Tax and Revenue Administration (TRA)

Alberta Corporate Income Tax Act
Information Circular CT-7R3
Calculation and Deduction of Losses

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NOTE: This Information Circular is intended to explain legislation and provide specific information. Every effort has been made to ensure the contents are accurate. However, if a discrepancy should occur in interpretation between this information circular and governing legislation, the legislation takes precedence.

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Calculation and Deduction of Losses

This Information Circular discusses the rules and procedures to be followed by a corporation in calculating and deducting losses under the *Alberta Corporate Tax Act* (the Act). It also describes the effect of a loss carry-back on interest and penalty charges and interest credits under the Act.

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With some modification, the Act adopts the definitions for losses and the rules for their use from the federal *Income Tax Act* (the federal Act). This Information Circular assumes the reader is familiar with many of the federal concepts concerning losses, and focuses on net capital and non-capital losses, which are the most common losses processed by TRA.

TAX AND REVENUE ADMINISTRATION
9811 - 109 STREET, EDMONTON AB T5K 2L5

- Email: TRA.Revenue@gov.ab.ca
- Website: tra.alberta.ca
- Phone: 780-427-3044
- Fax: 780-427-0348

Note: for toll-free service in Alberta, call 310-0000, then enter the number.

Calculating Non-Capital Losses

1. In its calculation of income or loss for a year, a corporation may claim different discretionary amounts for Alberta purposes than the corresponding amounts claimed for federal purposes. It could therefore calculate a non-capital loss for Alberta purposes that is different than the amount calculated for federal purposes.

2. The amount of non-capital loss calculated for Alberta purposes may also differ from the amount of the federal loss because of the modifications in the Act to the federal definition of non-capital loss. The modifications relating to the calculation of losses are:

   a. The federal Act permits a corporation to increase its taxable income to claim additional foreign tax credits. The amount added to taxable income is also added to the corporation's non-capital loss for the year. A corporation may choose to increase its taxable income for Alberta purposes by any amount up to the amount used to increase taxable income for federal purposes. The non-capital loss, if any, for the year for Alberta purposes will be increased by the same amount as the increase to taxable income for Alberta purposes.

   b. The federal Act permits a private corporation to deduct all or part of a non-capital loss from its federal Part IV tax base instead of from its income. Because Alberta does not impose the equivalent of a Part IV tax, this use of losses does not apply for Alberta purposes. Accordingly, non-capital losses available for Alberta purposes are not reduced by any amount deducted from the federal Part IV tax base.

3. A common error noted by TRA in the calculation of a non-capital loss occurs when charitable donations are involved. In calculating taxable income on the federal T2 Corporation Income Tax Return, charitable donations and other items, such as taxable dividends, are shown as deductions from net income to arrive at taxable income. However, although charitable donations are deductible in the calculation of taxable income, they cannot be used to create or increase a non-capital loss. In contrast, taxable dividends are deductible in the calculation of taxable income and are added in the calculation of a non-capital loss. The difference in the treatment arises because the definition of non-capital loss in the federal Act specifically includes taxable dividends, but does not include charitable donations.

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The following table illustrates the treatment of $20 of charitable donations and $15 of taxable dividends:

	Case 1	Case 2	Case 3
Net income (loss) from business	$100	$(100)	$ 5
Charitable donations	(20)	0	0
Taxable dividends received	(15)	(15)	(15)
Taxable income	$ 65	$ 0	$ 0
Non-capital loss	$ 0	$(115)	$ (10)
Charitable donations available for carry-forward to subsequent years	$ 0	$ 20	$ 20

Charitable donations that cannot be deducted in the year they are made may be carried forward to any of the next five years. A schedule that shows charitable donations carried forward should be included with the Alberta Corporate Income Tax Return (AT1).

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Deducting Losses in Years Other Than the Loss Year

4. A corporation may apply unused losses by deducting them from income earned in the current or a previous taxation year, or may carry them forward to a future taxation year. Losses may be deducted in any order but, for each type of loss, the oldest available loss should be deducted first. The number of taxation years back and forward to which a loss may be applied are summarized in the following table.

