

## Income Tax

**IMP. 250.1-1/R2** Election in respect of the disposition of Canadian securities  
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Reference(s): *Taxation Act* (R.S.Q., c. I-3), ss. 21.4.6, 21.4.9, 21.4.10, 250.1, 250.1.1, 250.2, 250.3 and 250.4  
*Regulation respecting the Taxation Act* (R.R.Q., 1981, c. I-3, r.1, as amended), s. 250.2R1

*This version of interpretation bulletin IMP. 250.1-1 supersedes the version of May 31, 1994. The bulletin was revised to take into account legislative amendments and to elaborate on certain technical aspects, in particular, the amendment which provides that if a valid election is made for federal income tax purposes, the same election will be deemed made for Québec income tax purposes. Also, some changes in respect of style and conformity were made to ensure technical accuracy.*

The purpose of this bulletin is to define the rules for the election that may be made by a taxpayer in respect of all the Canadian securities owned by the taxpayer.

### GENERAL

1. The gain or loss resulting from the disposition of a Canadian security may be treated as income or a capital gain, or as a business loss or capital loss. Whether such a gain or loss is a capital gain or loss or a business gain or loss is a question of fact to be determined in each particular situation.

### APPLICATION OF THE ACT

#### ELECTION IN RESPECT OF THE DISPOSITION OF CANADIAN SECURITIES

2. Under the first paragraph of section 250.1 of the *Taxation Act* (TA), if a Canadian security is disposed of by a taxpayer in a taxation year and, as a consequence of the disposition, the taxpayer makes a valid election under subsection 39(4) of the *Income Tax Act* (R.S.C. 1985 (5th Supp.), c. 1; hereinafter "ITA") after 19 December 2006, every Canadian security owned by the taxpayer in the year or any subsequent taxation year is deemed to be a capital property owned by the taxpayer and every disposition by the taxpayer of any such Canadian security is deemed to be a disposition of a capital property.

3. Pursuant to section 250.1.1 of the TA, for the purpose of computing the income of a taxpayer who is a member of a partnership, the rules under sections 250.1 and 250.3 of the TA apply in respect of all the Canadian securities owned by the partnership as if they were owned by the taxpayer and as if all such securities disposed of by the partnership in a fiscal period were disposed of by the taxpayer at the end of that fiscal period.

4. However, according to section 250.3 of the TA, the first paragraph of section 250.1 of the TA does not apply to a disposition of a Canadian security by a taxpayer, other than a mutual fund corporation or a mutual fund trust, who, at the time of the disposition, is

- (a) a trader or dealer in securities;
- (b) a financial institution, within the meaning assigned by section 851.22.1 of the TA;
- (c) a corporation whose principal business is the lending of money or the purchasing of debt obligations, or a combination thereof; or
- (d) a person not resident in Canada.

5. A valid election made under the ITA and referred to in the first paragraph of section 250.1 of the TA does not apply to any Canadian securities disposed of during the time that section 250.3 of the TA applies to a taxpayer. During the time the election does not apply or if the election does not otherwise apply, points 15 through 19 of this bulletin are applicable in determining whether the gain realized or the loss sustained is a gain or loss of income or a capital gain or loss, unless section 250.4 of the TA applies. If section 250.3 of the TA ceases to apply, a valid election that was made previously and that is referred to in the first paragraph of section 250.1 of the TA becomes applicable again.

### **SHARES DEEMED CAPITAL PROPERTY**

6. Under section 250.4 of the TA, where a person disposes of all or substantially all of the assets used in a qualified business carried on by the person to a corporation for consideration that includes shares of the corporation, the shares are deemed to be capital property of the person.

7. Therefore, the election referred to in the first paragraph of section 250.1 of the TA cannot apply to such shares, since the disposition thereof will necessarily result in a capital gain or loss.

### **ELECTION NOT ALLOWED – TRADER OR DEALER IN SECURITIES**

8. The term “trader or dealer in securities” in section 250.3 of the TA refers to, inter alia,

- (a) a taxpayer who has a greater volume and frequency of purchase and sale transactions involving Canadian securities than what may reasonably be expected of a mere investor, as opposed to a trader;
- (b) a taxpayer who participates in the promotion or underwriting of a particular issue of shares, bonds or other securities;
- (c) a taxpayer who is held out to the public as a dealer in shares, bonds or other securities.

9. Subject to the type of situation referred to in paragraph (a) of point 8 above, the Ministère du Revenu du Québec does not usually consider a taxpayer to be a trader or dealer in securities solely because the taxpayer has carried out a commercial transaction involving Canadian securities. Consequently, the disposition of Canadian securities by such a taxpayer is not necessarily removed from the application of the election referred to in the first paragraph of section 250.1 of the TA.

10. Furthermore, the term “trader or dealer in securities” does not include an officer or employee of a firm or corporation that is engaged in the promotion or underwriting of issues of shares, bonds or other securities, or an officer or employee of a taxpayer held out to the public as a dealer in shares, bonds or other securities, unless the officer or employee carries out transactions involving securities as a result of the employer’s promotional or underwriting activities.

