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Canada

Preparing Returns for Deceased Persons

96

Before you start

Is this guide for you?

Use this guide if you are the legal representative (see information on page 4) who has to file an income tax return for a deceased person.

Which return should you use?

You can use a *General Income Tax Return*. However, the deceased may have received a different income tax return in the mail based on his or her situation last year. If the return covers the types of income you want to report and the deductions and credits you want to claim, you can use it instead of a *General Income Tax Return*. You cannot use a T1S-C income tax and benefit return to complete a return for a deceased person.

Where can you get the forms you need?

You can get a General income tax package from your Revenue Canada tax services office. You can find the addresses and telephone numbers under "Revenue Canada" in the Government of Canada section of your telephone book.

> **Note**
> If you cannot get a return for the year of death, use a blank one from a previous year. In the top right corner of page 1, indicate the year for which you are filing. We will assess the return based on the legislation in effect for the year of death.

What if you need help?

In this guide, we have used plain language to explain the most common income tax situations. If you need more help after reading this guide, or if you want any of our publications, please contact us.

We have other income tax guides and pamphlets that you may find helpful, and which include some of the related forms you may need.

If we have a guide or pamphlet on a particular topic, we mention it under the information for that topic. We also refer to interpretation bulletins and information circulars that give more details on specific tax topics.

If you have access to the Internet, many of our publications are now on line. Our Internet address is:

http://www.rc.gc.ca/

Do you need information from the deceased person's tax records?

You can call or write us for the information we have in the deceased's tax records. When you write for such information, place the words "The Estate of the Late" in front of the deceased person's name. Include your address so we can reply directly to you. Before we can give you information from the deceased's records, we need the following:

- a copy of the deceased's death certificate;
- the deceased's social insurance number; and
- a copy of the will or other document that shows you are the legal representative. If you visit us to get information from the income tax records of the deceased, you also have to show us one piece of identification with your picture and signature on it, or two pieces with your signature on them.

What's new for 1996?

The proposed changes we list below for 1996 were not law at the time of printing. Once they become law, they will be effective for 1996 and later years. We have outlined the areas in red throughout this guide.

> **Employment Insurance** – In this guide, we refer to the new "Employment Insurance" (EI) program. These references also include the previous program, called "Unemployment Insurance" (UI).
>
> **Charitable donations** – For deceased individuals, the maximum claim for both the year of death and the year before death has been increased to 100% of net income.

Visually impaired persons can get information on services available to them, and can order publications in braille or large print, or on audio cassette or computer diskette, by calling 1-800-267-1267 weekdays between 8:15 a.m. and 5:00 p.m. (Eastern Time).

La version française de cette publication est intitulée *Déclarations de revenus de personnes décédées*.

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Legal representative

Are you the legal representative?

If you are an executor, an administrator, or a liquidator, you can be the legal representative of a deceased person.

Executor – This is someone a will names to act as the legal representative to handle a deceased person's estate.

Administrator – There may not be a will, or the will may not name an executor. In this case, a court will appoint an administrator to handle the deceased's estate. An administrator is often the spouse or the next of kin.

Liquidator – In Quebec, the liquidator is responsible for liquidating all estates established after December 31, 1993. For estates with a will, the liquidator's role is similar to that of an executor. For estates without a will, the liquidator acts as the administrator of the estate.

What are your responsibilities as the legal representative?

This guide deals only with your responsibilities under the *Income Tax Act*. Under the Act, it is your responsibility to file all required returns, make sure all taxes owing are paid, and to let the beneficiaries know which of the amounts they receive from the estate are taxable.

As the legal representative, you are responsible for filing a return for the deceased for the year of death. This return is called the final return. See Chapter 1 for details.

In addition, you also have to file any returns for previous years that the deceased person did not file. If the person did not leave records about these returns, or if you cannot tell from existing records whether or not the returns were filed, contact us. If you have to file a return for a year before the year of death, use a *General Income Tax Return*.

You may also have to file a Form T3, *Trust Income Tax and Information Return*, for income the estate earned after the date of death. For details, see the *T3 Guide and Trust Return*.

Clearance certificate

As the legal representative, you may want to get a clearance certificate. If you do not get a certificate, you can be liable for any amount the deceased owes.

