

2023 Tax FAQ

What to Expect During Tax Season

It is important to be prepared and plan for effective tax management. Each year ETF investors can expect to receive tax forms from their respective brokerages. As an investor, your primary focus should be on the total return of your portfolio and the tax efficiency of your return depending on your type of account, taxable or non-taxable.

As 2023 was a particular tough year for both Fixed Income and Equity investors, investors could potentially benefit from tax loss harvesting.

What is tax-loss harvesting?

The act of selling securities with accrued capital losses to offset gains made in other securities that were sold at a profit. To avoid a superficial loss, the proceeds from the sale of these securities can then be reinvested in different securities with similar exposures to the securities that were sold, such as a BMO ETF.

If capital gains are not available in the current year, the realized losses may be carried back up to three years to recover tax paid on net gains realized in those years or carried forward to reduce capital gains in upcoming years.

In addition to common shares, tax-loss harvesting can also be applied in respect of other financial instruments that are in non-registered accounts such as Bonds, Preferred Shares, ETFs and Mutual Funds.

As ETF providers do not have insight to unit holders, investors will receive T3s from their respective brokerages. The ETF provider posts the factors to CDS generally around mid-February. The dealer will then prepare the tax slips for clients and the cost adjustment thereafter.



What Are The Types Of ETF Distributions?

Canadian Dividends: Dividend distributions occur when an ETF invests in Canadian equity securities that pay dividends.

Tax Treatment: Canadian residents qualify for a dividend tax credit, if the ETF invests in Canadian securities that pays dividends.

Interest and Other Income: Fixed income ETFs earn interest on their investments in bonds and other debt obligations.

Tax Treatment: When an ETF pays out distributions as interest and other income, distributions are treated as ordinary income.

Capital Gains: An ETF may incur capital gains if an underlying security in the ETFs portfolio is sold for more than its purchase price.

Tax Treatment: Only 50% of capital gains are subject to tax in Canada and must be included in the investor's taxable income.

Foreign Income and Foreign Tax Paid: When an ETF earns dividends or interest on foreign investments the ETF may have to pay foreign withholding tax.

Tax Treatment: When the ETF distributes this foreign income, a Canadian investor may be able to claim a foreign tax credit (in a taxable account) in respect of the foreign tax paid by the ETF.

Return of Capital: An ETF may distribute a portion of your initial investment.

Tax Treatment: An ETF may distribute return of capital which is non taxable to investors. However, such a distribution will decrease the ACB of the investor's units. When the investor sells the ETF units, the lower ACB will increase the capital gain (or decrease the capital loss) that would otherwise be realized on the sale.

How are ETFs Taxed?

As an ETF investor, there are two main tax considerations to understand, the treatment of distributions paid by the ETF and the treatment of the gain or loss realized on selling the ETF. Depending on what type of account, registered or non-registered, the ETF is held in will also impact the tax treatment. Distributions flow through to the unitholder, based on the ETF's underlying portfolio.

More About BMO ETF Distributions

What are ETF Distributions?

Investors who received distributions throughout the calendar year will receive information on the tax treatment of the distributions by the end of February of the following calendar year.

Are tax slips issued for ETFs held in my Tax-Free Savings Account or RRSP?

No. If investors hold ETFs within a tax sheltered account such as RRSP, RRIF, RDSP, and TFSA, they will not be taxed on distributions and therefore will not receive a T3 tax form. If the ETF is held within a taxable account and has a taxable distribution, the investor can expect to receive a T3 tax form.

How are ETF Distributions Paid?

BMO ETFs pay distributions in cash on either a monthly, quarterly, or annual basis. Generally, the greater the income generated in the fund, the higher the distribution frequency. If the ETF has any capital gains, they are typically distributed annually in December and investors receive them as reinvested distributions. BMO Covered Call ETFs also pay out capital gains on the option premiums on a monthly basis.

Is there any way of finding out in advance how much interest, dividends, capital gains or ROC will be paid by an ETF for a specific tax year?

Final distribution amounts per unit are not made until the end of a tax year so breakdowns will not be provided until the beginning of the next calendar year.

However estimated amounts for year-end reinvested capital gains and cash distributions* will be announced in November and will be posted to www.bmogam.com/ca-en/products/exchange-traded-funds/etf-centre

What triggers a Capital Gain?

An ETF could incur a capital gain if one of the following events occur:

Performance: If the ETF experiences positive returns since purchase and the underlying investment is sold, the ETF could realize a capital gain.

Corporate Action: When a merger or acquisition occurs on one of the underlying holdings, the ETF may realize a capital gain.

Portfolio Rebalancing: When this occurs, the ETF will trade the underlying securities, which could result in a capital gain.

More About Return of Capital (ROC)

Any distribution that is paid out in excess of taxable income is classified as ROC. For cash income distributions paid throughout the year, BMO ETFs generally distributes based on the underlying portfolio yield less expenses. This benefits investors by providing greater certainty on the payout. As the ETF grows, the income earned is allocated across unitholders.

The important consideration for ROC, is whether it impacts the sustainability of the distribution. We define good ROC as sustainable, where the invested capital is not depleted over time. We define bad ROC as dipping into the invested capital to support the distribution, which leaves less investment for future years.

* Estimates provided can be used for tax planning purposes and not for filing taxes as actual year-end distributions can be different from estimates provided.

Benefits of ROC:

Tax Efficiency: Unlike other forms of distributions such as interest, dividends and capital gains, distributions classified as ROC are not taxable in the year received by the unit holder. As a result Canadian government pensions such as Old Age Security amounts will not be affected by income that is classified as ROC.

Cash Flow: Funds that distribute ROC can be ideal for investors seeking regular cash flow from their investments. ROC can be used to help portfolio managers distribute regular distribution amounts, which can be important for retirees who require the consistent income.