TYPE OF LOSS	BACK	FORWARD	APPLIED AGAINST
Net capital	3 taxation years	Indefinitely	Taxable capital gains
Non-capital	3 taxation years	20 taxation years	Any income
Farm	3 taxation years	20 taxation years	Any income
Restricted farm	3 taxation years	20 taxation years	Net farming income
Listed personal property	3 taxation years	7 taxation years	Listed personal property gains
Limited partnership	No carry-back	Indefinitely	Same partnership's income

5. Except for net capital losses, a corporation cannot use another year's losses to create or increase a non-capital loss for the taxation year.

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6. Generally, when allowable capital losses are more than taxable capital gains, the difference is a net capital loss. The inclusion rate used to determine taxable capital gains and allowable capital losses is 50%. Therefore, an **allowable** capital loss is 50% of a capital loss, and a **taxable** capital gain is 50% of a capital gain.

7. Subject to the limitations described in paragraphs 25 to 27, a corporation may, in a year, deduct a different amount of loss for Alberta purposes than that deducted for federal purposes. Doing so could be advantageous for a corporation that, for example, has earned federal tax credits and desires to use the credits before deducting losses. The corporation may carry forward its losses for federal purposes while maximizing its loss claims for Alberta purposes.

8. Unlike taxable income, which must be allocated among jurisdictions in which a corporation has a permanent establishment, a loss is not allocated in the year it is incurred. Instead, the loss is carried over to another year and deducted from net income for tax purposes to arrive at the taxable income for that year. The resulting amount is then allocated among the jurisdictions for that year.

   For example, assume that a corporation has permanent establishments in Alberta and Manitoba. In Year 1, 60% of taxable income is allocated to Alberta and 40% to Manitoba. Year 2 is a loss year but, if there had been taxable income in Year 2, it would have been allocated 80% to Alberta and 20% to Manitoba.

	Year 1 Initial Assessment	%	Year 2 Initial Assessment	%	Year 1 After Loss Deduction	%
Taxable income (loss)	$10,000		$(5,500)		$4,500	
Allocated to Alberta	6,000	60%	0	80%	2,700	60%
Allocated to Manitoba	4,000	40%	0	20%	1,800	40%

   Note that the loss deduction is made before allocation. Therefore, the taxable income of $10,000 in Year 1 less the loss of $5,500 from Year 2 results in revised taxable income of $4,500 for Year 1. This revised amount is then allocated to the provinces using the allocation factors (percentages) that existed in Year 1. The percentages in Year 2 (the year the loss was incurred) are not relevant to the allocation of taxable income in Year 1.

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Loss Claims after Reorganizations

Acquisition of Control

9. A corporation's ability to deduct previously unused losses is restricted when control of the corporation is acquired. Where control of a corporation is acquired, the federal Act provides that the taxation year of the corporation is deemed to end immediately before the time that control is acquired, and a new taxation year is deemed to begin immediately after the time control is acquired. For loss purposes, the taxation year that ended is considered a full year in any count for determining a loss carryover period.

10. Net capital losses incurred before an acquisition of control cannot be deducted in taxation years following the acquisition of control. Net capital losses incurred following an acquisition of control cannot be deducted in taxation years before the acquisition of control.

11. Generally, non-capital losses incurred before an acquisition of control cannot be deducted in years following the acquisition of control. However, the federal Act permits a corporation, in computing its taxable income for a taxation year ending after an acquisition of control, to deduct a non-capital loss incurred before the acquisition of control if

    a. the loss was a loss from carrying on a business, and

    b. the business in which the loss was sustained (the Business) is carried on for profit or with a reasonable expectation of profit throughout the taxation year in which the corporation wishes to deduct the loss.