We cannot give you a clearance certificate until you file all the required income tax returns and you receive the *Notice of Assessment* for each of them. Also, you will have to pay or secure all amounts owing.

Use Form TX19, *Asking for a Clearance Certificate*, to ask for a certificate. You can get Form TX19 from us. Once you complete the form, send it to us. Do not include Form TX19 with a tax return.

A certificate covers all tax years to the date of death. It is not a clearance for any amounts a trust owes.

If you need more details about clearance certificates, contact your tax services office. You can also get Information Circular 82–6R, *Clearance Certificate*.

Common questions and answers

Here are some common questions and answers you may want to look at before you read this guide.

Q. Can I deduct funeral expenses?

A. No. These expenses are not deductible.

Q. Who reports a death benefit that an employer pays?

A. A death benefit is income of the estate or beneficiary that receives it. Up to $10,000 of the total of all death benefits paid is not taxable. For details, see line 130 in the *General Income Tax Guide*.

Q. Who reports amounts an employer pays for vacation and unused sick leave?

A. Vacation pay is income of the deceased person. Payment for unused sick leave is often income of the estate or beneficiary that receives it. In some cases, sick leave payments can be a death benefit. For details, see line 130 in the *General Income Tax Guide*.

Q. On what return do I report Canada Pension Plan or Quebec Pension Plan benefits for the deceased?

A. A Canada Pension Plan or Quebec Pension Plan (CPP or QPP) death benefit shown in box 18 of Form T4A(P), *Statement of Canada Pension Plan Benefits*, has to be reported on the tax return of the beneficiary or trust that receives it. Do not report the amount on the deceased's return. This benefit is not eligible for the $10,000 death benefit exemption. It is not like a death benefit that an employer pays. You have to report all other CPP or QPP benefits on the deceased's return.

Q. If the deceased person was paying tax by instalments, do I have to continue making those instalment payments?

A. No. The only instalment payments we require are those that were due before the date of death.

Chapter 1 – Final return

This chapter explains the requirements for filing the final return, as well as how to complete it. We define some of the terms we use in this chapter on page 18.

On the final return, report all of the deceased's income from January 1 of the year of death, up to and including the date of death. Report income earned after the date of death on Form T3, *Trust Income Tax and Information Return*. For details, see the *T3 Guide and Trust Return*.

Tax tip
In addition to the final return, you can choose to file up to three optional returns for the year of death. Information about the deceased's income sources will help you determine if you can file any of these optional returns.

You do not have to file any of the optional returns. However, by choosing to file one or more of the returns, you may reduce or eliminate tax that you would otherwise have to pay for the deceased.

You do not report the same income on both the final and an optional return. However, you can claim certain credits and deductions on more than one return. In this regard, there may be a tax advantage if you file one or more of the optional returns in addition to the final return.

For more details, see "Chapter 2 – Optional returns" on page 10.

What date is the final return due?

Generally, the final return is due on or before the following due dates:

Period when death occurred	Due date for the return
January 1 to October 31	April 30 of the following year
November 1 to December 31	Six months after the date of death

If the deceased or the deceased's spouse was carrying on a business in 1996 (unless the expenditures of the business are primarily in connection with a tax shelter), the following due dates apply:

Period when death occurred	Due date for the return
January 1 to December 15	June 15 of the following year
December 16 to December 31	Six months after the date of death

Tax tip
If a person dies after December 31, 1996, but before the filing due date for his or her return, and he or she had not filed a return for 1996, the due date for the return is six months after the date of death.

The deceased's will or a court order may set up a **spousal trust**. When certain debts of the deceased or the estate are being handled through a spousal trust, the due date for the final return is extended to 18 months after the date of death. However, any taxes owing have to be paid by the due date shown in the section called "What is the due date for a balance owing" on this page. For more details, get the *T3 Guide and Trust Return* and Interpretation Bulletin IT-207, *"Tainted" Spouse Trusts.*

What happens if you file the return late?

