Invesco

Tax & Estate

Death and taxes

Everyone knows that life has two certainties: death and taxes. Fewer know that the two often coincide.

Canada has no official death, estate or inheritance taxes. However, without proper planning, an estate may be faced with large and unexpected tax liabilities upon death. This publication describes how registered or non-registered (open) investments in mutual funds or exchange traded funds (ETFs) might be taxed on the death of an annuitant/investor.

Non-registered (open) accounts

Though special rules apply to registered retirement savings plans (RRSPs) and registered retirement income funds (RRIFs), a taxpayer is generally deemed to have disposed of all his or her capital property (including stocks, exchange-traded funds, bonds, mutual funds, real estate, farm property, etc.) immediately before death at fair market value (FMV). When the proceeds of disposition exceed the property's adjusted cost base (ACB), the result is a capital gain. One half (50%) of the capital gain is taxable to the deceased and must be reported in the deceased's final tax return, known as the terminal return. On that return, a capital gains deduction may be claimed against any capital gains arising from qualifying property, such as shares of a qualified small business corporation or qualified farm or fishing property.

Spouse or common-law partner as beneficiary
The most common exception to the deemed disposition rules occurs when the capital property is transferred to a deceased taxpayer's spouse or common-law partner, or testamentary spousal or common-law partner trust. A testamentary spousal or common-law partner trust is typically created through a taxpayer's Will. It must meet specific criteria, but generally entitles the spouse or common-law partner to receive all the income of the trust during his or her lifetime. When property is transferred to a spouse or common-law partner, or testamentary spousal or common- law partner trust, the transfer may be done without triggering any immediate capital gains and the associated tax liability.

ACB transfer to spouse or common-law partner not always called for
Sometimes it may not be beneficial to transfer all mutual fund investments to a spouse or common-law partner, or testamentary spousal or common-law partner trust, at the ACB. It may be preferable to have the deceased's legal representative (e.g., the estate executor) elect out of the ACB transfer to a spouse or common-law partner to trigger a certain amount of capital gains on the terminal return. This would be advantageous in situations where the deceased taxpayer has unused capital loss carryforwards that would otherwise expire on death. These amounts could be used to reduce the tax on the capital gain that would otherwise result from the deemed disposition of the mutual funds at death.

Scenario one

Tax deferral to spouse
Jack and Nancy are husband and wife. Jack holds a non-registered investment in a mutual fund with an original ACB of $150,000. At Jack's death, the FMV of his holdings grew to $250,000. That represents an accrued capital gain of $100,000.

Had Jack left his investment in the mutual fund to Nancy (perhaps by naming her as the beneficiary of this property in his Will), the investment could simply be transferred into Nancy's name. Nancy would be deemed to have acquired the property at the same ACB of $150,000, thereby deferring tax on the $100,000 accrued capital gain.

If Nancy wasn't the beneficiary of Jack's mutual fund investment, Jack would have been deemed to have disposed of his units for proceeds equal to the FMV of $250,000. That would have resulted in a capital gain of $100,000, with 50% of it taxable. Depending on Jack's marginal tax rate in the year of death, the estate may have been liable for taxes of up to $22,500.[1]

[1] The average of the highest marginal tax rates is approximately 50% for 2020. We used 45% for illustrative purposes.

RRSPs

For many Canadians, the largest tax liability their estate will face is the potential tax on RRSPs. The *Income Tax Act* (Canada) (ITA) states that, unless certain conditions are met, the deceased's terminal return must report as income the fair market value of his or her RRSP on the date of death. Tax will be payable at the deceased annuitant's marginal rate for the year of death unless this income inclusion can be avoided by using one of the strategies discussed below.

Spouse or common-law partner as beneficiary

When an RRSP account is set up, the annuitant may designate a beneficiary of the RRSP. The beneficiary designation can be made on the RRSP account or through a declaration in the deceased's Will. If a spouse or common-law partner is the named beneficiary, the value of the registered plan at death qualifies as a refund of premiums. This refund of premiums may not be taxed in the hands of the deceased annuitant; rather, it can be taxed to the surviving spouse or common- law partner, who could choose to transfer the amount directly to his or her RRSP, RRIF, specified pension plan (SPP), pooled registered pension plan (PRPP) or to an issuer to purchase an eligible annuity and claim a deduction equal to the amount of the refund of premiums. The spouse or common-law partner beneficiary does not require RRSP contribution room to complete the transfer of the refund of premiums. As such, a part of or the entire amount of refund of premiums would continue to remain tax-deferred until the amounts are withdrawn or upon death of the spouse beneficiary.