12. Similarly, non-capital losses incurred following the acquisition of control generally cannot be deducted in taxation years before the acquisition of control. However, the federal Act permits a corporation, in computing its taxable income for a taxation year ending before an acquisition of control, to deduct a non-capital loss incurred after the acquisition of control if

    a. the loss is a loss from carrying on a business, and

    b. the business in which the loss was sustained (the Business) was carried on for profit or with a reasonable expectation of profit, both throughout the taxation year in which the loss was sustained and during the taxation year in which the corporation wishes to deduct the loss.

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13. Once the criteria described in paragraphs 11 or 12 are met, the loss that may be deducted in the taxation year is limited to

    a. the total income arising in the taxation year from the Business, and

    b. the total income arising in the taxation year from another business, if

        i. before the acquisition of control, the Business included the selling, leasing, renting or developing property or rendering services, and

        ii. substantially all of the income from the other business was derived from the sale, lease, rental or development of similar properties or the rendering of similar services.

14. Whether a corporation carried on “the Business” is a question of fact. Factors to be considered in determining whether the Business was being carried on include the following,

    - location of the business carried on before and after the acquisition of control
    - nature of the business
    - name of the business
    - nature of income-producing assets
    - existence of a period or periods of dormancy
    - extent to which the original business constituted a substantial portion of the activities of the corporation in the allocation of time and financial resources.

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Amalgamations

15. Unless otherwise expressly permitted by legislation, the corporation entitled to use a loss is the corporation that incurred the loss. Accordingly, upon an amalgamation of corporations, losses incurred by the predecessor corporations ordinarily cannot be deducted by the successor corporation nor may losses incurred by the successor corporation be deducted by its predecessors. However, the Act has adopted provisions of the federal Act that provide for certain exceptions that apply to amalgamations of taxable Canadian corporations, as described below.

16. A successor corporation is allowed to deduct losses of its predecessor corporations in the same manner and to the same extent that such losses would have been deductible by the predecessor corporations had there not been an amalgamation. The successor corporation is deemed to be the same corporation as, and a continuation of, each predecessor corporation. As a result, any loss of a predecessor corporation will be treated as the loss of the successor corporation. The losses of the predecessor corporations "age" by one year since each of these corporations was deemed to have a taxation year end immediately before the amalgamation and that taxation year is counted for the purposes of the loss carryover period.

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17. The exception described in paragraph 16 does not allow losses of the successor corporation to be carried back for deduction by a predecessor corporation. However, for amalgamations of a parent corporation and one or more of its wholly-owned subsidiaries, the successor corporation is permitted to carry back to the predecessor parent corporation losses it incurs after the amalgamation. Note that there is no provision that allows prior losses of the subsidiaries to be carried back for deduction by the parent corporation.

18. The restrictions that are placed on loss use following an acquisition of control take priority over the relieving provisions for amalgamations. For example, if an amalgamated corporation inherits a net capital loss carry-forward from a predecessor, that loss will expire if, subsequently, there is an acquisition of control of the amalgamated corporation.

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Wind-ups

19. Losses of a corporation normally expire upon the winding-up of the corporation. However, where a subsidiary corporation (a Canadian corporation) has been wound up into its parent (also a Canadian corporation), the subsidiary’s net capital losses, non-capital losses, farm losses, restricted farm losses and limited partnership losses are generally deemed to be losses of the same type to the parent for the taxation year of the parent in which the subsidiary’s loss year ended. Immediately before the winding-up, the parent must have owned at least 90% of each class of the subsidiary's capital stock and any shares not owned by the parent must have been owned by persons with whom the parent was dealing at arm's length.

20. The exception described in paragraph 19 will apply to a loss of the subsidiary, provided that any such loss

   a. was not previously deducted in computing the taxable income of the subsidiary, and

   b. would have been deductible in computing the taxable income of the subsidiary for any taxation year beginning after the commencement of the winding-up on the assumption that it had such a taxation year, and sufficient income to use the loss.

21. However, such losses are available to the parent in computing its taxable income only for taxation years **beginning after the commencement of the winding-up** (generally, the commencement of a winding-up is evidenced by a resolution of shareholders authorizing or requiring that the corporation be wound up).