If you file the return late and there is a balance owing, we will charge a late-filing penalty. The penalty is 5% of any balance owing, plus 1% of the balance owing for each full month that the return is late, to a maximum of 12 months. The late-filing penalty could be higher if we charged a late-filing penalty on a return for any of the three previous years. Even if you cannot pay the full amount owing by the due date, you can avoid this penalty by filing the return on time.

We may waive this penalty and interest if you file the return late because of circumstances beyond your control. If this happens, include a letter with the return giving the reasons why you filed the return late. Information Circular 92-2, *Guidelines for the Cancellation and Waiver of Interest and Penalties,* gives more details.

What is the due date for a balance owing?

The due date for a balance owing on a final return depends on the date of death:

Period when death occurred	Due date for the amount owing
January 1 to October 31	April 30 of the following year
November 1 to December 31	Six months after the date of death

If you do not pay the amount in full, we will charge interest on the unpaid amount from the due date to the date you pay the amount owing.

> **Note**
> In some cases, you can delay paying part of the amount due. For instance, you can delay paying part of the amount owing from rights or things (see page 11), and the deemed disposition of capital property (see page 13).
>
> If you want to delay payment, you will have to give us security in place of the amount owing. For more details, contact the Revenue Collections Division of your tax services office.
>
> You also have to complete Form T2075, *Election to Defer Payment of Income Tax, under Subsection 159(5) of the Income Tax Act by a Deceased Taxpayer's Legal Representative or Trustee.* You can get this form from us.

How to complete the final return

In this section, we briefly cover the most common lines on a return that apply to a deceased person. For details on these and other lines on a return, see the guide that came with the income tax return. Remember, if the types of income you want to report, or the deductions or credits you want to claim are not on the income tax return that you have, get a General income tax package.

Step 1 – Identification

In this area of the return:

- write "The Estate of the Late" before the name of the deceased;
- give your address as the return address;

- ensure the province or territory of residence on December 31 is the one where the deceased was living when he or she died; and
- enter the date of death on the proper line.

If you use a return with a label on it, make sure the information on the label is correct.

Step 2 – Goods and services tax (GST) credit

Since there is no GST credit for the year of death, do not complete the GST credit area when you file the final return.

It is possible that the deceased was receiving GST credit payments, based on his or her claim from the previous year. If this is the case, read the following paragraphs to find out what to do.

We may send out GST credit payments after a person dies because we do not know about his or her death. If this happens, you have to return the payments to us. Also, please give us the date of death so we can update our records.

Persons receiving the GST credit for self and for spouse

A person may die after claiming the GST credit for himself or herself, and for a spouse. If this happens, the spouse can contact us and ask to receive the rest of the payments. If the spouse did not file a return for the previous year, he or she has to do so before requesting the remaining payments.

Persons receiving the GST credit for self but not for spouse

A person's claim for the GST credit may not have included his or her spouse, or the person may not have had a spouse. In either case, if a person dies before we send out a GST credit payment, no one else can receive the payment. We cannot make any more payments in that person's name, or to the estate.

If a person dies during or after a month in which we send out a payment, return the cheque to us. We will then send the payment to the person's estate.

Step 3 – Total income

To complete the income part of the return, you need to determine the deceased person's income from all sources. The person's return for the previous year may help you.

Also, find out what amounts may be owing to the estate of the deceased because of his or her death. You will get this information from payers. Payers include employers, banks, trust companies, stock brokers, and pension plan managers. A safety deposit box may contain details about sources of income and benefits.

When you file a return, you may need to contact payers to get information slips. For example, from an employer you would get a T4, *Statement of Remuneration Paid*, and from a bank or trust company you would get a T5, *Statement of Investment Income*. The payer will know which information slip to issue.

Even if you cannot get any slips, you have to report all income. You can claim any related deductions. If a slip is not available, ask the payer to give you a note that states the income and deductions. Attach this note to the return. If you cannot get a note from the payer, estimate the income and deduction amounts. Then, attach a note to the return giving the amounts and the payer's name and address.

Report amounts that are paid regularly, even if the person did not receive them before he or she died. Some examples of these amounts are salary, interest, rent, royalties, and most annuities. These amounts normally accrue in equal daily amounts for the time they are payable.

