



# Canadian income tax and day-trading

—  
November 4, 2020

**Let's do this.**



# Presenters and introduction

## About our team



**Jonathan Warren, CPA,  
CA  
Partner, Tax**



**Jake Edgar, CPA  
Manager, Tax**



**Ryan Gertzbein, CPA, CA  
Specialist, Tax**

We stay ahead of the curve.

KPMG Enterprise tax professionals want to be the clear choice for your business and tax needs.



# Agenda



## Canadian income tax basics

Types of income related to investing and day-trading.  
Realized trading gains as capital or business income.



## Is my trading activity a business?

Not a choice of the taxpayer.  
Based on the facts and key determining factors.



## Focus on day-trading activities as a business.

How to file personal taxes.  
Types of expenses deductible.  
Potential incorporation.



## Other considerations

Day-trading and TFSA.  
Loss restrictions.  
39(4) Election.  
Record-keeping.  
Foreign securities (T1135).  
Canada Pension Plan.



RESIDENT

# Canadian tax basics

Let's do this.



# Types of income

## Canadian income tax treatment (for an individual)

### Interest income

Taxed at the recipient individual's marginal income tax rate.



### Foreign dividends

Taxed at the recipient individual's marginal income tax rate and subject to withholding taxes from source country (15% if US sourced).



### Canadian dividends

Preferential tax treatment because of the dividend tax credit.



### Return of capital

Not taxable upon receipt – instead this causes adjustment to cost base of investment.  $ACB < \$\text{nil}$  treated as capital gain.



### Capital gains

More to come...

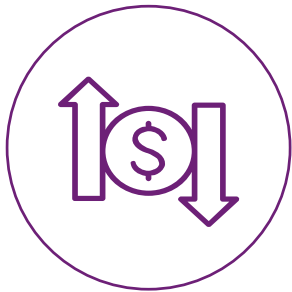


### Business income

More to come...



# Taxation of capital gains



## Special treatment Of capital gains

To foster investment in  
Canadian corporations

Realized trading gains (and losses)			
One-half taxable	Application of losses	Expenses deductible	How to report
<ul style="list-style-type: none"><li>– 50% of gain added to taxable income</li><li>– Per cent has changed over years</li></ul>	<ul style="list-style-type: none"><li>– Carry back three years</li><li>– Carry forward indefinitely</li><li>– Only apply against capital gains</li></ul>	<ul style="list-style-type: none"><li>– Generally, No expenses deductible</li><li>– Buy/sell costs added to cost base</li></ul>	<ul style="list-style-type: none"><li>– Proceeds and cost reported on Schedule 3 of T1 personal income tax return</li></ul>