Child or grandchild as beneficiary

If the beneficiary of the RRSP is a child or grandchild, the proceeds of the RRSP still qualify as a refund of premiums so long as the child or grandchild is financially dependent on the deceased annuitant. In this case, the refund of premiums could be taxed in the hands of the child or grandchild and not the deceased annuitant. If the child or grandchild is a minor, the proceeds of the RRSP could be used to purchase an annuity that must end by the time the child reaches the age of 18. This alternative has the effect of spreading the tax on RRSP proceeds over several years, allowing the child or grandchild to take advantage of personal tax credits, as well as graduated marginal tax rates, each year until he or she reaches the age of 18.

There is one situation in which RRSP money can be transferred to a child's or grandchild's own RRSP or RRIF. If the financially dependent child or grandchild was dependent on the deceased annuitant by reason of physical or mental infirmity, then the amount that qualifies as a refund of premiums may be rolled over into the child's or grandchild's RRSP, RRIF, SPP, PRPP or to an issuer to purchase an eligible annuity. In all other situations, if the children were not financially dependent on the deceased, the entire value of the RRSP would be taxable in the deceased annuitant's terminal return.

Joint and several liability

Generally, the tax liability arising out of the deceased annuitant's terminal tax return is the responsibility of the deceased annuitant's estate. Where an RRSP annuitant dies, the ITA provides that the recipient (i.e., a beneficiary) of an amount out of or under an RRSP is jointly and severally liable with the deceased annuitant for a portion of the deceased's additional tax payable that arose because the RRSP amount was included in the deceased's income. This joint and several liability is equal to the proportion of such additional tax attached to the RRSP payment received by the beneficiary. An annuitant of an RRSP may want to ensure that the estate has sufficient liquidity in the estate to pay any resulting income tax associated with the deemed disposition (and income inclusion) of an RRSP at his or her death in order to protect a non-spouse beneficiary's entitlement to the entire amount of the RRSP funds. Similar provisions apply to amounts received through a distribution of RRIF proceeds upon the death of a RRIF annuitant.

Estate as beneficiary

Sometimes an RRSP annuitant will name his or her estate as the beneficiary of the plan. In this case, where an amount is paid from an RRSP to the estate for the benefit of either the spouse or common-law partner, or a financially-dependent child or grandchild (assuming they were beneficiaries under the Will), the legal representative of the estate, along with the beneficiary, can file a joint election with the Canada Revenue Agency (CRA) to treat the amount as though it was transferred directly to the spouse or common-law partner, or child from the RRSP. In this case, the same refund of premiums treatment can be obtained.

Note: Invesco currently cannot accept beneficiary designations on RRSPs, RRIFs and TFSAs when the annuitant is a Quebec resident.

Scenario two

No tax deferral to spouse

Continuing from scenario one, assume Jack had $50,000 worth of capital loss carryforwards. Nancy is the beneficiary. If no election is made to trigger a capital gain, the units are transferred to Nancy's name at an ACB of $150,000. On Nancy's death, assuming the FMV of the mutual fund investment remains constant at $250,000, Nancy's estate would realize the capital gain of $100,000 and would be liable for taxes of up to $22,500.

On the other hand, if the executor of Jack's estate had elected to report $50,000 of capital gains on Jack's terminal return, this $50,000 could be reduced to zero by applying the capital loss of $50,000 against the elected gain. Because Nancy is the beneficiary of the mutual fund investment, she would acquire the units with a total ACB of $200,000. On Nancy's death, the resulting capital gain would be only $50,000, attracting taxes of up to $11,250. If Jack's executor elected to trigger the appropriate amount of capital gains, the savings to the final estates of both Jack and Nancy would be up to $11,250.

Scenario three

Estate as beneficiary

Jack set up an RRSP in 1982 naming his estate as the beneficiary. When Jack recently passed away, the RRSP account had grown to a value of $300,000. Because Jack's estate was named as the beneficiary, the entire value of the RRSP would be included as income in Jack's terminal return. Taxes of $135,000 could be owing, assuming a 45% marginal tax rate.

Scenario four

Tax deferral for registered plans

Instead of naming his estate as beneficiary of his RRSP, Jack named his wife Nancy as the beneficiary. The $300,000 value of the RRSP would then be taxable as a refund of premiums on her tax return. She could choose to transfer this amount to an RRSP in her name and receive an RRSP contribution receipt for $300,000, which would be used to offset the income inclusion of the refund of premiums. The net effect of this is to ensure that tax continues to be deferred after Jack's death.