There are two types of amounts that do not accrue in equal daily amounts:

- amounts receivable by the deceased, but not payable to the deceased on or before the date of death; and
- amounts from some annuity contracts that the *Income Tax Act* considers to have been disposed of on death.

For more details about amounts receivable on or before the date of death, see the section called "Return for rights or things" on page 11. You can also read Interpretation Bulletin IT–210, *Income of Deceased Persons – Periodic Payments.*

Amounts an employer pays to the deceased person's estate

There may be amounts that an employer will pay to a deceased employee's estate. For these amounts, an employer will usually complete a T4 or T4A slip.

Some of the amounts an employer pays will be part of the deceased's employment income for the year of death. Report these amounts on the final return. The amounts are employment income even if they are received in a year after the year of death. Box 14 of the T4 slip should include the following amounts:

- salary or wages (including overtime) from the end of the last pay period to the date of death;
- salary or wages (including overtime) for a pay period finished before the date of death, but paid after death; and
- payment for vacation leave earned but not taken.

The employer may change any of these amounts later because of an agreement or promotion. If the document that allows the change was signed **before** the date of death, report these additional amounts on the final return. However, if the document was signed **after** the date of death, the additional amounts are not taxable.

Some amounts may be **rights or things**, and you may be able to report them on an optional return. See the section called "Return for rights or things" on page 11 for details.

Some of the amounts an employer pays are income for the estate. Do not report these amounts on the final return. Instead, report them on Form T3, *Trust Income Tax and Information Return*. Look for estate income amounts in boxes 18 or 28 of the T4A slip. These amounts include:

- salary or wages, and any adjustments the employer pays *for the period after the date of death;*
- a payment for the full month in which the employee died, if he or she was not getting paid but was on authorized leave;

- severance pay received because of the death (since this is a death benefit, an amount up to $10,000 may be tax-free);
- future changes to severance pay, no matter when the collective agreement was signed;
- a refund of pension contributions payable because of the death;
- a guaranteed minimum pension payment that is not a death benefit; and
- a payment from a deferred profit-sharing plan.

Lines 101 to 104 – Employment income

Report all salary or wages received from January 1 to the date of death. Also include amounts that accrue from the start of the pay period in which the employee died to the date of death.

Lines 113 to 115 – Pension income

Report all pension income received from January 1 to the date of death. Do not include on line 113, the "Net federal supplements paid" from box 21 of the T4A(OAS) slip. Report this amount on "Line 146 – Net federal supplements." You may be able to claim a deduction for this amount on "Line 250 – Other payments deduction."

If the deceased person received annuity payments from a registered retirement income fund (RRIF) for the period from January 1 to the date of death, report that income on the final return. If the deceased was 65 or older, report the RRIF income on line 115. Also report the RRIF income on line 115 if the deceased was under 65 but received the RRIF payments because his or her spouse died. In all other cases, report the RRIF income on line 130 of the return. For more information, see the section called "Registered retirement income fund (RRIF) income" on page 8 of this guide.

When a person dies, a pension plan or fund may pay a lump sum to the spouse, a child, or the estate. An example of a lump sum is the death benefit from the Canada Pension Plan or Quebec Pension Plan. A lump sum is usually income of whoever receives it.

For more details on how to report lump-sum payments, see lines 114 and 130 in the guide that came with the income tax return. You may also want to read Interpretation Bulletins IT–301, *Death Benefits – Qualifying Payments*, and IT–508, *Death Benefits – Calculation.*

> **Note**
> If the deceased received Old Age Security pension or net federal supplements and the deceased's net income before adjustments (line 234) is more than $53,215, all or part of these benefits may have to be repaid. For details, see line 235 in the *General Income Tax Guide*. If you are using a *Special Income Tax Guide*, you can also find details at line 235 in that guide.

Line 119 – Employment Insurance (EI) benefits

Report any EI benefits the deceased received before death. If the deceased received EI benefits in 1996 and the deceased's net income before adjustments (line 234) is more than $48,750, part of these benefits may have to be repaid. For details, see line 235 in the *General Income Tax Guide.* If you are using a *Special Income Tax Guide*, you can also find details at line 235 in that guide.