11. Finally, a corporation whose principal activity is trading in shares or debt obligations is considered a trader or dealer in securities. However, a corporation whose principal activity is the holding of securities and which sells such investments from time to time is not a trader or dealer in securities.

## **CANADIAN SECURITIES**

12. A Canadian security in respect of which a taxpayer may make the election referred to in the first paragraph of section 250.1 of the TA is defined in section 250.2 of the TA as a security, other than a prescribed security, that is

- (a) a share of the capital stock of a corporation resident in Canada;
- (b) a unit of a mutual fund trust; or
- (c) a bond, debenture, bill, note, hypothecary claim, mortgage or similar obligation issued by a person resident in Canada.

The Ministère considers that a security sold short is included in the definition of “Canadian security”.

13. As indicated in point 12 above, the election referred to in the first paragraph of section 250.1 of the TA cannot be made in respect of a prescribed security. According to section 250.2R1 of the *Regulation respecting the Taxation Act* (RTA), a prescribed security, for a taxpayer referred to in section 250.1 of the TA, is

- (a) a share of the capital stock of a corporation, other than a public corporation, whose value at the time of its disposition by the taxpayer is mainly attributable to a property belonging to the corporation, another person or a partnership, and that is
  - i. immovable property, or an interest or option in respect of that property;
  - ii. a Canadian mining property;
  - iii. a foreign mining property; or

- iv. a combination of the properties referred to in subparagraphs (i) to (iii);
- (b) a bond, debenture, bill, note, hypothecary claim, mortgage or other similar obligation issued by a corporation, other than a public corporation, where at any time before the disposition of the obligation, the taxpayer was not dealing at arm's length with the corporation;
- (c) a share or a bond, bill, note, hypothecary claim, mortgage or similar obligation that was acquired by the taxpayer from a person with whom the taxpayer was not dealing at arm's length and who is not a person in respect of whom section 250.1 of the TA may apply for the person's taxation year that includes the time of the acquisition;
- (d) a security described in paragraph (c) above that was acquired by the taxpayer from a person who is not a person in respect of whom section 250.1 of the TA may apply for the person's taxation year that includes the time of acquisition, in circumstances in which section 518 (election upon the transfer of property to a corporation) or 529 (election upon the transfer of partnership property to a corporation) of the TA applied;
- (e) a share acquired by the taxpayer in the cases described in section 419 (shares deemed to be part of inventory) of the TA; or
- (f) a security described in paragraph (c) above that was acquired by the taxpayer as proceeds of disposition for a security of the taxpayer to which any of paragraphs (a) to (c) and (e) above applied in respect of the taxpayer, or as a result of one or more transactions that can reasonably be considered exchanges or substitutions of a security of the taxpayer to which any of paragraphs (a) to (c) and (e) applied.

**14.** A call or put option is not considered a Canadian security within the meaning assigned by section 250.2 of the TA. As a result, transactions involving call or put options cannot qualify for the capital gains election referred to in the first paragraph of section 250.1 of the TA.

## **DISPOSITION OF CANADIAN SECURITIES – GENERAL RULE**

**15.** In cases where the election referred to in the first paragraph of section 250.1 of the TA has not been made or could not be made, the general rules developed by the courts are applicable in determining whether the disposition of a security results in business income or a business loss, or a capital gain or loss (see also the current version of interpretation bulletin IMP. 232-1).

**16.** The gain or loss resulting from the disposition of securities is considered business income or a business loss where the taxpayer's whole course of conduct indicates that

- (a) the taxpayer, in security transactions, is purchasing and reselling securities in a way capable of realizing gains and with that object in view; and
- (b) the transactions are of the same kind and carried out in the same way as those of a trader or dealer in securities.

**17.** In determining whether the taxpayer's whole course of conduct indicates the carrying on of a business, the following factors are among those that may be considered:

- (a) frequency of transactions: a history of extensive purchasing and reselling of securities or of a quick turnover of properties;
- (b) length of time securities are held: securities are usually held only for a short period of time;
- (c) knowledge of securities markets: the taxpayer has some knowledge of or experience in securities markets;
- (d) taxpayer's field of activities: security transactions form a part of the taxpayer's ordinary activities;
- (e) time spent studying securities markets and investigating potential purchases: a substantial part of the taxpayer's time is spent on these activities;
- (f) financing: security purchases are financed primarily on margin or by some other form of debt;
- (g) advertising: the taxpayer's willingness to purchase securities has been advertised or otherwise made known by the taxpayer;
- (h) in the case of shares, their nature: usually speculative or non-dividend shares.

**18.** None of those factors by itself is sufficient to conclude that a taxpayer is carrying on a business and that the disposition of securities is part of the taxpayer's ordinary activities. However, a combination of some of those factors may be sufficient to characterize the activities of a taxpayer as a business.

