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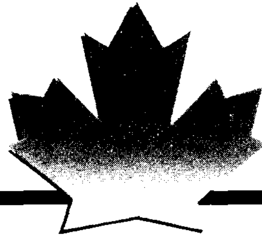
**Supplementary Guide**

# Deceased Persons Income Tax Guide

1990

Your Guide



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## WHAT'S NEW FOR 1990?

- **Proposed legislation.** This Guide refers to certain proposed changes to the *Income Tax Act* announced by the Minister of Finance on July 13, 1990. However, at the time this Guide was printed, these changes had not yet become law. For more details, contact your district taxation office.

- **Revised information slips.** All box indicators on information slips have been changed from letters to numbers. For example, Box (C) on the T4 slip is now Box 14. For 1990, you may receive the old or the new version of an information slip. We have shown both indicators where necessary.

This Guide uses plain language to explain the most common income tax situations. It does not replace the laws found in the *Income Tax Act*, the *Unemployment Insurance Act* and the *Canada Pension Plan* and their related regulations. For more information, please refer to these laws or contact your district taxation office.

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## INTRODUCTION

This Guide is for legal representatives (executors, trustees or administrators) of estates who file return(s) on behalf of deceased persons. It does not, however, include all the information necessary to complete the return(s). Therefore, please refer to the *1990 General Income Tax Guide*.

There is no specific income tax return for deceased taxpayers. You use the T1 General Income Tax Return. You may use the T1 Special Return if it contains all the lines necessary to report the income, deductions and credits of the deceased.

## FILING RETURNS

The legal representative is responsible for filing the required return(s) on behalf of the deceased person. Depending on the income sources of the deceased, and if certain elective provisions of the *Income Tax Act* are exercised, you may file as many as four separate income tax returns for the year of death.

If the income tax return for the year you are filing is not yet available, you may use a previous year T1 General Income Tax Return. Just change the year at the top right-hand corner of page 1.

### Ordinary return (150(1)(b))

You must file a return on behalf of the deceased for the year of death. This return should include all the income the individual received from January 1 of the year of death to the date of death. The required filing date for this return depends on the date of death.

- For persons who died between January 1 and October 31 of 1990, the required filing date for their 1990 return is April 30, 1991.
- For persons who died between November 1 and December 31 of 1990, their 1990 return is required to be filed within six months from the date of death.
- For person who died between January 1 and May 1 of 1991, their 1990 return is required to be filed within six months from the date of death.

The legal representative for the deceased is not required to remit income tax instalments that would otherwise become due after the death of the individual. However, if there is an amount owing on the return for the year of death, it should be paid when the return is due to be filed. If it is not paid in full, any amount outstanding will be subject to interest. Interest on arrears will begin to accrue immediately after the required filing date.

**1989 and prior year's return** — Legal representatives will no longer be granted the six month extension to file these returns on behalf of the deceased. If these returns were not filed by April 30 following the applicable taxation year, any amout outstanding will be subject to interest from May 1 of the year that the return should have been filed to the date that the amount is paid in full.

**Spouse trust (70(7))** — If a spouse trust exists from which testamentary debts must be paid, the deadline for filing the 1990 return for the deceased may be extended to 18 months after the date of death. However, the payment date for any taxes owing on this return is April 30 or six months after the date of death, whichever is later. Any amount outstanding after this date will be subject to interest. For more information on spouse trusts, see Chapter 5 in this Guide.

**Note**

If any ordinary return is filed late, the amount outstanding could also be subject to a penalty of 5% of the tax owed at the time the return should have been filed, plus 1% for each complete month the return is late, up to a maximum period of 12 months.

### Elective returns

**Note**

You must identify all elective returns by entering the number of the subsection or paragraph of the *Income Tax Act* at the top of page 1 of the return.

**Separate return for rights or things (70(2))**

As the legal representative for the deceased, you may elect to file a separate return for the value of "rights or things" at the time of death. This return is required to be filed within one year after the date of death, or 90 days after the mailing of any Notice of Assessment of tax for the year of death, whichever is later. For further details on rights or things, refer to Chapter 2 in this Guide.

If there is an amount owing on this return, it should be paid when the return is due to be filed. If the amount is not paid in full, the unpaid amount will be subject to interest. Interest will begin to accrue immediately after the required filing date. You may, however, elect to defer payment of a portion of the tax attributed to income from the value of rights and things. For more information, see the section called "Payment of tax" in Chapter 5 in this Guide.

**Separate return for income from partnerships or proprietorships (150(4))**

Special rules apply if the deceased was a member of a partnership or carried on a business, as a sole proprietor, that has a fiscal period that differs from the calendar year. If the taxpayer dies after the end of the fiscal

period of the partnership or business but before the end of the calender year in which the fiscal period ended, the business income from the end of the last fiscal period to the date of death (stub period) must be reported on the ordinary return in the year of death, unless you file a special election. This election allows you to report the income for this "stub period" on a separate return. This elective return must be filed with full payment of any tax owing at the same time as the ordinary return.

If you file this return late, and there is an amount outstanding, interest will be charged on this amount. Interest will begin to accrue immediately after the required filing date.

**Separate return for trust income (104(23)(d))**
A separate return may be filed if the deceased was an income beneficiary of a testamentary trust that has a fiscal period that differs from the calendar year. This return should include the income from the trust from the end of the last fiscal period of the trust to the date of death. You are required to file this return at the same time as the ordinary return.

If you file this return late, and there is an amount outstanding, interest will be charged on this amount. Interest will begin to accrue immediately after the required filing date.

# CHAPTER 1
# ORDINARY RETURN FOR THE YEAR OF DEATH

## "Step 1 — Identification" area of the return

If a personalized return is used, ensure that all the information on the label at the top of page one is correct. Check that

- "The Estate of the Late" is written before the name of the taxpayer,
- the address given is the address of the executor or administrator,
- the reference to the province or territory of residence on December 31 refers to the residence of the deceased at the date of death, and
- the date of death is entered on the appropriate line.

## Calculating total income

To complete the income area of the return, it is necessary to determine the income of the deceased from all sources. A copy of the immediately preceding year's income tax return may be of assistance.

In some instances, such as in the case of an early-filed 1991 return, it may be necessary to contact the people who made the payments to obtain the following information slips:

- T4 Statement of Remuneration Paid;
- T4A Statement of Pension, Retirement, Annuity and Other Income;
- T4A(P) Statement of Canada Pension Plan Benefits;
- T4A(OAS) Statement of Old Age Security;
- T4U Statement of Unemployment Insurance Benefits Paid;
- T5 Statement of Investment Income;
- T600 Ownership Certificate; and
- TFA1 Statement of Family Allowances.

You must report all types of income described on the return, if they were received by the deceased, even if no information slip was issued. If you cannot obtain an information slip, the Department will accept a letter or some other statement, from the people who made the payment, to confirm the income. If you cannot get this written confirmation or an information slip, estimate the income and attach a note to the return stating the amount received, and the name and address of the person who made the payment.

Income that is paid on a regular basis, such as interest, rents, royalties, annuities, or salaries and wages is considered to accrue in equal daily amounts during the period for which the amount was payable. This rule does not apply to amounts receivable but not payable on or before the date of death. In addition, it does not apply to income from annuity contracts that are considered to have been disposed of on death. For additional information on income receivable on or before the date of death, refer to Chapter 2 in this Guide.

Any amount that is not actually received before the taxpayer's death but is considered to have accrued to the date of death is included in the ordinary return for the year of death. For further details, obtain Interpretation Bulletin IT-210R, Income of Deceased Persons — Periodic Payments.

Certain income received after the date of death may be reported on the ordinary return for the year of death, or on the special return for "rights or things," if that filing option is exercised. Refer to Chapter 2 in this Guide for more information concerning rights or things.

The line numbers listed below refer to lines on the General and Special income tax returns. Only the most commonly used lines are explained.

**Lines 101 to 104 — Income from employment**
Include all amounts of salary or wages received from January 1 to the date of death. This includes amounts accrued from the beginning of the pay period in which the employee died to the date of death.

If a T4 slip is missing and cannot be obtained, estimate the income, the related payroll deductions such as Canada or Quebec Pension Plan contributions, Unemployment Insurance premiums, union dues and tax deducted at source. Attach a letter to the return explaining the situation and indicating the estimated amounts. Be sure to give the employer's name and address, and attach copies of any pay stubs available.

**Lines 113 to 115 — Pension income**
Include all amounts of pension or superannuation income received for the period from January 1 to the date of death. Do not include the "Net federal supplements paid" as shown in Box 21 or Box (H) on the T4A(OAS) slip. If the total "net income before adjustments" (line 234) from all returns filed for the year of death is more than $50,850, a portion of the Old Age Security benefits that the deceased received may have to be repaid. For more information, see line 235 of the *1990 General Tax Guide.*

Lump-sum amounts paid out of a pension fund or plan as a result of death are normally included in the income of the recipient. This includes a death benefit paid under the Canada or Quebec Pension Plan. The recipient beneficiary may be either the spouse, the children, or the estate. For information on how to report various lump-sum payments, including death benefits, refer to line 114 and item "D" under line 130 in the *1990 General Tax Guide.* For more information refer to Interpretation Bulletins IT-301, Death Benefits — Qualifying Payments and IT-508, Death Benefits — Calculation.

