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the Navigator

INVESTMENT, TAX AND LIFESTYLE PERSPECTIVES FROM RBC WEALTH MANAGEMENT SERVICES

Optional returns for a deceased individual

Optional tax returns could save the estate some money

Please contact us for more information about the topics discussed in this article.

You may be able to reduce or eliminate tax for the deceased by filing one or more optional returns in addition to the terminal return. Optional returns are returns on which you report some of the income that you would otherwise report on the final tax return.

This article outlines strategies, not all of which may apply to your particular circumstances. The information in this article is not intended to provide legal or tax advice. To ensure that your own circumstances have been properly considered and that action is taken based on the latest information available, you should obtain professional advice from a qualified tax and/or legal advisor before acting on any of the information in this article.

Types of optional returns

Optional returns may reduce or eliminate tax because you can claim certain tax credits more than once, split certain credits between returns, or claim them against specific kinds of income.

In addition to the final tax return of the deceased, there may be as many as three other separate types of returns for a deceased taxpayer that you can file:

1. A return for rights or things;
2. A return reporting business income (either as a sole proprietor or partner); and
3. A return for income from a Graduated Rate Estate (GRE).

Return for rights or things

“Rights or things” are income amounts that the deceased was entitled to receive before they died but that had not yet been paid. The main rights or things are:

- employment income (e.g. salaries, commissions, vacation pay) owing by the employer on the date of death for a pay period that ended before the date of death;
- uncashed matured bond coupons;
- bond interest earned up to a payment date before death, but not paid and not reported in previous years;
- unpaid dividends declared before the person died;
- Old Age Security, Employment Insurance (EI) and Canada Pension Plan benefits not yet received for a period ended before the date of death or for the month of death;
- work-in-progress if the deceased carried on a business as a sole proprietor or partner and had elected to exclude work-in-progress when calculating income; and
- retroactive payment of a disability annuity or EI benefit paid after the date of death, but to which the deceased was entitled prior to that date.

Some items that are not rights or things include:

- amounts that accumulate periodically, such as interest from a bank account;
- bond interest accumulated between the last interest payment date before the person died and the date of death; and
- Registered Retirement Savings Plan (RRSP) income.

If you elect to file a rights or things optional return, you must report all rights and things on that return except for rights and things transferred to beneficiaries. You cannot split rights or things between the final tax return and the return for rights or things. If you have transferred rights or things to a beneficiary before the filing deadline for the optional return, the beneficiary must report the income from the transferred rights or things on their return.

Return for a partner or proprietor

If the deceased carried on business as a partner or sole proprietor and the fiscal year of the business was not the calendar year, you can elect to report the business income earned between the end of the fiscal year of the business and the date of death in a separate optional return.

Return for income from a graduated rate estate (GRE)

If the deceased received income from a trust that is a GRE and the fiscal year end of the trust is not the calendar year end, you can elect to report the income received from the GRE that relates to the period between the taxation year of the trust and the date of death on a separate return.

You cannot split rights or things between the final tax return and the return for rights or things.

This situation can arise, for example, if the deceased was a beneficiary of his late spouse's estate which is still a GRE.

Generally, a GRE of an individual is the estate that arose on and as a consequence of the individual's death for the first 36 months after death. To be considered a GRE, the estate also needs to remain a testamentary trust and be designated for its first taxation year as the individual's GRE. A GRE is discussed in more detail in our article, "Testamentary Trusts."

Filing due dates

The filing dates for optional returns are the same as those for a final tax return, except for the rights or things return. The due date depends on the date of death. For deaths occurring January 1 to October 31, the filing due date is April 30 of the year following the year of death (or June 15 if the deceased was a self-employed individual). The filing due date is six months after the date of death for deaths occurring in November and December.

The filing due date for the rights and things return is the later of:

- 90 days after the Canada Revenue Agency (CRA) sends the notice of assessment or notice of reassessment for the final tax return; and
- one year after the date of death.

However, the due date for any balance of tax owing on all the optional returns, including the rights or things return, depends on the date of death. For deaths occurring January 1 to October 31, the balance of tax owing is due no later than April 30 of the year following the year of death. For deaths occurring in November and December the balance of tax owing is due no later than six months after the date of death.

Benefit of filing an optional return

There are two main benefits of filing an optional tax return in addition to a final tax return for a deceased individual:

1. Access to more than one use of the low graduated tax rates — Since each optional return is taxed like a separate person at graduated tax rates, the lowest tax rate may be used more than once (on the terminal tax return and on the optional return or returns) to minimize the tax liability at death.

2. Claiming certain personal tax credits more than once
— Some personal tax credits can be claimed in full on each return. On each optional return and on the final return, you can claim:

- the basic personal amount;
- the age amount;
- the spouse or common-law partner amount;
- the amount for an eligible dependant;
- the amount for infirm dependants age 18 or older;
- the family caregiver amount for children under 18 years of age and,
- the caregiver amount.

For example, if in the year of death, the deceased had employment income and dividends declared before the date of death, you may choose to file a rights and things return in addition to the final tax return. In this case, report the employment income on the terminal return and the dividends on the rights and things return. This allows the

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deceased to claim the basic personal amount on each of these returns. What this means is that the deceased pays no tax on income up to twice the basic personal amount. If there is any income above the basic personal amount, it is taxed at the graduated tax rates.

Conclusion

If the deceased has any income that may qualify for any of the optional returns then consider filing one or more of the optional returns to minimize the taxation on death. Consult with a qualified tax advisor to determine if filing optional returns would be beneficial in the circumstances.



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