**19.** Further, section 1 of the TA defines the term "business" to include an adventure or concern in the nature of trade, and the courts have held that the purchasing of securities by a taxpayer with the main intention of reselling them at a gain may constitute an adventure or concern in the nature of trade.

## **GAINS TREATED AS INCOME**

**20.** Even though a taxpayer may be classed as an "investor" or has made the election under the ITA referred to in the first paragraph of section 250.1 of the TA (with the result that gains or losses on the disposition of debt obligations are usually considered capital gains or losses), the following provisions of the TA require that the amount of any gain realized by the taxpayer be reported as income:

- (a) Where a debt obligation does not provide for the payment of interest, or where the rate of interest on the debt obligation is substantially below the market rate at the date of issue, any discount realized on the repayment of all or part of such a debt obligation may be regarded as interest and must be included as such in computing income, pursuant to paragraph c of section 87 of the TA.

- (b) On the disposition of a debt obligation, any amount received by the transferor that may reasonably be regarded as a payment of accrued interest must be included in computing the taxpayer's income, pursuant to section 167 of the TA.
- (c) A portion of any payment received on a debt obligation taken as consideration for property previously sold by the holder of the debt obligation may have to be included in computing income, pursuant to the rules relating to payments that are provided for in section 120 of the TA.
- (d) The value of a debt obligation taken in satisfaction of an income debt may have to be included in computing income. However, any subsequent gain or loss on the disposition of the debt obligation is to be treated in the normal manner, that is, the circumstances of each case will determine whether the gain or loss is a gain or loss of income, or a capital gain or loss.
- (e) Sections 122 to 125 of the TA provide special rules for an obligation that is a bond, debenture, bill, hypothecary claim, mortgage or other similar obligation issued by a person exempt from tax under sections 980 to 998 of the TA, a person not resident in Canada who is not carrying on business in Canada, or a government, municipality or public body performing a function of government. In certain cases, a discount on such an obligation is included in computing the income of the first holder of the obligation who is resident in Canada.
- (f) In accordance with section 88 of the TA, where a taxpayer receives a cash bonus in respect of a Québec or Canada Savings Bond, one-half of the cash bonus so received must be included as interest in respect of the Québec or Canada Savings Bond in computing the taxpayer's income.

**21.** Where the taxpayer who acquires a debt obligation is the person who issued the debt obligation, sections 179 and 263 of the TA apply.

## **THE ELECTION**

**22.** Since 20 December 2006, the rules provided for in the first paragraph of section 250.1 of the TA relate to the federal election made under subsection 39(4) of the ITA. Thus, a taxpayer may no longer make separate elections for purposes of the Québec and federal tax systems.

**23.** The second paragraph of section 250.1 of the TA provides that Chapter V.2 of Title II of Book I of the TA applies in relation to an election made under subsection 39(4) of the ITA or in relation to an election made under section 250.1 of the TA before 20 December 2006. That chapter sets forth general administrative and transitional rules (sections 21.4.4 to 21.4.15 of the TA).

**24.** In accordance with section 21.4.6 of the TA, if a taxpayer makes a valid election under subsection 39(4) of the ITA after 19 December 2006, the taxpayer must notify the Minister in writing of the election and attach to the notice a copy of every document sent to the Minister of National Revenue in connection with the election. The notice must be sent on or before the later of the following dates:

- the date of the 30th day following that on which the election is made; or
- the filing-due date of the taxpayer for the taxation year for which the election was sent to the Minister of National Revenue.

### **Election made before 20 December 2006 under the TA**

**25.** Before 20 December 2006, a taxpayer was able to make an election for Québec purposes, separate from the election made for federal purposes, in the tax return filed by the taxpayer for the year by using the prescribed form (TP-250.1-V).

**26.** Section 21.4.9 of the TA confirms the validity of such an election made before 20 December 2006 under section 250.1 of the TA. Section 250.1 of the TA, as it read before that date, applies in respect of the election unless, after 19 December 2006, the taxpayer makes the corresponding election for purposes of federal income tax (a valid election under subsection 39(4) of the ITA). In that case, in respect of the election made for Québec purposes, section 250.1 of the TA applies as it read on 20 December 2006, and not as it read before that date.

### **Election not made before 20 December 2006 under the TA**

**27.** Section 21.4.10 of the TA provides that, if an election was made under the ITA before 20 December 2006 and no corresponding election was made for Québec purposes, the provision respecting the election made for Québec purposes may nevertheless be applied in certain situations, according to the new rules.

**28.** Therefore, if a taxpayer made the election for federal purposes under subsection 39(4) of the ITA before 20 December 2006 and did not, before that date, make the corresponding election for Québec purposes (section 250.1 of the TA, as it read before 20 December 2006), the taxpayer may, with the consent of the Minister, apply for Québec purposes the valid election made for federal purposes, as if the election were a valid election made after 19 December 2006 (section 250.1 of the TA, as it read on 20 December 2006).