Lines 120 and 121 – Investment income

Report investment income received from January 1 to the date of death. This type of income includes dividends and interest. Also include the following:

- amounts earned from January 1 to the date of death that have not been paid;
- bond interest earned from the last time it was paid to the date of death, if the deceased did not report it in a previous year; and
- compound bond interest accrued to the date of death, if the deceased did not report it in a previous year.

You can report some types of investment income as rights or things. See the section called "Return for rights or things" on page 11 for details.

Line 127 – Taxable capital gains

See Chapter 3 for details about this type of income.

Line 129 – Registered retirement savings plan (RRSP) income

When a person dies, he or she may have an RRSP. At the time of death, the RRSP may or may not have matured. Depending on the situation, the amount you include in the deceased's income can vary.

A **matured RRSP** is one that is paying retirement income. It usually pays monthly annuity payments.

For a matured RRSP, report on line 129, the RRSP payments the annuitant received from January 1 to the date of death. If, because of the annuitant's death, his or her surviving spouse begins receiving the remaining annuity payments from the plan, the surviving spouse has to report the remaining payments as income.

The spouse may be a beneficiary of the estate instead of a beneficiary of the deceased's RRSP. If this is the case, you and the spouse can jointly elect, by telling us in writing, to treat the amounts paid from the RRSP to the estate as being paid from the RRSP to the spouse. A copy of the written election has to be attached to the return of the surviving spouse. The election has to specify that the surviving spouse is becoming the annuitant of the RRSP.

If the amounts from the RRSP are paid to a beneficiary other than the deceased's spouse, see the income tax guide called *RRSPs and Other Registered Plans for Retirement* for more information.

An **unmatured RRSP** is one that does not yet pay retirement income.

We consider a deceased RRSP annuitant to have received, immediately before death, an amount equal to the fair market value (FMV) of all the property of the unmatured plan at the time of death. The FMV of the property is shown in box 34 of the T4RSP slip issued in the deceased person's name. You have to include this amount in the deceased's income for the year of death.

If all of the property held in the RRSP is paid (as specified in the RRSP contract) to the surviving spouse, **and** that payment is transferred to the surviving spouse's RRIF, RRSP, or to an issuer to buy an eligible annuity for the surviving spouse, a T4RSP slip will not be issued in the deceased's name. In this case, the surviving spouse has to report the payment as income and is eligible to claim a deduction equal to the amount transferred.

If a T4RSP slip showing the FMV of the plan at the time of death is issued in the name of the deceased, you may be able to reduce the amount you include in the deceased's income. For details, see Form T2019, *Death of an RRSP Annuitant – Refund of Premiums*, and the income tax guide called *RRSPs and Other Registered Plans for Retirement.*

Home Buyers' Plan
The deceased may have participated in the Home Buyers' Plan. If so, the deceased would have made a withdrawal from his or her RRSP and may have been making repayments to the RRSP. In this case, include on line 129, the total of all amounts that remain to be repaid at the time of death.

However, you do not have to report these amounts when you and the surviving spouse jointly elect to have the surviving spouse continue to make the repayments. For more information, see the pamphlet called *Home Buyers' Plan (HBP) – For 1997 Participants.*

Lines 130 to 146 – Other types of income

Use these lines to report other types of income. Remember, if the income tax package you have does not cover the types of income you want to report, you can get a General income tax package from us.

Registered retirement income fund (RRIF) income
When a person dies, he or she may have a RRIF. Depending on the situation, the amount you include in the deceased's income can vary.

If the deceased received annuity payments from a RRIF for the period from January 1 to the date of death, see "Lines 113 to 115 – Pension income" on page 7.

If the annuitant elected to have the RRIF payments continue to his or her spouse after death, the surviving spouse has to report the remaining payments as income.

If the annuitant did not elect to have the RRIF payments continue to his or her spouse, the spouse can still become the annuitant of the RRIF after the annuitant's death. This is the case if the legal representative consents to the deceased's spouse becoming the annuitant, and the RRIF carrier agrees to continue the payments to the surviving spouse.

