

# Mobley & Company

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## **S Corporations, Loss Deductions and Basis**

An S corporation is a corporation that generally does not pay Federal tax on its income. Instead the income flows through to the shareholders who report the income on their individual returns.

An important planning point to watch for before year end deals with a potential loss situation. If the S corporation has a loss for the year, the shareholder can deduct the loss on the individual return assuming that the shareholder has adequate "basis" for the loss. If there is not an adequate basis, the loss deduction of the shareholder will be limited.

In general, the shareholders "basis" is the acquisition cost of the stock increased by prior S corporation earnings and decreased by prior S corporation deductions and distributions. Loans made by the shareholder to the corporation also create basis for deducting losses.

If it is determined that there is not enough basis to deduct the anticipated loss, you may want to consider making an additional loan to the corporation before year end to increase your basis and thus maximize your deduction.

## **C Corporations - Capital gains and losses**

C Corporations should generally avoid investing excess cash in stocks or other capital assets, since a loss may not be deductible. Many business owners fail to remember that the rules with C Corporate Capital Gains and Losses are different for Corporations than they are for individuals. Capital Losses of C Corporations can only be used to offset Capital Gains. Furthermore, Capital Losses can only be carried back three years and forward five years. After the this time expires, a C Corporation can no longer use that loss.

You should have some means of tracking Capital Gains and Losses to prevent the expiration of unused losses.

Another point to remember regarding C Corporation Gain is that a C Corporate Capital Gain could be at a rate significantly higher than at the individuals preferential rates.