications will differ from what has been described in the previous scenarios. Attribution may apply and the amount subject to attribution will depend on the amount of funds you initially contributed to the joint account and the amount you ultimately transferred to your spouse.

Consider your circumstances

The tax consequences of separating the assets in a joint account will vary depending on your intentions and your circumstances. Always consult with a qualified tax advisor before acting on any information in this article.

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



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