If the payments do not continue to the spouse, we consider a RRIF annuitant to have received, immediately before death, an amount equal to the fair market value (FMV) of the plan at the time of death. The FMV of the property is shown in box 18 of the T4RIF slip issued in the deceased person's name. You have to include this amount in the deceased's income for the year of death. However, you may be able to reduce the amount you include in income. For details, see Form T1090, *Death of a RRIF Annuitant – Designated Benefit*, and the income tax guide called *RRSPs and Other Registered Plans for Retirement.*

If all of the property held by the RRIF is paid (as specified in the RRIF contract) to the surviving spouse, and that payment is transferred to the surviving spouse's RRIF, RRSP, or to an issuer to buy an eligible annuity for the surviving spouse, a T4RIF slip will not be issued in the deceased person's name. In this case, the surviving spouse has to report the payment as income and may be eligible to claim a deduction equal to the amount transferred.

Reserves in the year of death
Sometimes, when a person sells property, some of the proceeds are not payable until after the year he or she sells it. Similarly, if a person is self-employed, he or she may have amounts that will be received in a later year for work done this year. An example would be for work in progress.

Usually, a person can deduct from income the part of the proceeds that are not payable until a later year. This is called a reserve.

In most cases, you cannot deduct a reserve in the year of death. However, there may be a transfer, to a spouse or spousal trust, of the right to receive the proceeds of disposition or the income owing. When this happens, the legal representative and the beneficiary can choose to claim a reserve on the deceased's return. To do this, complete Form T2069, *Election in Respect of Amounts Not Deductible as Reserves for the Year of Death*, and attach a copy to the deceased's return.

This choice will be available only if the deceased was resident in Canada right before death. In the case of a transfer to a spouse, the spouse also has to have been resident in Canada right before the deceased's death. In the case of a transfer to a spousal trust, the trust has to be resident in Canada right after the proceeds or income become locked in for the trust. For the meaning of **locked in**, see page 19.

The spouse or spousal trust includes in income an amount equal to the reserve that is on Form T2069. The spouse or spousal trust has to include this income on the return for the first tax year after death. You have to attach a copy of Form T2069 to that return.

Step 4 – Taxable income

Line 208 – Registered retirement savings plan (RRSP) contributions

Use this line to deduct RRSP contributions the deceased made before his or her death. These include contributions to both the deceased's RRSPs and those of the deceased's spouse. After a person dies, no one can contribute to the deceased's RRSPs.

You can also deduct amounts you contribute after the date of death for the deceased to an RRSP of the deceased's spouse. You have up to 60 days after the end of the year in which the death occurred to contribute these amounts.

The amount you can deduct on the deceased's return for 1996 is usually based on the deceased's 1996 RRSP deduction limit. You can also deduct amounts for contributions the deceased made for certain income the deceased received and transferred to an RRSP.

For more information, see the income tax guide called *RRSPs and Other Registered Plans for Retirement.*

Line 237 – Accumulated forward-averaging amount withdrawal

There may be an accumulated forward-averaging amount. As the legal representative, you have three choices:

- You can ignore the amount. If you do this, there will be no tax effect on the deceased's income.
- For the year of death, you can include all or part of the amount as income. When you do this, we may tax the amount at a lower rate. To make this choice, complete Form T581, *Forward Averaging Tax Credits*. If you include only part of the amount, there is no tax effect on the part you did not include.
- You can ask for a three-year carryback of the part you did not include as income in the second choice. To do this, complete Form T541, *Forward Averaging Tax Calculation – Deceased Individuals*.

You can get Forms T581 and T541 from us. Send us the completed forms on or before the due date for the final return.

Line 253 – Net capital losses of other years

See Chapter 4 for details about these losses.

Step 5 – Non-refundable tax credits

Personal amounts

If the deceased lived in Canada from January 1 to the date of death, claim the full personal amounts. Do not prorate the personal amounts.

If the deceased lived outside Canada for part of the time between January 1 and the date of death, you may have to prorate the personal amounts. If the deceased immigrated to Canada in the year of death, see the income tax pamphlet called *Newcomers to Canada*. If the deceased emigrated from Canada in the year of death, see the income tax pamphlet called *Emigrants and Income Tax*.

Line 300 – Basic personal amount

Claim the full basic personal amount for the year.

Line 301 – Age amount

If the deceased was 65 or older on the date of death, and the deceased's net income is less than $49,134, you may be able to claim a full or partial age amount. The amount you can claim will depend on the deceased's net income for the year.