## Note

**A T3 Trust Income Tax Return and Information Return** must be filed when an estate is created after the death of a taxpayer. This return and the T3 Guide are available at any district office.

**Line 118 — Family allowance payments**
If the deceased was married from January 1, 1990, until the date of death, or separated as a result of a marriage breakdown for a period of less than 90 days starting in 1990,

- the spouse with the higher net income (before including family allowance and deducting child care expenses and social benefits repayments) must report the family allowance received in the year up to the date of death, no matter who received them;
- the surviving spouse reports the family allowance benefits that were received for the rest of the year.

If the deceased married in 1990 or was separated as a result of a marriage breakdown for a period of 90 days or more starting in the year of death,

- the family allowance payments for all the months that the couple was separated or not married must be reported by the person who received the family allowance cheques;
- the family allowance payments for all the other months, up to the date of death, must be reported by the spouse with the higher net income (before including family allowance and deducting child care expenses and social benefits repayments) for the year; and
- the surviving spouse must report the family allowance benefits that were received for the months after the date of death.

A portion of the family allowance payments may have to be repaid if the total "net income before adjustments" (from line 234) on the return(s) of the deceased for the year of death is more than $50,850. This amount includes the "net income before adjustments" from all returns filed for the year of death. For further information, refer to line 235 in the *1990 General Tax Guide.*

## Note

If one of the individuals is claiming an equivalent-to-married amount for a child, that individual must report the family allowance payments for the entire year for that particular dependant. This will be the case regardless of who actually received the payments.

**Line 119 — Unemployment Insurance benefits**
The deceased may have received Unemployment Insurance benefits before his or her death in 1990. A portion of these benefits must be repaid if the total "net income before adjustments" (from line 234) on the return(s) of the deceased for the year of death is more than $49,920. This amount includes the "net income before adjustments" from all returns filed for the year of death. For further information, refer to line 235 in the *1990 General Tax Guide.*

**Lines 120 and 121 — Investment income**
Report investment income received from January 1 to the date of death that was not reported in a previous year. Amounts accrued in that period but not yet paid should also be included.

Report interest from bonds that accrued from the last interest date before death to the date of death. Interest accrued on compound interest bonds to the date of death that was not already included in income in a previous year, is income of the deceased. Certain amounts of investment income may be reported as rights or things on a separate return. Refer to Chapter 2 in this Guide for more information.

Refer to the *1990 General Tax Guide* for more information on investment income.

### Line 129 — Registered retirement savings plan (RRSP)

For payments made out of an RRSP, a spouse must be a person of the opposite sex who up until the time of death

- was married to the deceased taxpayer,
- was living with the deceased in a conjugal relationship for at least one year, or
- was living with the deceased in a conjugal relationship and is a natural or adoptive parent of the child of the deceased.

The deceased may have been an annuitant under an unmatured RRSP. If the spouse of the deceased was the beneficiary under the plan, the spouse is entitled to receive the amount built up in the plan. The amount received is a "refund of premiums" and is included in the income of the spouse. If there is no spouse but certain children or grandchildren, who are financially dependent on the deceased, are beneficiaries under the plan, the amount received as a "refund of premiums" is considered to be their income.

However, you may have to include a portion of the amount in the plan in the income of the deceased. The amount you include is the difference between the fair market value of all the property in the RRSP, at the time of death, and the amounts designated as "refund of premiums" to the spouse, or dependent children or grandchildren.

Sometimes the deceased names the estate as the beneficiary of the RRSP. If this is the case, the funds in the RRSP are paid to the estate of the deceased. The legal representative and a beneficiary of the estate may then jointly elect to treat part or all of the amount as having been received by the beneficiary as a "refund of premiums." This may only be done, however, if the elected amount could have qualified as a "refund of premiums" had it been paid out of the RRSP directly to the beneficiary. This designation may be made by filing Form T2019, Registered Retirement Savings Plan (RRSP) Refund of Premiums Designation — Spouse. You may also use this form to designate a "refund of premiums" to a child or grandchild. Form T2019 is available at any district office.

Under certain circumstances, a "refund of premiums" to a named beneficiary may be transferred to an annuity or to an RRSP. This transfer must be done within the year the funds are received or within 60 days after the end of that year. For more information regarding amounts paid out of an RRSP as a result of death, refer to the *1990 Pension and RRSP Tax Guide* and Interpretation Bulletin IT-500, Registered Retirement Savings Plans (maturing after June 29, 1978) — Death of Annuitant after June 29, 1978.

**Note**

Refund of premiums received by the estate of the deceased can no longer be reported on the T3 return for the estate.

### Lines 130 to 143 — Other types of income

These lines on page 1 of the return cover other types of income that must be reported. Information on the various types of income and the required schedules may be found in the *1990 General Tax Guide*. If the deceased owned capital property at the date of death, refer to Chapter 3, "Deemed disposition of capital property at death," in this Guide.

### Reserves in year of death

When calculating income from a business and gains from the disposition of capital property, there are provisions that allow for the deduction of reserves that represent the income element of the proceeds of sale that the taxpayer will not receive until a later taxation year. A somewhat similar provision permits an insurance agent or broker to deduct a reserve for unearned commissions.

Generally, such reserves may not be deducted in the year of death. However, if the right to receive the uncollected proceeds is transferred to the spouse or spouse trust, the legal representative and the beneficiary of the transfer may jointly elect, on the prescribed form, to claim a reserve for this property. To make this election, you must fill out and submit Form T2069, Election in Respect of Amounts Not Deductible as Reserves for the Year of Death.

The deceased taxpayer, as well as the spouse to whom the property right is transferred, must have been resident in Canada immediately before the death of the taxpayer. In the case of a spouse trust, the trust must have been resident in Canada immediately after the time the property vested indefeasibly in the trust. Include an amount equal to the reserves claimed in the election as income from business, capital property or commissions, as the case may be, when computing the income of the spouse or spouse trust for the first taxation year ending after the death.

When a capital gains reserve arising from a disposition of property occurring after 1984 is reported by the spouse, spouse trust or by the deceased, this amount may qualify for the capital gains deduction for 1988 and subsequent taxation years.

## Lines 207 to 232 — Deductions from total income

### Line 208 — Registered Retirement Savings Plan (RRSP) contributions

When an individual dies, no further contributions can be made to his or her RRSP because there is no longer an annuitant. However, contributions, within the limits, can be made to a spousal RRSP on behalf of the deceased within 60 days of the date of death. For more information on the purchase of the spousal RRSP, refer to Interpretation Bulletin IT-307R2, Registered Retirement Savings Plan for Taxpayer's Spouse. Refer to the *1990 Pension and RRSP Guide* for more information on RRSPs.

**For information on line 207 and 212 to 232, see the *1990 General Tax Guide.***

**Line 237 — Accumulated forward-averaging amount withdrawal**
There are three options available for a deceased individual with an accumulated forward-averaged amount. The legal representative may choose one of the following:

- Ignore the accumulated forward-averaged amount. In this case, there are no further tax consequences.
- Elect to bring back all or part of the forward-averaged amounts into the income of the deceased for the year of death. In this case, the income may be taxed at a reduced rate under special provisions. If such an election is made using only a portion of the accumulated forward-averaged amounts, there will be no further tax consequences on the balance, unless you elect to have the three year carryback provision apply.
- Elect to apply the three year carryback provision.

Use Form T541, Forward Averaging Tax Calculation — Deceased Taxpayers, to calculate the tax on the forward-averaging amount. This form may be obtained at any district office.

**Note**
This form must be submitted on or before the date the return for the year of death is required to be filed.

## Deductions from net income

**Line 253 — Net capital losses of other years**
Special rules apply to capital losses in the year of death. Refer to Chapter 4 in this Guide for more information.

**Follow the instructions in the *1990 General Tax Guide* for the remaining deductions from net income.**

## Calculating total non-refundable tax credits

These credits are calculated in the section entitled "Calculation of total non-refundable tax credits" on page 2 of the 1990 T1 General Income Tax Return, and are explained in detail in the *1990 General Tax Guide.*

**Personal amounts**
You may claim the full personal amounts on the income tax return of the deceased. In other words, you do not prorate the personal amounts unless the deceased lived outside Canada at any time during the period from January 1 until the date of death. If the deceased immigrated to or emigrated from Canada before the date of death, refer to the *1990 Tax Guide for Emigrants,* or the *1990 Tax Guide for New Canadians.*

**Line 300 — Basic personal amount**
The deceased is entitled to the full basic personal amount of $6,169 for 1990.

**Line 301 — Age amount**
If the deceased was 65 years of age or older on the day of death, the individual is entitled to the age amount of $3,327 for 1990.