Scenario five

No tax deferral

Nancy has received Jack's RRSP as a refund of premiums and transferred the $300,000 to an RRSP account in her own name. As outlined in scenario four, this defers the tax otherwise due upon Jack's death. Nancy names her 35-year-old daughter Judy as the beneficiary of her RRSP. Judy has a great job and does not have any mental or physical infirmities. At the time of Nancy's death, the FMV of the investments grew to $310,000. The entire amount is taxable on Nancy's terminal return; no further relief, rollovers or deferred tax liability is possible.

Scenario six

Tax deferral election

Nancy is the beneficiary of the entire estate, as specified in Jack's Will. Jack has named his estate as the beneficiary of his RRSP. Upon Jack's death, Nancy and the executor of Jack's estate could file a joint election to deem the $300,000 as a refund of premiums. When transferring this amount to her RRSP, Nancy will receive an offsetting contribution receipt as though she received the money directly as a named beneficiary of the RRSP.

RRIFs

The rules concerning the taxation of RRIF accounts on death essentially mirror those for RRSPs, with some minor variations. Generally, an annuitant of a RRIF must include the FMV of his or her RRIF as income on the date of death. This amount must be reported on the terminal return, and tax will be payable at the deceased annuitant's marginal rate for the year of death.

Spouse or common-law partner as successor annuitant
RRIFs and RRSPs share the potential for tax deferral on the income inclusion at death in the terminal return. When a RRIF is established, the annuitant may designate a successor annuitant and/or a beneficiary of the RRIF. A successor annuitant is the surviving spouse or common-law partner of the original annuitant who, if designated by the original annuitant, continues to receive RRIF payments after the death of the original annuitant. With a successor annuitant designation, the deceased RRIF annuitant would be responsible for reporting RRIF withdrawals received while alive. The successor RRIF annuitant would be responsible for reporting any new RRIF withdrawals received after the date of death. The regular income inclusion rule discussed previously would not apply, with a successor annuitant designation.

Spouse or common-law partner as beneficiary
Alternatively, if a spouse or common-law partner is the named beneficiary of the RRIF, the value of the RRIF at death qualifies as a designated benefit. This designated benefit is not taxable to the deceased annuitant; rather, it is taxable to the surviving spouse or common-law partner, who can transfer this amount directly to his or her RRSP, RRIF, SPP, PRPP or to an issuer to purchase an eligible annuity and claim a deduction equal to the amount of the designated benefit. As with a transfer of a refund of premiums with an RRSP, a transfer of a designated benefit by a spouse or common-law partner as beneficiary does not require RRSP contribution room. By doing so, the value of the RRIF is simply transferred into the surviving spouse's or common-law partner's RRSP, RRIF, SPP, PRPP or to an issuer to purchase an eligible annuity and continue to remain tax-deferred (less any required minimum annual withdrawals).

Child or grandchild as beneficiary
If the beneficiary of the RRIF is a financially-dependent child or grandchild, the proceeds of the RRIF still qualify as a designated benefit. This designated benefit is taxable in the hands of the child, not the deceased annuitant. If the child or grandchild is a minor, the proceeds of the RRIF could then be used to purchase an annuity, which must end by the time that child reaches the age of 18.

If the financially-dependent child or grandchild is dependent on the deceased annuitant by reason of physical or mental infirmity, the amount that qualifies as a designated benefit may be rolled over into the child's or grandchild's RRSP, RRIF, SPP, PRPP, or to an issuer to purchase an eligible annuity. If the children are not financially dependent, the entire value of the RRIF will be taxable in the deceased annuitant's terminal return.

Estate as beneficiary
Finally, as with RRSPs, if a RRIF annuitant simply names his or her estate as the beneficiary of the plan, the amount paid from the RRIF to the estate for the benefit of either the spouse or common-law partner, or the financially-dependent child or grandchild can be considered to have been transferred directly to them. The same treatment outlined in scenario six would apply. As with RRSPs, a joint election between the legal representative of the estate and the beneficiary must be filed with the CRA.

Scenario seven

Tax deferrals for RRIFs
John, age 67, and Ann, age 72, are husband and wife. Ann has a RRIF from which she is currently receiving payments each year. On February 5, after Ann withdrew the minimum amount required from the RRIF for the year, she died.

If Ann had named John as the successor annuitant under the RRIF, the RRIF payments would simply continue as before, except they would be paid to John, not Ann. On the other hand, if Ann designated John as the beneficiary of her RRIF, the entire FMV at February 5 may be taxable to John as a designated benefit.