T Series ETFs

T Series ETFs are designed to provide a higher, predictable and potentially more tax-efficient cash flow. Similar to a T Series Mutual Fund, the T Series ETF will pay a fixed annual distribution rate, monthly based on end of year NAV and will pay out Return of Capital (ROC) above the portfolio's yield less expenses.

Reinvested 'Phantom' Distributions

On a cash distribution of ROC, the ACB is reduced by the amount of ROC, since this is a return of the investor's money. Note that investors do not adjust their ACB from cash distributions of realized capital gains throughout the year since the NAV is decreased by those distributions. On a reinvested distribution, the ACB is increased, since the investor is paying tax on the distribution.

If I reinvested the distributions from ETFs that are in a non-registered account, are they taxable?

Yes. Distributions received in your non-registered investment account are taxable, whether you receive them in cash or reinvest them in additional units of the ETF. All distributions, whether reinvested or paid out to you, are reported on your tax slips, which include a breakdown of types of income paid. See below for example of Income T3 Slip you will receive from your broker.

Accumulating Units

Accumulating units offer an effective solution to mitigate price declines by reinvesting coupons and consolidating the units.

Accumulating units will distribute a quarterly reinvested and consolidated distribution which will be added back to the NAV. Investors of Accumulating units will still receive a tax slip at year end, similar to distributing ETFs.

Inflation Protected Bonds ETFs - Special Income

In general, the outstanding principal of the bond rises with inflation for inflation-linked bonds. The principal adjustment and the interest on these bonds are taxed in the year they are accrued. This income may be distributed via reinvestment and consolidation or as "phantom income".

Covered Call ETFs

BMO ETFs treat the premiums earned from writing call options on portfolio securities as capital gains. While the premiums earned are paid out as part of the monthly cash distributions, the premiums are combined with the gains and losses from selling underlying holdings which may result in higher ROC on the T3 tax form. Note that "in-the-money options" do not decrease the value of the ETF, as the increase in value of the sold option is offset by the increase in value of the underlying portfolio holding at the same time. This means that we consider this good ROC, as the invested capital is not depleted.

For more information on BMO ETFs covered call lineup see our white paper [BMO Covered Call ETFs Methodology](#).

Currency Hedging

On our ETFs, currency hedging is treated as capital gains. We use one month forward contracts, where the gains and losses are recognized as the contract expires in the year. A proxy for capital gains from currency is the movement in the exchange rate over the year, subject to fund growth. These capital gains co-mingle with the gains and losses from the underlying portfolio.

BMO ETFs – Efficient Solutions for Foreign Investing

By investing in Canadian listed ETFs, investors can mitigate the amount of foreign taxes paid. BMO ETFs offers investors a comprehensive suite of solutions that provide tax effective foreign diversification

Withholding Taxes

Dividend income received from non-Canadian investments may be subject to withholding taxes. Foreign tax credits can be claimed for investments held in taxable, non-registered accounts. If international securities are held indirectly through a U.S. ETF, withholding taxes are not recoverable. If a Canadian resident holds a US listed ETF that holds international securities in a non-registered account, investors could be subject to paying two levels of withholding tax. BMO ETFs avoid this unrecoverable tax by holding their underlying securities directly, allowing for foreign taxes to be claimed.

BMO ETFs Solutions:
ZEА & ZDM & ZEQ
 Holds International Equities directly.

T1135

Investors who own certain foreign property with a total cost over CDN\$100,000 are required to file form T1135. Canadian ETFs are exempt from this reporting requirement, even if they hold foreign securities.

BMO ETFs Solutions:
ZBK & ZUE & ZSP
 Canadian ETFs are not subject to the T1135 reporting requirement and ordinarily are not subject to U.S. estate tax.

U.S. Estate Taxes

High net worth Canadians with worldwide assets exceeding US\$12.92M (for 2023, indexed to inflation) who have U.S. assets with a value that exceeds US\$60,000 may be required to pay U.S. estate tax upon death on the value of their U.S. assets. Canadian ETFs are generally not considered U.S. assets.

Example of a T3 tax slip

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Example of a RL-16 Slip for Quebec residents

RELEVÉ						RL-16 (20XX-10)	
16 Revenus de fiducie						Année	Codedu relevé
						N° du dernier relevé transmis	200000021
A- Gains en capital	B- Paiement unique de retraite	C1- Montant réel des dividendes déterminés	C2- Montant réel des dividendes ordinaires	D- Rente de retraite donnant droit à un crédit d'impôt	E- Revenus d'entreprise de source étrangère		
F- Revenus de placement de source étrangère	G- Autres revenus	H- Gains en capital donnant droit à une déduction	I- Montant imposable des dividendes déterminés et ordinaires	J- Crédit d'impôt pour dividendes	K- Impôt étranger sur des revenus d'entreprise		
L- Impôt étranger sur des revenus non tirés d'une entreprise	M- Rajustement du prix de base d'une participation	N- Dons attribués par un organisme religieux	Numéro d'assurance sociale du bénéficiaire	Autre numéro	Type	Indicateur	
Renseignements complémentaires						Numéro d'identification	
						Nom de la fiducie	
						Nom et adresse du fiduciaire ou du liquidateur de succession	



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Commissions, management fees and expenses all may be associated with investments in exchange traded funds. Please read the ETF Facts or prospectus of the BMO ETFs before investing. Exchange traded funds are not guaranteed, their values change frequently and past performance may not be repeated.

For a summary of the risks of an investment in the BMO ETFs, please see the specific risks set out in the BMO ETF's prospectus. BMO ETFs trade like stocks, fluctuate in market value and may trade at a discount to their net asset value, which may increase the risk of loss. Distributions are not guaranteed and are subject to change and/or elimination.

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