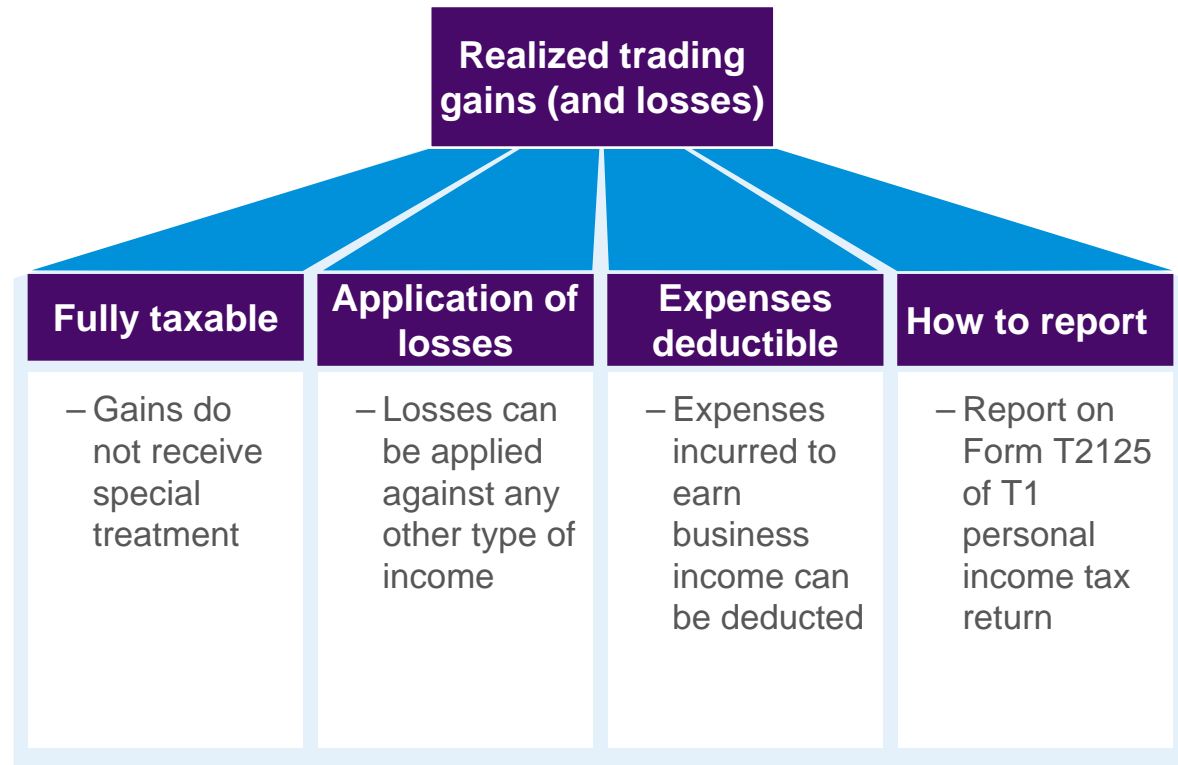
# Taxation of business income



## Realized gains

As business income

Adventure or concern in  
the nature of trade





# Determining capital vs. business income

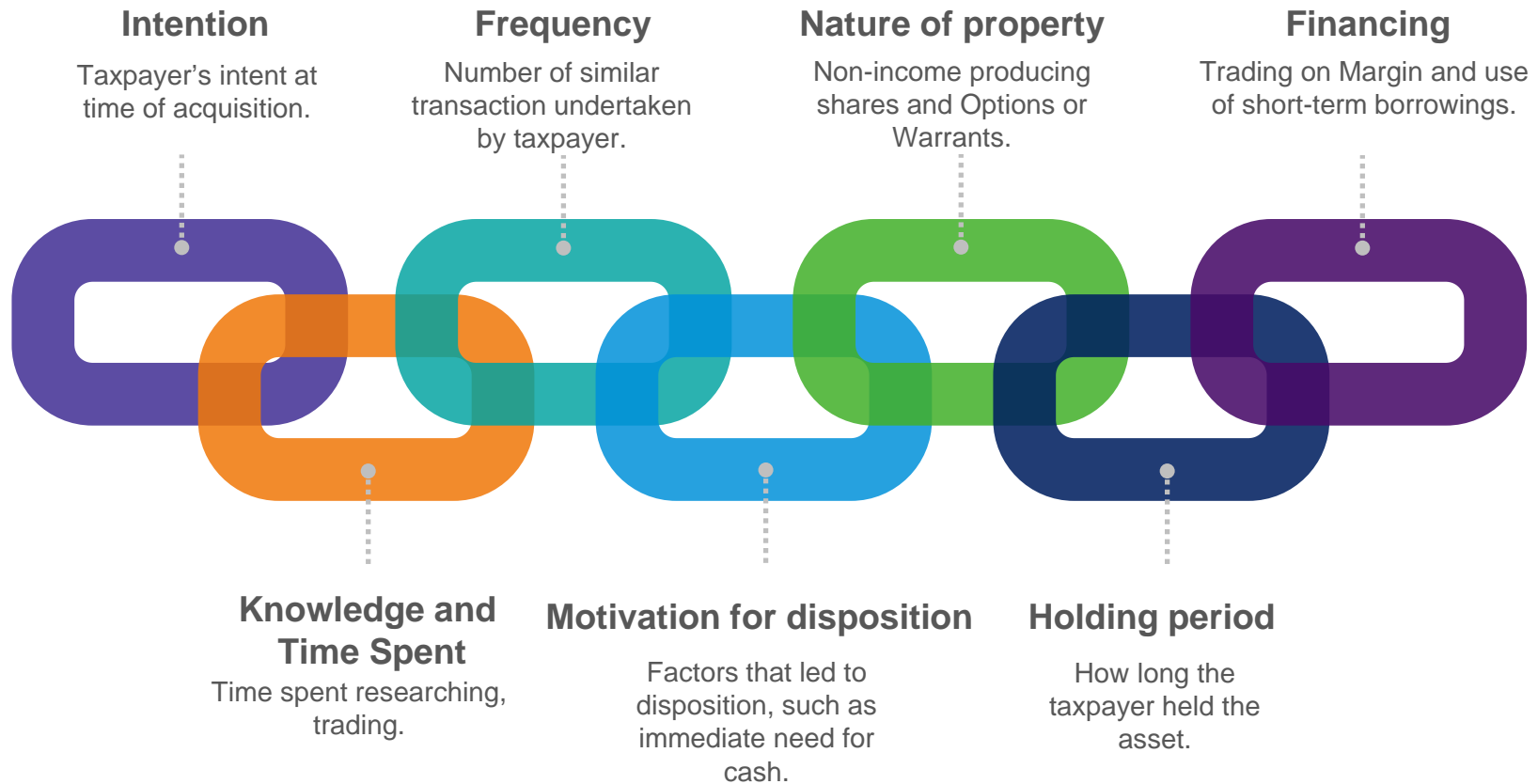
**Let's do this.**



# Capital vs business income

## Not a choice

## Determined based on the facts



# Capital vs business income

## Example portfolio

### Capital in nature

- Shares of Canadian dividend paying corporations.
- Purchased with intent to earn appreciating dividend income and benefit from long-term capital appreciation.
- Diversified portfolio.
- Limited time researching/trading.
- Sold security even after short holding period because taxpayer needs cash for personal expenditure.

### Business

- Shares of Canadian corporation that do not pay dividends.
- Purchased with intent to sell once certain threshold is reached (Stop-loss, limit orders).
- Significant time spent trading and/or researching.
- Clears position in security regularly.
- Utilizes more complex investment strategies like Options and Warrants, as well as margin account.

