ACT 461| ACTUARIAL MATHEMATICS II
KING SAUD UNIVERSITY
COLLEGE OF SCIENCE
2019

Constructive Sale

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What is a Constructive Sale?

A simple definition of a constructive sale:

A constructive sale is created when you hold an appreciated position and enter into an opposite position in the same (or substantially identical).The taxpayer recognizes gains as if the position were closed on that date, and then immediately re-opened.

The constructive sale rule also affects the holding periods involved with the transactions.

In general, most times if there is a constructive sale, there will also be a straddle. But there is often a straddle when there is no constructive sale.

Many combinations of transactions can make up a constructive sale, including those using short positions or substantially identical securities. As a result, it is important to take into account the different interactions between constructive sales and other taxable events, such as wash sales , straddles and qualified dividends.

Example of Constructive Sales:

Example 1 - Long Constructive Sale.

Activity: The taxpayer buys a single share of stock ABC on January 3rd of 2011 for $100. On December 30th, the taxpayer shorts one share of stock ABC at $125. The short does not settle until sometime in January of 2012.

Result: The taxpayer is liable for a short-term capital gain of $25 achieved on December 30th due to a constructive sale created on that date. The cost basis adjustment is $25, meaning the cost basis of the long share purchased on January 3rd is increased from $100 to $125 and the apparent tax date of this position is reset to December 30th. But this configuration also forms a basic straddle, so the day-counter for the holding period is suspended while the basic straddle is in place.