If John didn't need the income, he might choose to transfer part of all of the amount into an RRSP instead of a RRIF, maximizing the amount that can remain tax deferred. John is able to do this because he is able to hold an RRSP up to December 31 of the year in which he turns 71, the time at which the RRSP must be collapsed. He would obtain a contribution receipt for the amount of the transfer. This amount would offset the income inclusion of the designated benefit. The result would be a tax-deferred rollover from Ann's RRIF to John's RRSP.

Rollover to a registered disability savings plan (RDSP)

Since July 1, 2011, qualified beneficiaries of an RRSP or a RRIF who are a financially-dependent child or grandchild that also have a physical or mental infirmity can roll over the proceeds to an RDSP tax-free. These rollovers cannot exceed the maximum RDSP contribution room of $200,000 and will also reduce the room by the amount transferred. Government grants will not be paid into the RDSP on funds rolled over in these scenarios. For more information, please refer to our *Tax & Estate InfoPage* titled *Registered Disability Savings Plans (RDSPs)*.

RRSP/RRIF losses after death

As mentioned earlier, the FMV of RRSP or RRIF investments is generally included in the deceased annuitant's income in the year of death.

A subsequent increase in investment value is generally included in the income of the RRSP or RRIF beneficiaries upon distribution. Until the 2009 Federal Budget, there was no income tax provision to recognize a decrease in the value of RRSP or RRIF investments occurring after death and before distribution to beneficiaries.

Presently, for final distribution from a deceased annuitant's RRSP or RRIF occurring after 2008, post-death decreases in value may be carried back and deducted against income on the deceased's terminal tax return. The amount will generally be calculated as the difference between the year-of-death RRSP/RRIF income inclusion and the total of all amounts paid out of the RRSP or RRIF after the death of the annuitant.

Tax-free savings accounts (TFSAs)

Upon death of a TFSA accountholder, an amount up to the FMV of the plan as of the date of death is received tax-free to the beneficiary of the TFSA or to the deceased's estate if no beneficiary is named. Any payment made to a beneficiary of the TFSA that relates to an increase in value from the date of death and that is paid out by the end of the year following the year of death is generally taxable to the beneficiary. These amounts will be reported on a T4A tax slip and identified as "other income." The amount is to be included as income to the beneficiary for the year that it is paid. A beneficiary designation may be made directly on the TFSA or through instruction of the deceased TFSA accountholder's Will.

Exempt contribution(s)

The spouse or common-law partner of a deceased accountholder is considered a "survivor." If a survivor directly or indirectly acquires the rights to the TFSA plan as the beneficiary, it is possible to transfer the proceeds over to his or her own TFSA and designate this contribution as an "exempt contribution." An exempt contribution will not affect the survivor's own TFSA contribution room, nor does the survivor require TFSA contribution room to make the contribution. It is important to note that only a spouse or common-law partner can be considered a survivor and make use of the exempt contribution; beneficiaries other than a survivor in receipt of a payment from the deceased accountholder's TFSA are not able to contribute and designate any amount as an exempt contribution.

In order to ensure the contribution by the survivor is considered an exempt contribution, the contribution should be made within the "rollover period." This period continues up to December 31 of the calendar year following the year of death (or any later time that is approved and acceptable by the CRA). Also, the survivor must file the prescribed CRA form RC240 entitled Designation of an *Exempt Contribution Tax-Free Savings Account* (TFSA) within 30 days after the day the contribution is made to designate the contribution as an exempt contribution.

Note that the exempt contribution amount is generally limited to the FMV at the date of death and the payment must be contributed to the survivor's respective TFSA during the rollover period.

Successor TFSA accountholder

The TFSA accountholder may designate his or her spouse or common-law partner as a successor TFSA accountholder directly on the TFSA. Upon death of the TFSA accountholder, the proceeds of the TFSA plan simply continue to remain in the tax-sheltered vehicle and the successor TFSA accountholder becomes the new TFSA accountholder. It is important to note that, where the deceased TFSA accountholder was in an excess TFSA contribution position prior to his or her death, the successor TFSA accountholder is deemed to have made a TFSA contribution for the amount of this excess at the beginning of the month following his or her death.

