TD Wealth

Investor or Trader? Your Taxes May Differ

Did you know that your approach to investing may affect how your investments will be taxed? If your approach is that of an ordinary investor, then the gains derived from the sale of your investments will likely be taxed as capital gains, which means only 50% of the gain is subject to tax. On the other hand, if your investment activities constitute operating an investment business, then 100% of the gains will be taxable as business income.

The Canada Revenue Agency (CRA) has provided a list of factors that it considers in determining whether an individual is carrying on an investment business or not.

These include:

Frequency of transactions – has there been a history of extensive buying and selling of securities?

Period of ownership – are the securities usually held for only a short period of time?

Knowledge of the securities markets – does the individual have some knowledge of, or experience in, the securities markets?

Does the individual purchase shares that are normally speculative in nature or of a non-dividend type?

Do security transactions form a part of the individual's ordinary business?

Time spent – does the individual spend a substantial part of his/her time studying the securities market and investigating potential purchases?

Financing – are security purchases financed primarily on margin or other debt?

Advertising – does the individual advertise or otherwise make it known that he or she is willing to purchase securities?

According to the CRA, it is not one but a combination of factors previously described that could render an individual's investment activities to constitute carrying on a business.

The CRA also considers a single transaction in shares may be all it takes to be carrying on a business if the conduct and intention clearly indicate it to be such.

If you would like to ensure that your investments are taxed as capital gains and not as income, you should consider filing an election (CRA form T123) with your tax return.

- The effect of such an election is that the disposition of certain investments in the year of the election and all subsequent years will, subject to certain exceptions, be treated as capital gains or losses.
- Once this election is made it cannot be revoked. The capital gains treatment provided by the election is also limited to certain Canadian investments including stocks, mutual fund trusts, and bonds.
- The election does not apply to other investments such as options or U.S. stocks.
- The election will also not apply to any transaction in which you were considered a “trader” at the time the transaction occurred. In that case, the transaction will be deemed as income and not capital gains even if you have filed an election.

It is not clear what makes a person a “trader”.

What is certain is that a trader can be anyone who carries on a business of buying and selling securities and is not limited to persons who are registered or licensed by regulatory authority.

What is less certain is whether, to be considered as a trader, the person must possess some special knowledge of the market in which the securities trade (*e.g.*, a company insider), in addition to carrying on a business.

Otherwise, the purpose behind allowing individuals to file the election may well be defeated.

Individual circumstances differ so please consult a professional tax advisor.

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