**Line 303 — Married amount**
The deceased is entitled to the full married amount for a spouse whose income, for the entire year, was not more than $514. A partial amount may be claimed if the spouse's income, for the entire year, was more than $514 but less than $5,655.

**Note**
The income of the surviving spouse for the entire year, rather than to the date of death, must be used to calculate the married amount. When claiming amounts for dependent children and additional personal amounts, the income for the entire year must also be used in the calculations.

The surviving spouse may claim the married amount for the deceased, within the same limits, if the surviving spouse had sufficient income before the death of the deceased, and was in a position to support the deceased. This would apply even if the income of the deceased, in the year of death, was not more than $514. To calculate the married amount, the surviving spouse must use the net income of the deceased from all returns filed for the year of death.

**Lines 304 and 305 — Amounts for dependent children and additional personal amounts**
Amounts for dependent children are calculated in the *1990 General Tax Guide.* Additional personal amounts are calculated on Schedule 6, Additional Personal Amounts. The person who is required to report the family allowance payments for a child may claim the "Amounts for dependent children" for that child.

If more than one person reports the family allowance received for a particular child, they both may claim an amount for the dependent child. The amount for the child is split in the same proportion as the family allowance is reported. However, the combined claim made by the deceased and the other person for each dependant may not be more than the maximum amount allowed for each child.

**For information on lines 308, 310 and 312, refer to the *1990 General Tax Guide.***

**Line 314 — Pension income amount**
If the deceased received eligible pension income before the date of death, it may be possible to claim the pension income amount. The amount that you may claim is the amount of pension income received in the year or $1,000, whichever is less.

Line 314 in the *1990 General Tax Guide*, lists eligible and ineligible pension income. Also included are charts that can be completed by different age groups. To help you calculate the eligible pension income, complete the chart that corresponds with the age of the deceased person.

**Lines 316 and 318 — Disability amount**
You may claim the disability amount of $3,327 if the deceased

- had a severe and prolonged mental or physical impairment in 1990 (a severe impairment is one that markedly restricts the activities of daily living), and
- the impairment has lasted or was expected to last for a continuous period of at least 12 months.

You may not claim the disability amount if the deceased or some other person claimed, on behalf of the deceased, medical expenses for a full-time attendant or full-time care in a nursing home because of a mental or physical impairment. You may claim the medical expenses or the disability amount, whichever is more favourable, but not both.

However, subject to certain conditions, the deceased may be entitled to the disability amount and medical expenses for an attendant. The attendant must have cared for the taxpayer in Canada before the date of death to enable the deceased to earn income for the year. For further information on "Attendant care expenses," refer to line 215 in the *1990 General Tax Guide.*

For more information on the disability credit, see the *How You Claim the Disability Credit* pamphlet and Interpretation Bulletin IT-519, Medical Expense and Disability Tax Credits.

**Line 326 — Amounts transferred from spouse**
You may transfer to the return of the deceased the unused portion of certain available credit amounts that are not required to reduce the surviving spouse's federal income tax to zero. Note, however, that the surviving spouse's income for the entire year must be considered.

Similarly, you may transfer to the return of the surviving spouse any unused portion of these amounts that are not required to reduce the federal income tax of the deceased to zero (on all returns filed for the deceased).

The following credits may be transferred:

- age amount (if the spouse was 65 years of age or older);
- pension income amount;
- disability amount; and
- tuition fees and education amount.

Refer to Schedule 2, Amounts Transferred from Spouse, in the 1990 General Tax Return package.

**Line 330 — Medical expenses**
The deceased is entitled to medical expenses that are more than $1,542 or 3 % of his or her net income, whichever is less. The expenses may be for any 24-month period, including the date of death, provided they have not previously been claimed. To make such a claim, complete Schedule 4, Medical Expenses, in the 1990 T1 General Tax Return package and attach the schedule and all receipts to the return.

For more details on eligible medical expenses, refer to Interpretation Bulletin IT-519, Medical Expense and Disability Tax Credits.

**Line 340 — Charitable donations**
The deceased is entitled to all charitable donations made in the current year and in the five immediately preceding years that were not previously claimed. If the claim includes amounts carried forward from previous years, attach a note to the return indicating the year in which these donations were made, and the amount carried forward. The maximum you may claim in the return of the deceased is 20 % of the net income for the year in question. You must attach official receipts to the return.

You may deduct charitable donations made in the year of death by the deceased, in the year before he or she died as long as the donations are not claimed in the year of death. You may claim bequests specified in the will of the deceased that are made to registered charities in the year of death if amounts claimed are supported by proper receipts. Refer to line 340 in the *1990 General Tax Guide.*

**Line 342 — Gifts to Canada or to a province**
You may claim an amount for gifts made to Canada, a province or to an institution in Canada for property certified by the Canadian Cultural Property Export Review Board.

Refer to the section "Charitable donations or gifts by will" in Chapter 5 in this Guide for further details.

## Summary of tax and credits

The tables required to calculate the taxes payable by the deceased are contained in the *1990 General Tax Guide.* If the income of the deceased is too high to use the tables, you must complete Schedule 1, Detailed Tax Calculation.

All items described under the heading "Summary of tax and credits" in the *1990 General Tax Guide* apply to the year of death.

**Note**
If the deceased paid minimum tax in 1986, 1987, 1988 or 1989, part of that tax may be deducted from the 1990 taxes payable. To calculate this claim, complete Part VII of Form T691, Calculation of Minimum Tax, and attach the completed form to the return of the deceased. Please note, however, that minimum tax does not apply in the year of death.

Line 446 — Federal sales tax credit
This credit may be claimed on the return of either the deceased or the surviving spouse. However, only one combined claim may be made.

**Note**
The total net income of the deceased from all returns filed for the year of death must be reflected in the calculation of this credit.

Provincial or territorial tax credits
A number of provinces have tax credit systems that work through the personal income tax system. In some cases, the deceased may be entitled to one of these tax credits. This credit is calculated on the provincial or territorial tax credit form included with the 1990 T1 General Income Tax Return package. Information or help to complete this tax credit form is available from any district office.

# CHAPTER 2
# ELECTIVE RETURNS

## Rights or things

At the time of death, the deceased may have had "rights or things." Rights or things are unpaid amounts that would have been included in income when realized or disposed of had the taxpayer not died. You must include the value of these amounts at the time of death in the income of the deceased for the year of death.

Items that are rights and things:

**Employment:**

- salary or wages,
- commissions,
- Unemployment Insurance benefits,
- Canada or Quebec Pension benefits, and
- vacation pay,

if they are owing to the deceased at the date of death but they relate to a pay period completed before the date of death.

**Other:**

- uncashed matured bond coupons;
- any other bond interest accrued before the most recent interest payment date and not reported in previous taxation years;
- harvested farm crops;
- livestock on hand (less basic herd);
- supplies on hand, inventory and accounts receivable of a taxpayer who reported on the cash method; and
- dividends declared before the date of death and unpaid at the date of death.

Items that are not rights or things:

- bond interest accrued between the most recent interest payment date before the taxpayer's death and the date of death;
- eligible capital property (see Chapter 3 in this Guide);
- resource properties;
- land in the inventory of the business of the deceased; and
- income from an income-averaging annuity contract.

For more details, obtain Interpretation Bulletins IT-210R, Income of Deceased Persons — Periodic Payments, IT-212R3, Income of Deceased Persons — Rights or Things, IT-234, Income of Deceased Persons — Farm Crops, IT-427, Livestock of Farmers, and Information Circular 86-6, Basic Herds.

As the legal representative of the deceased, you may elect to file a separate return and include only the value of rights or things as income. Details on the filing deadline for this return are explained at the beginning of this Guide under "Filing Returns."

If this election is made, income amounts you reported on this return should not be reported on the ordinary return. Prepare the separate return as though it was the return of another person. Refer to the section "Allowable deductions and non-refundable tax credit amounts for elective returns" in this Chapter for a list of allowable deductions and non-refundable tax credits.

**Note**
You may revoke this election by filing a written Notice of Revocation, signed by you as the legal representative for the deceased, within one year from the taxpayer's date of death or within 90 days after any Notice of Assessment for the year of death is mailed, whichever is later.

Rights or things that you would otherwise include in the income of the deceased may be transferred to a beneficiary if they are transferred within the time limit for filing a separate return. Do not include in the income of the deceased the value of the rights or things transferred to the beneficiary. The amount you include in the income of the beneficiary upon the realization or disposition of the right or thing are the proceeds eventually received for the right or thing minus

- its cost to the deceased (to the extent it was not deducted when computing the income of the deceased in any previous taxation year), and
- any expenses the beneficiary incurred to acquire the property.