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22. If a subsidiary has a loss in a taxation year that **starts after its winding-up has commenced**, the parent may elect under the federal Act to move that loss into a year that is one earlier than the year in which it otherwise would be deemed to have been incurred. This may hasten its deductibility to the parent. In the case where the winding-up process is of limited duration, the loss, like other subsidiary losses, will be available to the parent in its first taxation year commencing after the winding-up commenced.

23. To illustrate the points related to a wind-up, the following example is provided.

Assumptions:

- The normal taxation year end of the subsidiary is October 31
- The normal taxation year of the parent is January 31
- The winding-up of the subsidiary commenced on September 1, 20X7 and dissolution occurred on February 15, 20X8
- The subsidiary has the following unused non-capital losses

Subsidiary's Year End	Subsidiary's Unused Non-Capital Loss	Tax Year In Which Loss is Deemed Incurred by Parent	Beginning of First Tax Year that Loss is Available for Use by Parent
October 31, 20X4	$(1,200)	January 31,20X5	February 1, 20X8
October 31, 20X7	(800)	January 31, 20X8	February 1, 20X8
February 15, 20X8 (final year end on dissolution)	(500)	January 31, 20X9 (without election – see (1))	February 1, 20X9
February 15, 20X8 (final year end on dissolution)	(500)	January 31, 20X8 (with election – see (2))	February 1, 20X8

Assumed Elections:

(1) The parent has not elected to move the subsidiary's unused loss of $500 into the preceding year (as described in paragraph 22).

(2) The parent has elected to move the subsidiary's unused loss of $500 into the preceding year (as described in paragraph 22).

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Summary of Results:

- The non-capital loss of $1,200 for the subsidiary's 20X4 year is deemed to be a non-capital loss incurred by the parent for its year ended January 31, 20X5. Similarly, the non-capital loss of $800 for the subsidiary's 20X7 year is deemed to be a non-capital loss incurred by the parent for its year ended January 31, 20X8. The parent cannot use these losses before its year ended January 31, 20X9, which begins February 1, 20X8 and is the first year of the parent that starts after the winding-up commenced on September 1, 20X7.

- By not filing the election described in paragraph 22, the non-capital loss of $500 for the subsidiary’s short year ended February 15, 20X8 is deemed to be a non-capital loss incurred by the parent for its year ended January 31, 20X9. The parent cannot use this loss in that year because a loss cannot be deducted in the year in which it was incurred.

- By filing the election described in paragraph 22, the loss of $500 for the subsidiary’s short year ended February 15, 20X8 year is deemed to be incurred by the parent for its year ended January 31, 20X8. Therefore, the parent is permitted to use this loss in its year ended January 31, 20X9.

24. The parent's use of subsidiary losses is restricted or eliminated if there is an acquisition of control of the parent during the period in which the losses could otherwise be deducted. Net capital losses expire and non-capital losses are restricted as described in paragraphs 11 and 13, above. The same restrictions apply if there was an acquisition of control of the subsidiary after its loss year and before the winding-up.

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Effect on Losses of a Change in Permanent Establishment

25. A corporation that moves into Alberta and has a permanent establishment in Alberta at any time in a taxation year becomes subject to the Act. The corporation brings its federal loss balances with it. Losses calculated, deducted or deductible under the federal Act for a previous taxation year where the corporation was not subject to the Act are deemed to have been calculated, deducted or deductible under the Act for the previous taxation year.

    For example, assume that a corporation incurred a non-capital loss of $25,000 in 20X6 and deducted $10,000 for federal purposes in 20X7. In 20X8, the corporation acquired a permanent establishment in Alberta. The $10,000 is deemed to have been deducted under the Act and the balance that is available for Alberta purposes is the same as that for federal purposes, being $15,000.

26. Similarly, if a corporation incurs a loss while it is subject to the Act and, for federal purposes, applies that loss back to a year in which the corporation was not subject to the Act, that application is deemed to have occurred for Alberta purposes.