**No single factor is indicative of Capital or Business income**

**The Authorities look at the whole picture**

# Capital vs business income

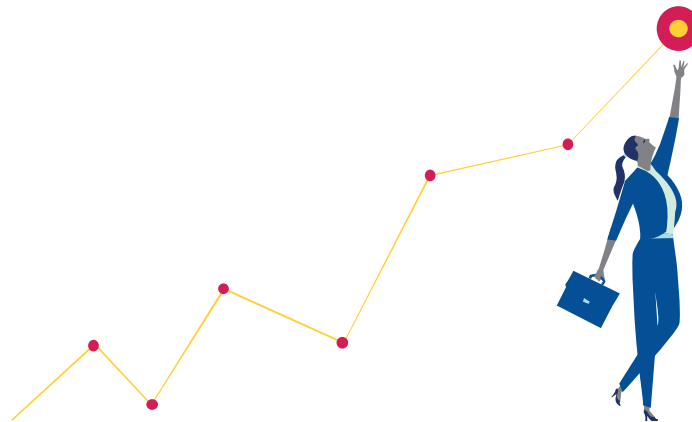
## CRA Publication IT-459 – “Adventure or concern in the nature of trade”

*“It is a general principle that when a person habitually does a thing that is capable of producing a profit, then he [or she] is carrying on a trade or business notwithstanding that these activities may be separate and apart from his [or her] ordinary occupation.”*

Also see CRA publication IT-479R – “Transactions in securities”

## What if I do both?

Maintain separate accounts!





# Day-trading as a business - Personal

Let's do this.



# Personal - Form T2125

## Statement of Business or Professional Activities

Where a taxpayer has established a business as a day-trader, the income or losses from day-trading activities would be reported on Form T2125. The securities traded would be considered “inventory” and would be reported as sales and purchases/cost of goods sold.