## Allowable deductions and non-refundable tax credits for elective returns

As indicated at the beginning of this Guide under the "Filing Returns" section, you may file up to four separate T1 income tax returns for the deceased in the year of death. The credits and deductions that you may claim on these returns are listed below.

Certain non-refundable tax credits that you claim on the ordinary return may also be claimed on **each** of the elective returns. These are the

- basic personal amount,
- age amount,
- married amount,
- amounts for dependent children, and
- additional personal amounts.

You may also claim other non-refundable tax credits on **any** of the returns regardless of the type of income reported on the return. You may claim the total credit on one of the returns or you may split the credit and claim a portion on all the returns. However, the total claim for each credit may not be more than the credit that you could claim if you only filed the ordinary return with all the income reported on it. These credits are the

- disability amount,
- disability amount for dependant other than spouse,
- tuition fees and education amount for the deceased,
- tuition fees and education amount transferred from the child,
- medical expenses,
- charitable donations, and
- gifts to Canada or a province.

**Note**

Medical expenses are reduced by $1,542 or 3 % of the total net income reported on **all** returns, whichever amount is less. You may claim them on any one of the returns for the year of death.

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Charitable donations you claim on any return may not be more than 20 % of the net income reported on **that** return.

You may claim certain deductions from net income and certain non-refundable tax credits **only** on those returns on which you report the related income. These are

- Canada or Quebec Pension Plan contributions,
- Unemployment Insurance premiums,
- pension income amount,
- employee home relocation loan deduction,
- stock option and shares deduction,
- social benefits repayment, and
- vow of perpetual poverty deduction.

You may claim other deductions and credits only on the ordinary return of the deceased, as they do not apply to any of the elective returns. These include

- amounts transferred from spouse,
- capital gains deduction,
- child care expenses,
- losses from other years,
- northern residents deductions,
- withdrawals from the accumulated-averaging amount,
- child tax credit,
- federal sales tax credit, and
- refund of investment tax credit.

# CHAPTER 3
# DEEMED DISPOSITION OF CAPITAL PROPERTY AT DEATH

To help you understand the meaning of certain terms used in this chapter, we have provided the following definitions.

**"deemed disposition or acquisition"** means that the taxpayer is considered to have disposed of or acquired property, even though the transaction did not actually happen.

**"deemed proceeds"** means that the taxpayer is considered to have received an amount for the property even though no funds were actually received.

**"fair market value (FMV)"** is the highest price, expressed in terms of money or money's worth, that you can get in an open and unrestricted market between parties acting at arm's length, neither party being under any compulsion to transact.

**"capital property"** means any property including depreciable property, the disposition of which would result in a gain or loss.

## General information

The deceased is considered to have disposed of all capital property immediately before death. Such dispositions may result in

- a taxable capital gain, or
- an allowable capital loss,

and in the case of depreciable properties,

- a recapture of capital cost allowance (CCA), or
- a terminal loss.

In determining the capital gain or loss on the disposition of the property as well as any recapture of CCA or terminal loss, there are four relevant amounts. These four amounts are as follows:

- **The capital cost of the property.** For depreciable property, the capital cost usually means the actual cost plus the cost of additions and improvements minus any grant or financial assistance received or receivable from a government, municipality or other public agency for the purchase of that property. For other capital property, the adjusted cost base is required. The adjusted cost base usually means the actual cost plus or minus the additions and deductions provided in Subsections 53(1) and (2) of the *Income Tax Act*.
- **The undepreciated capital cost (UCC).** This is generally the capital cost of depreciable property in a prescribed class, less the sum of any disposals (i.e., proceeds of disposition or capital cost, whichever is less) in that class, and any CCA previously claimed.
- **The Valuation Day (V-Day) value.** This is the fair market value (FMV) of the property on V-Day. The V-Day value is important only for property acquired before January 1, 1972. For publicly traded shares, the V-Day is December 22, 1971. For all other assets it is December 31, 1971. If the deceased has not previously made the "V-Day" election, the legal representative may do so when the ordinary return is filed.
- **The proceeds of disposition.** This is the amount that is considered to have been received by the deceased at the time of death. It is generally equal to the FMV for capital property and an amount that is half-way between the FMV and UCC for depreciable property.

For the 1990 taxation year, the taxable portion of a capital gain and the allowable portion of a capital loss is **three quarters (3/4)**. If allowable capital losses incurred are more than taxable capital gains, refer to Chapter 4 in this Guide. For information on the capital gains deduction, refer to the *1990 Capital Gains Tax Guide*.

CCA on depreciable property **may not** be claimed for the financial period ending at the date of death.

**Note**

For certain passenger vehicles, a recapture of capital cost allowance is not required to be included in income, and a terminal loss is not deductible from income. Refer to Chapters 4 and 6 in the *1990 Business and Professional Income Tax Guide* for more information.

## Depreciable property of a prescribed class

### Deceased's deemed disposition

All depreciable property of a prescribed class that was owned by the deceased at the time of death is considered to have been disposed of immediately before death. The deceased is considered to have received proceeds of an amount that is half-way between the property's fair market value and its undepreciated capital cost at the time of death.

**Example**

| | |
|---|---|
| Undepreciated capital cost (UCC) at death | $30,000 |
| Fair market value (FMV) at death | $42,000 |

Deemed proceeds of disposition:

$$= \frac{FMV + UCC}{2}$$

$$= \frac{\$42,000 + \$30,000}{2}$$

$$= \$36,000$$

If the deemed proceeds of disposition are more than the capital cost, a capital gain will result. You must report the taxable capital gain on the ordinary return of the deceased. The disposition may also produce a recapture of CCA claimed in previous years. You also include any recapture as income on the ordinary return. Form T2086, Capital Dispositions Supplementary Schedule re: Depreciable Property upon the Death of a Taxpayer, may be of assistance. You will find a copy of the form in this Guide.

### Beneficiary's deemed cost

The cost of depreciable property to a beneficiary (other than a spouse or spouse trust) is generally considered to be equal to

$$\frac{\text{Fair market value of the particular depreciable property at time of death}}{\text{Fair market value of all depreciable property of that prescribed class at time of death}} \times \text{Amount of the proceeds deemed to have been received by the deceased for all depreciable property of that prescribed class}$$

If this calculation results in a cost that is less than the capital cost to the deceased, the capital cost to the beneficiary will be an amount equal to the capital cost to the deceased. The excess is considered to have been allowed as CCA to the beneficiary.

The effect of the above is that terminal losses and the recapture of CCA are reduced for the deceased below what they would have been if the property was disposed of at its FMV during the life of the deceased. These reductions are passed on to the beneficiary where they may be realized when the property is actually disposed of.

**Transfer to spouse or spouse trust**

If depreciable property of a prescribed class is transferred to the spouse or a spouse trust, the deceased is considered to have disposed of the property, and the spouse or spouse trust to have acquired it at a cost equal to

$$\frac{\text{Fair market value of the particular property immediately before death}}{\text{Fair market value of all property of that prescribed class immediately before death}} \times \text{Undepreciated capital cost to the deceased of all property of that class immediately before death}$$

The property is generally transferred or "rolled over" to the spouse or spouse trust without giving rise to any recapture of CCA, terminal loss or capital gain for the deceased. The spouse or spouse trust calculates future CCA claims based on the UCC of the property to the deceased, as indicated in the previous calculation.

If the property's cost, as previously calculated, to the spouse or spouse trust is less than the capital cost to the deceased, the cost to the spouse or spouse trust is considered to be equal to the capital cost to the deceased. The excess is considered to have been allowed as CCA to the spouse or spouse trust.

The effect of the above is that any accrued capital gains, recapture of CCA and terminal losses are generally carried forward until the time the property is actually disposed of by the spouse or spouse trust or until the death of the spouse, whichever comes first.

As the legal representative, you may elect not to apply the rollover provisions. Instead, you may use the disposition rules explained under the "Deceased's deemed disposition" and "Beneficiary's deemed cost" sections in this chapter. For additional details, obtain Interpretation Bulletin IT-305R3, Establishment of Testamentary Spouse Trust.

Depreciable farm property of a deceased taxpayer that is transferred to his or her child may also be rolled over at a value equal to its UCC. Refer to the section "Disposition of farm property to a child" in this chapter.

**Transitional rules**

Certain transitional rules provide for an adjustment to the deemed proceeds of disposition to prevent taxing any capital gain that accrued on property before December 31, 1971 (V-Day). For these rules to apply,

- the depreciable property must have been owned by the deceased on V-Day,
- the capital cost of the property to the deceased was less than the FMV on V-Day, and
- the capital cost to the deceased was less than the proceeds of disposition as determined under the section "Deceased's deemed disposition" in this chapter.