Scenario eight

Rollovers for TFSAs

Nancy has received Jack's RRSP as a refund of premiums. Jack also has a TFSA, and named his wife Nancy as 100% beneficiary of the plan. When Jack passes away, Nancy has until the end of the following year (the rollover period) to facilitate an exempt contribution into her own TFSA. Jack's TFSA was valued at $100,000 at the time of his death. When Nancy completes the transfer of Jack's TFSA funds into her own TFSA, she has 30 days from the date of the transfer to complete and file the CRA form RC240, to designate the amount as an exempt contribution with the CRA. When Nancy completed the transfer, the TFSA grew to $101,000. The income generated from the date of death ($1,000) is included as income to Nancy and is taxed in her hands. She will also need the necessary TFSA contribution room to contribute this amount into her own TFSA as the exempt contribution will generally be limited to the date-of-death value, which in this case is $100,000.

Scenario nine

Successor accountholder on TFSA

Where Jack named Nancy as a successor TFSA accountholder either directly on the TFSA or through his Will, Nancy can essentially take over the plan immediately after Jack's death, and the plan can continue with Nancy as the new TFSA accountholder. Any income generated after the date of death would not be taxable to Nancy, as it is in scenario eight, since she will step in as the new TFSA accountholder immediately after Jack's death, and these amounts continue to be tax-sheltered within the TFSA plan itself. Nancy does not have to designate this as an exempt contribution on form RC240, as she will simply take over the plan as of the date of death. This option is similar to the successor annuitant designation available with RRIFs.

Registered education savings plans (RESPs)

Death of an RESP subscriber

Upon the death of an RESP subscriber, if an RESP is held jointly, the surviving joint owner would inherit the deceased joint subscriber's rights in the RESP as per the rights of the survivorship provision (except in Quebec) and may continue as subscriber of the RESP. Alternatively, if there is no joint subscriber or the subscriber was a resident of Quebec, the transition from the original subscriber to a replacement subscriber would depend on the provisions of the deceased subscriber's Will. If there is no joint subscriber and the deceased subscriber has not named a successor subscriber through his or her Will, it may be possible for the estate trustee (or legal representative of the estate) to approach the courts to name a new subscriber to take over the RESP. In cases where there is sufficient flexibility accorded to the estate trustee through the Will, it may also be possible for the estate trustee to acquire the rights under the RESP and manage the RESP on behalf of the beneficiary.

If no successor subscriber can be named, an RESP would be terminated as a result of the subscriber's death. All contributions would normally be refunded to the estate of the subscriber, and all Canada Education Savings Grants and any other grants or bonds remaining in the account would be refunded to the government. If certain conditions are met, an Accumulated Income Payment (AIP), which is subject to income tax and a penalty tax, may be payable to the estate. All amounts payable to the estate would normally be distributed along with other estate assets to the beneficiaries of the estate according to the deceased's Will. In these instances, the RESP assets would form part of the deceased subscriber's estate and may subsequently be subject to probate.

Death of an RESP beneficiary

In the event that an RESP beneficiary dies, it may be possible to name a sibling as a replacement beneficiary, subject to certain conditions. If the RESP is a family plan, the surviving beneficiaries would be able to use any growth and government grants (excluding the Canada Learning Bond) that were received by the deceased. Where no replacement beneficiary exists or there is no other beneficiary who qualifies to use the deceased's growth and grant, the plan can be terminated, with the grants being returned to the government and contributions refunded to the subscriber. If certain conditions are met, an AIP (which is subject to income tax and a penalty tax) can be paid to the subscriber. Alternatively, provided sufficient RRSP contribution room exists, it may be possible for the original subscriber or his or her spouse or common-law partner to continue the tax-deferred growth of an AIP by transferring it directly into his or her own RRSP. Under this option, provided certain conditions are met, the income and penalty taxes normally associated with an AIP would be waived.

Scenario ten

Successor subscriber for RESPs

Joseph has an RESP for his 15-year-old granddaughter Ella. The total value of the plan equals $25,000 ($20,000 in contributions, $4,000 in government grants and $1,000 in investment returns). Joseph passes away prior to Ella beginning post-secondary studies. Upon review of Joseph's Will, it is determined that he left specific instructions for Ella's father Jack to be the successor subscriber of the RESP in the event of Joseph's death. If there were no instructions in the Will and there was nobody willing or able to continue the RESP as a successor subscriber, the plan may have to be collapsed and the RESP assets, after the grants are returned to the government, would be distributed to the beneficiaries of the estate.

In either case, the assets would potentially be subject to probate. However, the naming of a successor subscriber could save the estate an additional $650 in taxes on the plan growth (AIP withdrawal of $1,000 less penalty and income tax).[2] More importantly, the naming of a successor subscriber ensures that Ella still has educational assistance with her future school expenses when she needs them.