Protected B when completed

### Statement of Business or Professional Activities

- Use this form to calculate your self-employment business and professional income.
- For each business or profession, fill in a separate Form T2125.
- Fill in this form and send it with your income tax and benefit return.
- For more information on how to fill in this form, see guide T4002, Self-employed Business, Professional, Commission, Farming, and Fishing Income.

Part 1 – Identification					
Your name				Your social insurance number	
Business name			Business number		
Business address			City	Prov./Terr.	Postal code
Fiscal period	From	Date (YYYYMMDD)	to	Date (YYYYMMDD)	Was this your last year of business? <input type="checkbox"/> Yes <input type="checkbox"/> No
Main product or service			Industry code (see the appendix in Guide T4002)		
Accounting method (commission only)	<input type="checkbox"/> Cash	<input type="checkbox"/> Accrual	Tax shelter identification number	Partnership business number	Your percentage of the partnership %
Name and address of person or firm preparing this form					

# Personal - Form T2125

## Deductible expenses examples (must be tied to earning business income)

- Interest on debt
- Membership dues / Subscription fees
- Accounting / legal fees
- Capital cost allowance (tax depreciation)
- Travel expenses
- Home office (more on next slide)

Part 4 – Net income (loss) before adjustments		4A
Gross business or professional income (line 8299 of Part 3C) or Gross profit (line 8519 of Part 3D)		_____
<b>Expenses (enter only the business part)</b>		
Advertising	8521	_____ 4B
Meals and entertainment	8523	_____ 4C
Bad debts	8590	_____ 4D
Insurance	8690	_____ 4E
Interest and bank charges	8710	_____ 4F
Business taxes, licences, and memberships	8760	_____ 4G
Office expenses	8810	_____ 4H
Office stationery and supplies	8811	_____ 4I
Professional fees (includes legal and accounting fees)	8860	_____ 4J
Management and administration fees	8871	_____ 4K
Rent	8910	_____ 4L
Repairs and maintenance	8960	_____ 4M
Salaries, wages, and benefits (including employer's contributions)	9060	_____ 4N
Property taxes	9180	_____ 4O
Travel expenses	9200	_____ 4P
Utilities	9220	_____ 4Q
Fuel costs (except for motor vehicles)	9224	_____ 4R
Delivery, freight, and express	9275	_____ 4S
Motor vehicle expenses (not including CCA) (amount 15 of Chart A)	9281	_____ 4T
Capital cost allowance (CCA). Enter amount i of Area A minus any personal part and any CCA for business-use-of-home expenses	9936	_____ 4U
Other expenses (specify): _____	9270	_____ 4V
<b>Total expenses: Total of amounts 4B to 4V</b>		_____ 9368
<b>Net income (loss) before adjustments: Amount 4A minus line 9368</b>		_____ 9369

# Personal - Form T2125

## Home office expenses

- If the principal place of business is the home, one may be able to deduct a pro-rated portion of their home expenses as a business expense.
- For example, if the office from which one operates the business represents 10% of the square-footage of the home, one could deduct 10% of home expenses such as utilities and mortgage interest.

<b>Part 7 – Calculation of business-use-of-home expenses</b>	
Heat .....	7A
Electricity .....	7B
Insurance .....	7C
Maintenance .....	7D
Mortgage interest .....	7E
Property taxes .....	7F
Other expenses (specify): .....	7G
<b>Subtotal: Add amounts 7A to 7G</b> .....	7H
Personal-use part of the business-use-of-home expenses .....	7I
<b>Subtotal: Amount 7H minus amount 7I</b> .....	7J
Capital cost allowance (business part only), which means amount i of Area A minus any portion of CCA that is for personal use or entered on line 9936 of Part 4 .....	7K
Amount carried forward from previous year .....	7L
<b>Subtotal: Add amounts 7J to 7L</b> .....	7M
Net income (loss) after adjustments (amount 5C) (if negative, enter "0") .....	7N
<b>Business-use-of-home expenses available to carry forward: Amount 7M minus amount 7N (if negative, enter "0")</b> .....	7O
<b>Allowable claim: The lesser of amount 7M and 7N above (enter your share of this amount on line 9945 of Part 5)</b> .....	7P