The transitional rules specify that the taxpayer's proceeds of disposition of the property shall be deemed to be an amount equal to the total of

- the capital cost of the property to the deceased,

**plus**

- the amount, if any, by which the deceased's proceeds of disposition (as determined under the section "Deceased's deemed disposition" at the beginning of this chapter), exceeds the FMV of the property on V-Day.

## Example

Mrs. Lee died in June 1990. Mrs. Lee owned depreciable property at her date of death that she had purchased in 1966 for $74,000. The FMV of the property on V-Day is $80,000, and the FMV of the property at the date of death is $100,000. The UCC of the property is $66,000.

Deemed proceeds of disposition as determined under "Deceased's deemed disposition" in this chapter

$$\frac{(\$100{,}000 + \$66{,}000)}{2} = \$83{,}000$$

**The deemed proceeds of disposition calculated using the transitional rules equals $77,000 ($74,000 + ($83,000 — $80,000).**

| | |
|---|---|
| Deemed proceeds of disposition | $77,000 |
| Capital cost | $74,000 |
| Capital gain | $ 3,000 |
| Taxable capital gain ($3,000 × ¾) | $ 2,250 |
| Capital cost | $74,000 |
| Undepreciated capital cost | $66,000 |
| Recapture of capital cost allowance | $ 8,000 |

Therefore, you report a taxable capital gain of $2,250 on Mrs. Lee's Schedule 3, Summary of Dispositions of Capital Property in 1990. Also, you

report a recapture of $8,000 on her return. You may complete these calculations on Form T2086, Capital Dispositions Supplementary Schedule re: Depreciable Property upon the Death of a Taxpayer.

The deceased may have had more than one capital property. For information on the deemed disposition of more than one property, refer to the Special Release dated September 13, 1982 for Interpretation Bulletin IT-217, Capital Property Owned on December 31, 1971 — Depreciable Property.

The depreciable property owned on December 31, 1971 may have been transferred to a spouse or spouse trust. In this situation, the transitional rules do **not** apply in determining the proceeds of disposition for the deceased and the acquisition cost to the spouse or spouse trust.

The instructions for "Transfer to spouse or spouse trust" should be followed in such cases. For transfers of depreciable farm property to the child of the deceased, follow the calculation under "Disposition of farm property to a child" in this chapter. When the spouse, spouse trust or child eventually dispose of the property, the transitional rules could apply as if the spouse, spouse trust or child had acquired the property before 1972, and owned it from December 31, 1971 until the date of disposition.

## Other capital property

Other capital property, such as shares of a small business corporation, is considered to be disposed of at its fair market value (FMV) at the date of death. The cost of the property to the beneficiary is considered to be equal to the deemed proceeds of disposition.

If farm property is passed to a child as a result of death, calculate the proceeds as explained under "Disposition of farm property to a child" in this chapter.

**Note**

If qualified small business corporation shares were disposed of after June 17, 1987, resulting in a net taxable capital gain in the year of death or in a preceding year, you may claim the upper limit of the capital gains deduction. Refer to the *1990 Capital Gains Tax Guide* for information on how to calculate this deduction.

### Transfer to spouse or spouse trust

When capital property is transferred to the spouse or a spouse trust, the deemed proceeds of disposition are equal to the adjusted cost base to the deceased immediately before death. Accordingly, the spouse or spouse trust is considered to have received the property at this adjusted cost base.

**Note**

As the legal representative, you may elect not to apply this rule. If this is the case, follow the usual rules for FMV dispositions. Refer to Interpretation Bulletin IT-305R3, Establishment of Testamentary Spouse Trust.

Under proposed legislation, in certain circumstances, if property transferred is an interest in a partnership, the deceased taxpayer will be treated as not having disposed of the interest before his or her death. The spouse or the spouse trust will effectively be treated as having acquired the interest for an amount equal to the adjusted cost base to the deceased. This rule will apply to transfers, distributions and acquisitions after January 15, 1987.

### Transitional rules

The deceased may have owned capital property (other than depreciable property or a partnership interest) on December 31, 1971. You may use the "median rule" to calculate the cost of the property unless it is elected to establish the cost for all such property at the FMV on V-Day value. To use the median rule, you need to know the actual cost of the property, the FMV of the property on V-Day and the proceeds of disposition. The cost of the property is considered to be the median of these three amounts.

However, if the deceased had disposed of any such property before the date of death, and either one of the valuation methods was selected, the legal representative must follow the same method for all deemed dispositions of such property in the year of death. Obtain Interpretation Bulletins IT-84, Capital Property Owned on December 31, 1971 — Median Rule (Tax-Free Zone), and IT-139R, Capital Property Owned on December 31, 1971 — Fair Market Value, and the *1990 Capital Gains Tax Guide* for further details on the median rule and the FMV methods.

You must report any capital gains and claim any capital losses arising from the deemed disposition of such other capital property on the ordinary return. Refer to the *1990 Capital Gains Tax Guide* for details regarding the capital gains deduction. For details on claiming capital losses, refer to Chapter 4 in this Guide.

### Disposition of farm property to a child

A family farm (depreciable property and land) may be transferred to a child upon the death of a taxpayer. If farm property is transferred to a child, you do not handle the deemed disposition the same as other deemed dispositions if:

- the property, located in Canada, was used in the business of farming by the taxpayer, the spouse or any of the taxpayer's children immediately before the taxpayer's death;
- the child was resident in Canada immediately before the taxpayer's death; and
- it can be shown that the property became vested indefeasibly in that child within 36 months of the

death. If additional time is needed to prove that vesting occurred, you may request an extension by writing to the Minister. This request must be made within 36 months after the date of death. For further details, refer to Interpretation Bulletin IT-449R, Meaning of "Vested Indefeasibly."

The definition of **child** includes:

- a grandchild;
- a great-grandchild;
- a child of the taxpayer's spouse;
- a spouse of the taxpayer's child;
- an adopted child of the taxpayer;
- a person of whom the taxpayer is the natural parent whether the person was born within or outside a marriage; and
- a person who, at any time while he or she was under 19 years of age, was in the custody and control of the deceased, in law or in fact, and was wholly dependent on the deceased for support.

For purposes of the transfer rules, the taxpayer's relationship with the child must have existed at the time of the transfer.

You calculate the proceeds of the farm property's deemed disposition as follows:

(a) for depreciable property of a prescribed class:

$$\frac{\text{Fair market value of the particular property immediately before death}}{\text{Fair market value of all property of that prescribed class immediately before death}} \times \text{Undepreciated capital cost to the taxpayer of all property of that prescribed class immediately before death}$$

(b) for land:

the adjusted cost base of the property to the taxpayer immediately before his or her death.

As a result of this calculation, no capital gain, capital loss, terminal loss or recapture of CCA generally arises for the deceased taxpayer. The cost of the property to the child is considered to be an amount equal to the deemed proceeds of disposition for the deceased.

If the child is considered to have acquired a depreciable property of a prescribed class at a cost that is less than the capital cost of the property for the deceased, the cost for the child is considered to be equal to the capital cost for the deceased. The excess is considered to have been allowed as CCA to the child.

You may replace these rollover provisions with alternative rules. Under the alternative rules, you may transfer the properties at any amount elected. However, the amount is subject to certain restrictions. For depreciable property, the elected amount must be between the UCC and the FMV. If there is more than one property in a class, you allocate the UCC to each property concerned in accordance with the formula used in (a) above. In the case of land, the elected amount must be between the adjusted cost base and the FMV immediately before the death of the taxpayer. If you wish to transfer the farm property using the alternative rules, file the election with the ordinary return of the deceased.

This election and rules relating to land also apply when a share of the capital stock of a family farm corporation or an interest in a family farm partnership has been transferred to the child of the deceased.

Under proposed legislation, when property transferred is an interest in a family farm partnership, the deceased taxpayer will be considered not to have disposed of the property as a result of his or her death. The child will generally be treated as having acquired the interest (property) for an amount equal to the adjusted cost base to the deceased taxpayer. This rule will apply to partnership interests, other than those to which Subsections 100(3) of the Act applies, and will apply to transfers, distributions and acquisitions occuring after January 15, 1987.

Farm property, located in Canada, could be transferred to a spouse trust created by a will, or under an inter vivos transfer, first for the benefit of the spouse, and then upon the death of the spouse for the benefit of the child or children of the deceased. If this is the case, the property is considered to have been disposed of by the spouse trust and acquired by the child at its UCC or adjusted cost base to the trust. It could happen that the child, who has received farm property either directly upon the death of the taxpayer, or upon the death of the taxpayer's spouse through an intervening testamentary or inter vivos spouse trust, dies before the parent. In such a situation, you may distribute such property to the parent in the manner indicated in the preceding paragraphs.

The definition of **parent** includes

- a person of whom the taxpayer is the child, whether born within or outside the marriage;
- the taxpayer's mother-in-law and father-in-law;
- a person who has custody and control of the taxpayer or had custody and control before the taxpayer reached 19 years of age and on whom the taxpayer is wholly dependent for support; and
- a person who, in law or in fact, had adopted the taxpayer.