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27. If a corporation leaves Alberta so that it is no longer subject to the Act, it can carry back, for Alberta purposes, losses incurred within three years of the last year it was subject to the Act. TRA will process a loss carry-back if the Canada Revenue Agency has allowed a corresponding deduction.

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Filing for a Loss Deduction

28. A loss carry-back is claimed by filing an "Alberta Loss Carry-Back Application – AT1 Schedule 10" (Form AT293). This includes a corporation that is exempt from filing an AT1 for the year, as explained in Information Circular CT-2, *Filing Requirements*. The loss carry-back request may not be processed if the effect on the corporation's Alberta tax payable, interest and penalties is minimal and the request does not accompany other adjustments.

29. When a loss is deducted in a taxation year that is two or more years before the year in which the loss occurred, it may affect the calculation of Alberta tax for the intervening years. TRA will process the changes required in all of the years affected.

30. When a corporation deducts a loss from an earlier year in its federal T2 Corporation Income Tax Return, the loss deduction will apply for Alberta purposes (providing there are losses available for Alberta purposes) unless the corporation specifies otherwise.

31. In any year in which a loss applied or an opening loss balance for Alberta purposes differs from the corresponding loss applied or opening loss balance for federal purposes, the corporation must file an "Alberta Calculation of Current Year Loss and Continuity of Losses - AT1 Schedule 21" (Form AT173) and an "Alberta Income/Loss Reconciliation - AT1 Schedule 12" (Form AT112).

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Effect of a Loss Carry-Back on the Corporation's Tax Account

32. A loss carry-back does not alleviate any late-filing penalty previously assessed.

33. For the purposes of calculating interest and penalties on late or deficient instalments, a reduction in tax for a year resulting from a loss carry-back is deemed to be a payment on account of tax for the year. The effective date assigned to this deemed payment is the latest of

   a. the first day following the loss year,

   b. the day on which the AT1 for the loss year is filed (if not exempt from filing as explained in Information Circular CT-2, *Filing Requirements*),

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c. the day on which the Alberta Loss Carry-Back Application - AT1 Schedule 10 is filed, and

d. the day on which a request was made for the loss carry-back.

For the purpose of criterion "d", above, the day on which a request was made for the loss carry-back is considered to be the day the request is received by TRA, provided that TRA can process the request. For example, TRA cannot process an Alberta Loss Carry-Back Application – AT1 Schedule 10 that is blank or contains amounts that cannot be supported, nor will TRA process a request if no income from which a loss may be deducted has been assessed.

34. If a corporation requests a change to a discretionary amount originally claimed in the taxation year (such as capital cost allowance) to make room for a loss carry-back, there may be the following interest implications

a. if the adjustment to the discretionary amount is acceptable (refer to Information Circular CT-6, *Reassessments*), tax is recalculated, taking into consideration the higher taxable income resulting from the change in the discretionary amount, but not taking into account the loss application,

b. interest is charged on the revised tax payable from the day tax for the year was originally due to the effective date of the loss carry-back as described in paragraph 33, and

c. the tax reduction as a result of a loss carry-back is applied as a payment on account as of that effective date, and interest is further calculated on any balance remaining.

Such interest implications can result in interest owing for a period preceding the effective date of the loss carry-back even though the tax payable after the loss carry-back is nil. In addition, if the AT1 for the year was filed late, the substitution of the loss carry-back for another discretionary deduction may result in the creation of, or increase to, a late-filing penalty.

35. Subject to provisions of the Act that allow TRA to issue a refund of an overpayment only if an AT1 has been filed within three years from the end of the taxation year, any overpayment that arises from a loss carry-back may be automatically applied to any unpaid balance on the corporation's account. The corporation may request that the remainder, or any portion of the remainder, be applied as an instalment for a subsequent taxation year. Any further amount remaining may be refunded. However, for administrative efficiency, TRA does not refund an amount less than $20.00 unless specifically requested to do so.

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