[2] The AIP penalty tax is 20% and assumes a top marginal tax rate of 45%.

Scenario eleven

Transfer of AIP to RRSP

If Ella were to pass away and there were no possible replacement beneficiaries, the RESP would need to be collapsed and all grants would be returned to the government. However, provided he has the necessary unused deduction room, Joseph may be able to transfer (subject to conditions) the AIP amount into his spouse's or common-law partner's RRSP without any withholding tax or penalty tax. Note that the AIP rollover to an RRSP or RRIF applies only to the original subscriber of the RESP or the spouse or common-law partner of the original subscriber. If a non-spouse or common-law partner became the subscriber of an RESP due to the death of the original subscriber, the regular withholding and penalty taxes would apply to the AIP.

RDSPs

Death of an RDSP holder

In general, the holder of an RDSP can be the parent(s) of the beneficiary, a guardian, tutor, public department, or any other qualified individual or body. Additionally, if the beneficiary is over 18 and legally able to enter into a contract, the beneficiary can also be the planholder.

In the event that an RDSP holder who is not the beneficiary dies, the deceased must be removed from the plan as a holder. Where this occurs, the RDSP rules state that a new holder must be named in order for the plan to carry on. The successor holder of the RDSP could be the beneficiary (provided he or she is the age of majority and contractually competent), a surviving parent or qualified relative, the beneficiary's guardian or a public trustee, to name a few. If a qualified person has not been named in the deceased planholder's Will, the assignment of a successor RDSP holder may have to be determined by the applicable courts or the office of the public guardian and trustee.

Scenario twelve

RDSP at Death

Jake is a 35-year-old RDSP beneficiary and the holder of his own plan based on his age and the fact that he is contractually competent. For the past 15 years, annual contributions of $1,500 have been made into the RDSP, resulting in a balance of $80,000 ($22,500 contributions + $52,500 in Canadian Disability Support Grants + $5,000 in investment income). If Jake were to die, his RDSP must be collapsed and all funds remaining after the required assistance holdback amount would be paid into his estate to be distributed by the provisions of his Will or the laws of intestacy (if there was no Will) in his province. In this scenario, the assistance holdback amount repaid to the government would be $35,000 ($3,500 x 10 years), leaving $45,000 paid to Jake's estate, of which $22,500 ($45,000 - $22,500 in contributions) is taxable on Jake's terminal return. Additionally, the entire $45,000 may be subject to probate.

Death of an RDSP beneficiary

As discussed above, an RDSP can be managed either by a qualified holder or by the beneficiary himself/herself. In either case, where the beneficiary of an RDSP has died, the RDSP must be closed, all amounts remaining in the plan must be paid out to the beneficiary's estate and the plan must be terminated by December 31 following the calendar year in which the beneficiary dies. Any grant or bonds deposited in the plan in the 10 years prior to the beneficiary's death must be returned to the government (this is known as the "assistance holdback amount"). However, any accumulated growth on these amounts does not need to be repaid. All other grants, bonds and accumulated growth on the plan will be distributed and taxable to the beneficiary's estate. As with RESPs, original contributions will be distributed to the beneficiary's estate tax-free. In these instances, the RDSP assets would also be subject to probate.

Terminal return versus estate return

It is important to note that the income inclusion and subsequent tax implications (absent a spousal tax deferral option) due to death is reported on the terminal return. The terminal return (otherwise known as the final return), is the deceased final income tax return for the year of death. The terminal return records income generated by the deceased from January 1 of the year of death until the date of death. This is distinguishable from an estate return, which is the income tax return for all the income generated by the assets that fall into the estate of the deceased after death. Generally, an estate is a trust for tax purposes, and the trust can designate itself as a Graduated Rate Estate (GRE) up to the first 36 months following the individual's death. If the trust files annual T3 trust returns and designates itself as a GRE, it will be taxed at graduated tax rates instead of the top marginal tax rate during the GRE period. No other estate may designate itself as a GRE, and the Social Insurance Number of the deceased must be provided. For more information about the taxation of trusts and estate, please see our bulletin called, "Trusts – Tax features and strategic management".

Getting advice

Bear in mind that the situations outlined above are simple summaries of often complex tax scenarios. All cases should be dealt with on an individual basis, and professional legal and tax advice should always be obtained when dealing with estates.

For more information about this topic, contact your advisor, call us at 1.800.874.6275 or visit our website at invesco.ca.

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