For more information on this subject, contact your district office. You can also obtain Interpretation Bulletin IT-349R2, Intergenerational Transfers of Farm Property on Death.

## Eligible capital property

This type of property consists of goodwill and other "nothings" acquired after 1971 to produce income from a business. When an eligible capital property of the deceased is **acquired by a person, other than a spouse, or a controlled corporation** that carries on the business of the deceased, the eligible capital property is considered to have been disposed of immediately before death.

The property will be disposed of for an amount equal to either twice or four-thirds (4/3) the cumulative eligible capital, depending on whether the taxpayer's death occurred before or after the beginning of the first fiscal period of the deceased taxpayer's business starting after 1987. As a result of the deemed disposition, no amount is included in the income of the deceased. Since there is a zero balance in the cumulative eligible capital account of the deceased, the deduction that is normally allowed when a taxpayer no longer carries on a business does not apply.

If the **spouse or the controlled corporation carries on the business** of the deceased, the value of eligible capital property for the beneficiary is the same amount as the cumulative eligible capital of the deceased at the date of death. As a result of the business transfer, you do not include any amount in the income of the deceased for the eligible capital property that the deceased had at the time of death.

If the eligible capital property is **not transferred to any person** upon the death of the taxpayer, the deceased is considered to have stopped carrying on the business at the time of death. In this situation, a deduction of the cumulative eligible capital account that is normally allowed when a taxpayer no longer carries on a business will apply at the date of death.

For additional information, refer to Chapter 7 in the *1990 Business and Professional Income Tax Guide* and obtain Interpretation Bulletin IT-344R, Eligible Capital Property — Deceased Persons.

## Resource property or land inventory

If an individual holds Canadian or foreign resource property or holds land in the inventory of a business at the time of death, special rules apply to the deemed disposition of this property. Obtain Interpretation Bulletin IT-329R, Income of Deceased Persons - Resource Properties, for more details.

# CHAPTER 4
# NET CAPITAL LOSSES

## Net capital losses in the year of death

A capital loss may be incurred in the year of death as a result of a disposition (including a deemed disposition) of capital property owned by the deceased before death. This does not include depreciable property or most personal-use property such as a principal residence.

If a taxpayer's allowable capital losses in the year of death are more than the taxable capital gains in the same year, you may apply the excess against the taxable capital gains of the three immediately preceding years. You must reduce any remaining net capital losses by the lifetime capital gains deduction claimed to date by the deceased. You may then apply the balance of net capital losses, in full, to reduce other income in either the year of death, the immediately preceding year, or a portion may be deducted in each year.

In some situations, you may decide not to apply the net capital loss or a part of it against the taxable capital gains of the three immediately preceding years. If this is the case, reduce the net capital loss not carried back by the lifetime capital gains deduction claimed to date by the deceased. Then apply the balance of the net capital loss to reduce other income in either the year of death, the immediately preceding year or a portion may be deducted in each year.

The deductible portion of capital losses has increased since 1988. The taxable portion of capital gains has also increased by the same ratio. In 1988, the deductible portion of losses was increased from one half (1/2) to two thirds (2/3). It remained at two thirds (2/3) for 1989. In 1990, it was increased to three quarters (3/4). As a result, a 1990 net capital loss which had been calculated at three quarters (3/4) requires an adjustment when you carry it back to a year before 1990. You adjust the 1990 capital loss as follows:

- If you carry a 1990 net capital loss back to 1987, reduce the loss by multiplying it by .667.
- If you carry a 1990 net capital loss back to 1988 or 1989, reduce the loss by multiplying it by .889.

When you apply the above factors to a net capital loss, you obtain the **adjusted net capital loss.**

If any balance of the **adjusted net capital loss** for the year of death remains after you apply the maximum amount deductible in any of the three previous years, you must readjust this amount to reflect the 1990 net capital loss ratio. You may then apply this readjusted amount of net capital loss to offset other income in the year of death, in the preceding year, or a combination

of both. You determine the readjusted amount and the maximum deduction from other income as follows:

- unapplied **adjusted net capital loss** for 1988 and 1989 (for a 1987 capital loss use 1.5) × 1.125 = balance of the 1990 net capital loss

- balance of the 1990 net capital loss − lifetime capital gains deduction claimed to date by the deceased = the deductible amount against other income in the year of death, the preceding year or both

### Example

Mrs. O'Brien died in 1990. She incurred a net capital loss of $1,800 during 1990. She did not have any taxable capital gains in 1990. However, she reported a taxable capital gain of $300 in 1989. Therefore, her legal representative is requesting that part of the net capital loss be carried back to 1989 and applied against the capital gain incurred in that year. Her lifetime capital gains deduction claimed to date is nil.

The maximum amount of Mrs. O'Brien's 1990 net capital loss that may be applied against her net taxable capital gains in 1989 is the lesser of

- $1,800 × .889 = $1,600 (**adjusted net capital loss**) and
- $300.

The maximum deductible amount is $300, which is the taxable capital gain for 1989.

$1,600 **adjusted net capital loss**
− 300 maximum to be applied to 1989
$1,300 unapplied **adjusted net capital loss**

To deduct Mrs. O'Brien's unapplied 1990 net capital loss against other income for 1990, 1989 or a portion on both returns, the unapplied adjusted net capital loss must be converted to the 1990 ratio.

$1,300 × 1.125 = $1,463 (Amount deductible against other income)

To request an adjustment to a return for the previous year, complete Form T1A, Request for Loss Carry-Back, available from any district office.

### Note

The capital gains deduction that can be claimed for the year of death or the immediately previous year is reduced by any net capital losses deducted in those years.

## Net capital losses before the year of death

The deceased may have net capital losses that were incurred before the year of death but were not claimed in a previous year. To deduct capital losses of previous years against 1990 taxable capital gains, you must first convert them to the 1990 amount. You do this by using the following adjustment factors:

- If you carry net capital losses of 1987 forward and apply them against net taxable gains in 1990, you must first increase the loss by multiplying it by 1.5.
- If you carry net capital losses of 1988 or 1989 forward and apply them against net taxable gains in 1990, you must first increase the loss by multiplying it by 1.125.

When you apply the 1.5 or 1.125 factor to the unapplied net capital loss, you get the adjusted net capital loss. For example, if the deceased had 1988 or 1989 unapplied net capital losses, and you want to carry them forward to 1990, you would use the 1.125 factor in the following calculation:

unapplied net capital loss of prior years (1988 and 1989) × 1.125 = the **adjusted net capital loss** at the 1990 ratio.

You would then apply the **adjusted net capital loss** against net taxable capital gains in the year of death. You would report the lesser of this amount and the net taxable gain in the year of death on the return of the deceased.

After you apply the adjusted net capital loss against net taxable gains, there may still be some unapplied losses. If there is, you readjust any remaining losses by multiplying the balance by the adjustment factor for the year in which the losses were incurred (.667 if the net capital loss was incurred in 1987 and .889 if the net capital loss was incurred in 1988 or 1989). You reduce this readjusted balance by the total capital gains deductions claimed to date, including the year of death, and apply any remaining amount to reduce taxable income in either the year of death, the immediately previous year, or a portion in each year. You determine the readjusted amount and the maximum deduction from other income as follows:

- **unapplied adjusted net capital loss** (1988 and 1989) × 0.889 = balance of the net capital loss of prior years

- balance of the net capital loss of prior years − lifetime capital gains deduction claimed to date including the year of death = the amount deductible against other income in the year of death, the preceding year or both.

### Example

Mr. Burdick died in 1990. He had a 1988 unapplied net capital loss of $10,000. In 1990 he had a net taxable capital gain of $3,000.

Mr. Burdick claimed a total capital gains deduction of $4,000 in previous years.

The maximum amount of the previous year net capital loss that may be applied against Mr. Burdick's 1990 net taxable capital gains is the lesser of

- $10,000 × 1.125 = $11,250, and
- $3,000.

The maximum amount is $3,000, which is the net taxable capital gain in 1990.

| | |
|---|---|
| $11,250 | **adjusted net capital loss** |
| − 3,000 | maximum to be applied in 1990 |
| $ 8,250 | unapplied **adjusted net capital loss** |

The amount of the unapplied net capital loss that may be applied against Mr. Burdick's other income in 1990, 1989 or a portion on both returns is calculated as follows:

- $8,250 × .889 = $7,334;
- $7,334 − $4,000 = $3,334 (amount that may be applied against his other income in the year of death, the preceding year, or a combination of both).

### Example

Mr. O'Donnell died in 1990. He had a 1987 unapplied net capital loss of $180. In 1990, he had a net taxable capital gain of $300. Mr. O'Donnell claimed a total capital gains deduction of $50 in previous years.