# Personal - income tax

## Expected income tax

- Net business income is added to the individual's other net income (employment, etc.).
- Total taxable income of all types is taxed at the individual's marginal income tax rate and subject to regular deductions and non-refundable credits.
- Dividend income should maintain its normal treatment and not be considered business income.
  - Eligible Dividends: The corporation paid higher tax rates on the underlying income.
  - Other Than Eligible Dividends: The corporation paid lower tax rates on the underlying income.
  - Accordingly, dividend tax credit is higher for an eligible dividend.
- "Capital gains dividends" received on mutual fund or ETF holdings should also maintain their normal treatment and not be considered business income.

Individual Marginal Tax Rates for Interest<sup>1</sup>—2020

	\$0 to \$48,535	\$48,536 to \$97,069	\$97,070 to \$150,473	\$150,474 to \$214,368	\$214,369 and over
British Columbia <sup>2</sup>	20.06%	28.20%	40.70%	45.80%	49.80/53.50%
Alberta	25.00	30.50	36.00	42.00	47.00/48.00
Saskatchewan	25.50	33.00	38.50	43.50	47.50
Manitoba	25.80	37.90	43.40	46.40	50.40
Ontario	20.05	29.65	43.41	47.97	51.97/53.53
Quebec	27.53	37.12	47.46	49.97	53.31
New Brunswick	24.68	35.32	42.52	49.30	53.30
Nova Scotia	23.79	37.17	43.50	50.00	54.00
Prince Edward Island	24.80	37.20	44.37	47.37	51.37
Newfoundland and Labrador	23.70	35.00	41.80	46.30	51.30

Individual Marginal Tax Rates for Capital Gains<sup>1,2</sup>—2020

	\$0 to \$48,535	\$48,536 to \$97,069	\$97,070 to \$150,473	\$150,474 to \$214,368	\$214,369 and over
British Columbia <sup>3</sup>	10.03%	14.10%	20.35%	22.90%	24.90/26.75%
Alberta	12.50	15.25	18.00	21.00	23.50/24.00
Saskatchewan	12.75	16.50	19.25	21.75	23.75
Manitoba	12.90	18.95	21.70	23.20	25.20
Ontario	10.03	14.83	21.70	23.98	25.98/26.76
Quebec	13.76	18.56	23.73	24.98	26.65
New Brunswick	12.34	17.66	21.26	24.65	26.65
Nova Scotia	11.90	18.59	21.75	25.00	27.00
Prince Edward Island	12.40	18.60	22.19	23.69	25.69
Newfoundland and Labrador	11.85	17.50	20.90	23.15	25.65



# Day-trading as a business - Incorporation

Let's do this.



# Incorporation

## **Can I save tax by operating my business in a corporation by accessing the small business corporate tax rate?**

### **Integration**

- Generally, a Canadian taxpayer should be indifferent whether their business income is earned personally or through a corporation.
- If the earnings are extracted from the corporation by the shareholder immediately, in most Canadian provinces there is no benefit to incorporation, for top tax-rate income.

## **If there are no tax savings, why do people incorporate**

### **Deferral**

- If the funds are left in the corporation, a larger pool is available to be reinvested in the business. The immediate tax effect is a deferral of tax on that income, putting more capital to work.
- Illustration on next slide.