The maximum amount of the 1987 net capital loss that may be applied against Mr. O'Donnell's 1990 taxable capital gain is the lesser of

- $180 × 1.5 = $ 270, and
- $300.

The maximum amount is $270, which is the 1987 adjusted net capital loss.

| | |
|---|---|
| $ 300 | net taxable capital gains in 1990 |
| − 270 | maximum to be applied in 1990 |
| $ 30 | remaining net taxable capital gains in 1990 |

In this situation, Mr. O'Donnell's full net capital loss may be applied to reduce his net taxable capital gains.

You will find more information on losses in the *1990 Capital Gains Tax Guide*, which is available from any district office.

### Note

Please note that the capital gains deduction that can be claimed for the year of death or for the immediately previous year is reduced by any net capital losses deducted in those years.

# CHAPTER 5
# OTHER

## Spouse trust

A spouse trust is created by the terms of the will of the deceased. The Department also considers a trust to be created by the terms of the will if it is created by an order of a court according to any law of a province providing for the relief or support of dependants. The spouse must be entitled to receive **all of the income** of the trust that arises during the spouse's lifetime, and **no person except the spouse can obtain or use any of the income or capital while the spouse is alive.** A trust will not be recognized as being a spouse trust if the spouse ceases to be entitled to receive all income of the trust following an event other than his or her death.

A trust may still qualify as a spouse trust even though the testamentary debts, including all income taxes of the deceased, death taxes and income taxes of the trust, are payable out of property that otherwise would form part of the trust. The legal representative may decide to appoint sufficient assets to cover payment of these testamentary debts by listing designated assets, the value of which is equal to or more than the testamentary debts, in the return of the deceased. The appointed property is not subject to the rollover provisions, but the trust qualifies as a spouse trust for the remaining property.

A spouse trust will not be disqualified if dividends, excluded from trust income by virtue of Section 83 of the *Income Tax Act,* are treated as capital receipts and are distributed (after the spouse's death) to beneficiaries other than the spouse. For more details, obtain Interpretation Bulletin IT-207R, "Tainted" Spouse Trusts.

The following conditions must also be met if a transfer of property to a spouse trust is to be considered as a rollover:

- The deceased taxpayer had been resident in Canada immediately before death.
- The trust must have been resident in Canada immediately after the property vested indefeasibly in the trust.
- It must be shown within 36 months of the date of death that the property has become vested

indefeasibly in the spouse or spouse trust. If you need additional time, as the legal representative, you have the option of requesting an extension by writing to the Minister. The request must be made within 36 months after the date of death. Refer to Interpretation Bulletin IT-449R, Meaning of "Vested Indefeasibly," for more information on this matter.

A renunciation by a beneficiary under a will or on an intestacy makes possible the rollover of property, relating to this renunciation, to a spouse trust. A renunciation involves an outright refusal to accept the disposition of a will without specifying how the legal representative should distribute the disclaimed property. This disclaimer must be made within the 36-month period previously mentioned for indefeasible vesting of property. For a more detailed discussion on spouse trusts, refer to Interpretation Bulletin IT-305R3, Establishment of Testamentary Spouse Trusts.

## Disposition of property by legal representative (164(6))

In the course of administering the estate of a deceased taxpayer, you may have, within the first taxation year of the estate,

- disposed of capital property of the estate that resulted in an excess of capital losses over capital gains, or
- disposed of all the depreciable property of a prescribed class of the estate that resulted in a terminal loss in that class at the end of the first taxation year of the estate.

In such a situation, you may elect in a prescribed manner and within the prescribed time period to deem such losses or part of them to have been incurred by the deceased from the disposition of property in the year of death rather than by the estate. However, the amount of the capital losses for which you can make this election cannot be more than the excess of capital losses over capital gains. If the disposition resulted in a terminal loss, the elected amount cannot be more than the amount that would have been the total of the non-capital loss and the farm loss, if any, of the estate for its first taxation year in the absence of the election. To make this election, you must submit to the Department certain information, as outlined in Part X of the *Income Tax Regulations*. Contact any district office to obtain details on what information is required.

You must file this election and an amended return indicating "164(6) Election" at the top of the return for the deceased for the year of death by the later of

- the last day you are required or have elected to file for the year of death, and
- the day the estate's return must be filed for its first taxation year.

The election and the amended return have no effect on any of the previous year returns of the deceased. The estate does not claim any of the elected losses. Refer to the *1990 T3 Guide and Trust Return* for filing requirements of T3 estate returns.

## Charitable donations or gifts by will

When a deceased person has made, by will, a charitable donation, a gift to Canada or a province, or a cultural gift (supported by proper receipts), the donation or gift is considered to have been made by the taxpayer in the year of death.

The amount of charitable donations and gifts that you may claim on the return of the deceased is the total of

- the lower of
  - charitable donations made in the year as well as donations made in 1985 to 1989 which were not previously claimed, and
  - 20% of the deceased taxpayer's net income from all returns filed for the year of death,
- total gifts to Canada or a province,
- total cultural gifts certified by the Canadian Cultural Property Export Review Board.

The allowable amount of charitable donations is shown on line 340, and the total gifts to Canada or a province plus cultural gifts is shown on line 342 on the deceased taxpayer's income tax return.

The total amount of donations and gifts is then used to calculate the non-refundable tax credit. You apply 17% to the first $250 of the total and 29% to the total over $250. A donation may not be fully deductible in the year of death because it is more than the 20% limit, and the amount of gifts may not be fully deductible because the credit for the gifts is more than the taxpayer's tax payable for the year. If this is the case, you may request that the deceased taxpayer's previous year return be adjusted to include the donations and gifts within the limits mentioned.

**Note**

A claim for a credit for gifts to Canada or a province and cultural gifts is not limited to 20% of the individual's net income like the other donations.

The charitable donation or gifts to Canada or a province may consist of capital property which, at the time of the donation, had a fair market value greater than the adjusted cost base to the taxpayer. In such a situation, you may designate an amount, not greater than the fair market value and not less than the adjusted cost base, as the amount of the gift or donation. This amount is considered to be the proceeds of disposition of the property to the deceased, and is used to calculate the tax credit.

The charitable donation or gifts to Canada or a province may consist of a work of art created by the deceased person that is property in inventory. In this situation, you may designate the amount of the deemed proceeds of disposition of the work of art and use this amount to calculate the tax credit. This amount may be determined by allocating an amount, not greater than the fair market value and not less than the inventory value for tax purposes, for the work of art to the individual at the time of the donation. You must support the claim with a proper receipt.

For cultural gifts, you must attach to the return, Form T871 — Cultural Property Income Tax Certificate, issued for the property by the Canadian Cultural Property Export Review Board and the official receipt issued by the institution that received the gift. Cultural gifts are objects that the Board has determined meet all the criteria set out in the *Cultural Property Export and Import Act.*

For more information, refer to Interpretation Bulletins IT-297R, Gifts in Kind to Charity and Others, IT-407R2, Disposition of Canadian Cultural Property (for 1987 and previous years), IT-407R3, Disposition of Canadian Cultural Property (for 1988 and later taxation years), and the brochure entitled *Gifts in Kind.*

## Income earned after death

The legal representative of the estate reports income that is attributable to the period after death on a T3 Trust Return. The 1990 T3 Guide provides additional information on this matter. You may obtain this guide and return from any district office.

## Payment of tax

For the year of death, you may elect to defer payment of a portion of the tax attributed to income from the value of rights or things at the date of death, and from deemed dispositions of capital property at death. This election requires that you pay the deferred tax in 10 equal consecutive annual instalments. Interest, at a prescribed rate, will be charged. The first payment is due at the same time that you are required to file the return. You make this election on prescribed Form T2075, Election under Subsection 159(5) by a Deceased Taxpayer's Legal Representative to Defer Payment of Income Tax. You must submit a copy of Form T2075 to the district office serving the area where the taxpayer lived before his or her death, no later than the date on which the first instalment is due.

**Note**

You must furnish security acceptable to the Minister to guarantee payment of the deferred tax. To make security arrangements, contact the Collections Section of the district office serving the area where the taxpayer lived before his or her death.

## Clearance certificate

To avoid any personal liability for any unpaid taxes, interest and penalties owed by the deceased, every administrator or executor must get a clearance certificate before distributing any property under his or her control.

The Department cannot issue a clearance certificate until all the required income tax returns have been filed and assessed, and all taxes, contributions to Canada or Quebec Pension Plan, Unemployment Insurance premiums, interest and penalties have been paid or secured. Therefore, a request for a clearance certificate should **not** be made until the assessment notices have been received for all returns filed for the deceased. Do not include the request with the income tax returns, as returns are sent to a taxation centre for processing, while clearance certificates are issued by district offices.

Mail your written request for a clearance certificate to the attention of the Business Audit Section at the district office serving the area where you, the legal representative, are located. The request should identify;

- the name, address and title (such as executor or administrator) of the person(s) requesting the certificate; and
- the full name, last address, social insurance number and date of death of the deceased.

The following documentation should also be provided with the request:

- a copy of the will;
- a statement showing the assets of the estate at the date of death, together with the adjusted cost base and fair market value of the properties; and
- in the case of intestacy, identity of the administrator and details of the proposed distribution of the assets, including the names and addresses of the beneficiaries and their relationship to the deceased.

The certificate covers all taxation years to the date of death. It does not include a clearance for any liability resulting from a trust that was, or should have been, established for the period after death. The *1990 T3 Guide and Trust Return* contains more information regarding trusts. It can be obtained from any district office.

Under proposed legislation, the administrator or executor of the estate will have to provide an application for the clearance certificate in prescribed form.

For further details concerning a request for a clearance certificate, refer to Information Circular 82-6, Requesting Clearance Certificates for Estates and Trusts and Interpretation Bulletin IT-282R, Estate or Trust Distributions — Clearance Certificates.

# REFERENCES

For more information, you may obtain the following publications from any district office.

## Guides

Business and Professional Income Tax Guide
Capital Gains Tax Guide
Child Care Expenses Tax Guide
Employment Expenses Tax Guide
Farming Income Tax Guide
Fishing Income Tax Guide
General Income Tax Guide
Instalment Guide for Individuals
Northern Residents Deductions Tax Guide
Pension and RRSP Tax Guide
Rental Income Tax Guide
T3 Guide and Trust Return
Tax Guide for Emigrants
Tax Guide for New Canadians

## Brochures

Gifts in Kind
How You Claim the Disability Credit

## Forms

| | |
|---|---|
| T1A | Request for Loss Carry-Back |
| T541 | Forward Averaging Tax Calculation - Deceased Taxpayers |
| T657 | Calculation of Capital Gains Deduction (1990) |
| T691 | Calculation of Minimum Tax |
| T936 | Calculation of Cumulative Net Investment Loss on December 31, 1990 |
| T2019 | Registered Retirement Savings Plan Refund of Premiums Designation - Spouse |
| T2069 | Election in Respect of Amounts Not Deductible as Reserves for the Year of Death |
| T2075 | Election under subsection 159(5) to Defer Payment of Income Tax on the Deemed Disposition of Property |
| T2086 | Capital Dispositions Supplementary Schedule re: Depreciable Property upon the Death of a Taxpayer |
| T2204 | Calculation of Employee Overpayment of Canada Pension Plan Contributions and Unemployment Insurance Premiums |

## Interpretation Bulletins

| | |
|---|---|
| IT-84 | Capital Property Owned on December 31, 1971 — Median Rule (Tax-Free Zone) |
| IT-139R | Capital Property Owned on December 31, 1971 — Fair Market Value |
| IT-140R3 | Buy-Sell Agreements |
| IT-172R | Capital Cost Allowance — Taxation Year of Individuals |
| IT-172R | Special Release Dated June 13, 1986 |
| IT-207R | "Tainted" Spouse Trusts |
| IT-210R | Income of Deceased Persons — Periodic Payments |
| IT-212R3 | Income of Deceased Persons — Rights or Things |
| IT-217 | Capital Property Owned on December 31, 1971 — Depreciable Property |
| IT-217 | Special Release Dated September 13, 1982 |
| IT-234 | Income of Deceased Persons — Farm Crops |
| IT-278R | Death of a Partner or a Retired Partner |
| IT-282R | Estate or Trust Distributions — Clearance Certificates |
| IT-297R2 | Gifts in Kind to Charity and Others |
| IT-301 | Death Benefits — Qualifying Payments |
| IT-305R3 | Establishment of Testamentary Spouse Trust |
| IT-307R2 | Registered Retirement Savings Plan for Taxpayer's Spouse |
| IT-326R2 | Returns of Deceased Persons as "Another Person" |
| IT-329R | Income of Deceased Persons — Resource Properties |
| IT-337R2 | Retiring Allowances |
| IT-344R | Eligible Capital Property — Deceased Persons |
| IT-349R2 | Intergenerational Transfers of Farm Property on Death |
| IT-382 | Debts Bequeathed or Forgiven on Death |
| IT-407R2 | Disposition of Canadian Cultural Property (1987 and previous years) |
| IT-407R3 | Disposition of Canadian Cultural Property (1988 and later years) |
| IT-416R3 | Valuation of Shares of a Corporation Receiving Life Insurance Proceeds on Death of a Shareholder |
| IT-427 | Livestock of Farmers |
| IT-449R | Meaning of "Vested Indefeasibly" |
| IT-486R | Intergenerational Transfers of Shares of a Small Business Corporation |
| IT-500 | Registered Retirement Savings Plans (maturing after June 29, 1978) Death of Annuitant after June 29, 1978 |
| IT-502 | Employee Benefit Plans and Employee Trusts |
| IT-508 | Death Benefits — Calculation |
| IT-519 | Medical Expense and Disability Tax Credits |

## Information Circulars

| | |
|---|---|
| 82-6 | Requesting Clearance Certificates for Estates and Trusts |
| 86-6 | Basic Herds |

## Common questions

Q. What return must be completed and filed for a deceased person: T1 General, T1 Special or T3?

A. You must complete a T1 General or a T1 Special return for the period from January 1 to the date of death. You must prepare a T3 return if the trust, established as a result of the taxpayer's death, receives income.

Q. My father died in February. Must I wait until the current year's return is published before completing his return for the two months?

A. No. You can simply use the most recent T1 return and change the year at the top right hand corner of the first page of the return. Any change(s) in the Act will be taken into consideration during the assessment of the return.

Q. Who must report the vacation pay and payment of accumulated sick leave?

A. Vacation pay is taxable income for the deceased person. The payment of accumulated sick leave is usually taxable income of the person who receives it (i.e., the estate or beneficiaries). However, accumulated sick leave paid following the death of an employee may, in certain circumstances, be considered a death benefit. Refer to the *1990 General Tax Guide*, line 130(D).

Q. Who must report death benefits paid by an employer?

A. Death benefits are taxable income of the person who receives them (i.e., the estate or beneficiaries). However, up to $10,000 of the benefits may be excluded from income.

Q. How are capital gains and recovery of the capital cost allowance calculated?

A. Capital property is generally considered to have been disposed of at death. A capital gain or recovery of the capital cost allowance, if any, is calculated as of the day of death. Refer to Chapter 3 for an explanation of certain rules that apply to deemed dispositions.

Q. How are personal tax credits determined for the year of death if the spouse and children received income before and after the taxpayer's death?

A. It is necessary to include income received during the entire calendar year by the person for whom the personal tax credit is claimed, whether this be the spouse, dependent children or other dependants.

Q. The death benefit for a deceased person, issued by Canada or Quebec Pension Plan is shown on information slip T4A(P). On what return for the year of death should this amount be reported?

A. The Canada and Quebec Pension Plan death benefit shown in Box (G) or Box 18 of a T4A(P) slip should be reported on the income tax return of the recipient. This could be the T3 return for the estate, or the T1 return of the beneficiary. It should not be reported on a T1 return for the deceased. This amount is not eligible for the $10,000 death benefit exemption. All other amounts are to be reported on a T1 return for the deceased.

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**AREA FOR YOUR NOTES AND CALCULATIONS**

## AREA FOR YOUR NOTES AND CALCULATIONS

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## Improving the Guide

This Guide is reviewed each year. If you have any comments or suggestions to improve the explanations in this Guide, we would like to hear from you.

Please send your comments to:

Tax Forms Directorate,
875 Heron Road,
Ottawa, Ontario
K1A 0L8

Throughout this Guide, we refer to forms that you must attach to your return. We also mention publications that cover certain topics in more detail. If you need any of these forms or publications, complete the order form below.

You can order this material from your district taxation office by mail, by telephone, or in person. Please see the 1990 *General Tax Guide* for the address and telephone number of your district office. If you mail the order form, allow three weeks for delivery.

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**ORDER FORM**

Please check ( √ ) the boxes below or list the titles or numbers of the publications required in the spaces provided. Print your name and address at the bottom of the form and submit it to your district office.

| NAMES OF REQUESTED GUIDES OR PAMPHLETS | |
|---|---|
| ☐ Business and Professional Income Tax Guide | ☐ Northern Residents Deductions Tax Guide |
| ☐ Capital Gains Tax Guide | ☐ Pension and RRSP Tax Guide |
| ☐ Child Care Expenses Tax Guide | ☐ Rental Income Tax Guide |
| ☐ Deceased Persons Income Tax Guide | ☐ Tax Guide for Emigrants |
| ☐ Employment Expenses Tax Guide | ☐ Tax Guide for New Canadians |
| ☐ Farming Income Tax Guide | ☐ T3 Guide and Trust Return |
| ☐ Fishing Income Tax Guide | |
| **Other Guides or Publications** | |
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