# Incorporation

## Illustration - Flowed through a corporation vs. earned as sole proprietor

	B.C.	ALTA.	SASK.	MAN.	ONT.	QUE.	N.B.	N.S.	P.E.I.	NFLD.
<b>INCOME EARNED THROUGH A CORPORATION</b>										
Corporate income	1,000.00	1,000.00	1,000.00	1,000.00	1,000.00	1,000.00	1,000.00	1,000.00	1,000.00	1,000.00
Corporate tax	-110.00	-110.00	-110.00	-90.00	-122.00	-140.00	-115.00	-116.24	-120.00	-120.00
Available for dist. (N-E D) (A)	890.00	890.00	890.00	910.00	878.00	860.00	885.00	883.76	880.00	880.00
Tax payable by the individual	-435.12	-376.50	-359.33	-424.73	-419.16	-405.44	-422.57	-426.63	-397.99	-392.35
Net to the individual (B)	454.88	513.50	530.67	485.27	458.84	454.56	462.43	457.13	482.01	487.65
<b>INCOME EARNED DIRECTLY BY AN INDIVIDUAL</b>										
Personal income	1,000.00	1,000.00	1,000.00	1,000.00	1,000.00	1,000.00	1,000.00	1,000.00	1,000.00	1,000.00
Personal tax	-535.00	-480.00	-475.00	-504.00	-535.30	-533.05	-533.00	-540.00	-513.70	-513.00
Net to the individual (C)	465.00	520.00	525.00	496.00	464.70	466.95	467.00	460.00	486.30	487.00
<b>SUMMARY</b>										
Tax savings (cost) of earning income through a corporation (B) - (C)	-10.12	-6.50	5.67	-10.73	-5.86	-12.39	-4.57	-2.87	-4.29	0.65
Tax deferral advantage (A) - (C)	425.00	370.00	365.00	414.00	413.30	393.05	418.00	423.76	393.70	393.00

\* This table assumes the corp. earns active business income eligible for the small business deduction.

# Incorporation

- Depending on your circumstances and cashflow needs, a corporation might work for you.
- **Each situation is unique.**
- Consider the costs of incorporation and ongoing compliance costs:
  - Requirement to file T2 corporate tax returns;
  - T4 slip if salaries are being paid; and
  - T5 slip for dividends being paid to shareholder.



# Other considerations

Let's do this.



# Other considerations

## To consider in day-trading activities

### Tax Free Savings Account [TFSA]

- “No tax payable... except that... it carries on one or more businesses...” – ITA 146.2(6)
- Therefore, carrying on the business of day-trading in a TFSA will *taint* the tax-free status and result in gains being subject to a 100% advantage tax, meaning the entire gain is taken away.
- No contribution-room for non-residents

### Foreign Securities

- If a taxpayer owns specified foreign property with a cost basis of greater than \$100,000 at any time during the taxation year, they are required to file a T1135 – Foreign Income Verification Statement.
- True whether you acquired the security directly, through a Canadian brokerage, through an online platform.
- Total holdings need to be considered. Not individual holdings or only country-by-country holdings.
- Not filing a T1135 can cause costly penalties.

### Election for Canadian Securities [ss. 39(4)]

- A taxpayer may elect pursuant to subsection 39(4) of the Act to treat all transactions in Canadian Securities as capital in nature.
- Does not apply where the taxpayer is operating a business.

# Other considerations

## To consider in day-trading activities

### Loss restrictions for individuals – Superficial losses

- Where a taxpayer has realized a loss on property or inventory, and then repurchased identical property within 30 days, that loss is denied and instead added to the cost base of the new property for income tax purposes until the new property is ultimately disposed of. This rule applies whether the taxpayer is operating a business or selling capital property.

### Record-keeping

- Taxpayers have the obligation to maintain records to support any income and expenses claims made on their tax return.
- Don't rely on your broker or trading platform to maintain these records [i.e. Quadriga exchange customers can no longer access any of their records on that platform].

### Canada Pension Plan

- Business income is self-employment income and subject to CPP requirements.

# Thank you

## Wrap up and Questions

Everyone's situation is unique and KPMG Enterprise is here to assist you.

**Jake Edgar, CPA**  
Manager, Tax  
[jedgar@kpmg.ca](mailto:jedgar@kpmg.ca)  
613-541-7402

**Ryan Gertzbein, CPA, CA**  
Specialist, Tax  
[rgertzbein@kpmg.ca](mailto:rgertzbein@kpmg.ca)  
613-541-7365





[kpmg.ca](https://kpmg.ca) #LetsDoThis



The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

© 2020 KPMG LLP, a Canadian limited liability partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved.

The KPMG name and logo are registered trademarks or trademarks of KPMG International.