Line 303 – Spousal amount

Depending on the spouse's net income for the year, you may be able to claim a full or partial spousal amount. Use the spouse's net income for the whole year, not just up to the deceased's date of death.

Line 305 – Equivalent-to-spouse amount

If the deceased is entitled to claim the equivalent-to-spouse amount, use the dependant's net income for the whole year, not just up to the deceased's date of death.

Line 306 – Amounts for infirm dependants age 18 or older

If the deceased is entitled to claim an amount for an infirm dependant who is 18 or older, use the dependant's net income for the whole year, not just up to the deceased's date of death.

Line 314 – Pension income amount

The deceased may have received eligible pension income before the date of death. If this is the case, you may be able to claim the pension income amount of up to $1,000.

Line 316 – Disability amount

You can claim a disability amount if **both** of these conditions are met:

- The deceased had a severe mental or physical impairment in the year. A severe impairment is one that markedly restricts the basic activities of daily living. It has to last, or be expected to last, for a continuous period of at least 12 months.
- The deceased or someone else has not claimed medical expenses for a full-time attendant that are more than $10,000, or for full-time care in a nursing home because of the impairment.

In some cases, you can claim both the disability amount **and** either expenses for attendant care that allowed the deceased to earn income (line 215), or expenses for full-time or part-time attendant care provided in Canada that are not more than $10,000 as a medical expense (line 330).

For more details on the disability credit, see the pamphlet called *Tax Information for People with Disabilities*, and Interpretation Bulletin IT–519, *Medical Expense and Disability Tax Credits and Attendant Care Expense Deduction.*

Line 318 – Disability amount transferred from a dependant other than your spouse

If the deceased had a dependant who is entitled to claim a disability amount, you may be able to claim all or a part of the dependant's disability amount.

Line 326 – Amounts transferred from your spouse

Sometimes there are amounts that a spouse does not need to reduce his or her tax to zero. In these situations, you can transfer the unneeded amounts to the deceased's final return.

Also, the deceased may have amounts that are not needed to reduce his or her tax to zero. If this is the case, you can transfer the unneeded amounts to the spouse's return. However, before you can do this, you have to reduce the tax to zero on the final return you file for the deceased.

For either situation, you can transfer the following amounts:

- age amount (line 301) if the spouse was 65 or older;
- pension income amount (line 314);
- disability amount (line 316); and
- tuition fees (line 320) and education amount (line 322).

Line 330 – Medical expenses

You can claim medical expenses that are more than the **lower** of:

- $1,614; or
- 3% of the deceased's total net income from line 236 of all returns for the year of death.

The expenses can be for any 24-month period that includes the date of death, as long as no one has claimed them on any other return.

Attach the receipts for medical expenses to the return. For more details on medical expenses, see line 330 in the *General* or *Special Income Tax Guide*. If you are using a *T1S-A Income Tax Guide*, you can also find details at line 330 in that guide.

Line 340 – Charitable donations

Use this line to claim charitable donations the deceased made before the date of death. Support these claims with official receipts that the registered charity or other qualified donee has issued.

In addition, you can claim charitable donations made through the will, as long as you support the donations. The type of support you have to provide depends on when the registered charity or other qualified donee will receive the gift:

- For gifts that will be received right away, provide an official receipt.
- For gifts that will be received at some later time, provide a copy of each of the following:
  - the will;
  - a letter on behalf of the estate to the charitable organization that will receive the gift, advising of the gift and its value; and
  - a letter from the charitable organization acknowledging the gift and stating that it will accept the gift.

The deceased may have donated amounts in the five years before the year of death. As long as the deceased did not claim the amounts before, you can claim them in the year of death. Attach a note to the return to tell us about the amounts and the year or years the deceased made the donations.

The most you can claim on line 340 of the final return is the **lower** of:

- amounts donated in the year of death (including gifts by will), plus any amounts donated in the five years before the year of death, if the deceased did not claim them before; or
- under proposed changes, 100% of the deceased's net income (line 236) on the final return.

On the return(s) for the year of death, you may not be able to claim all of the gifts the deceased gave in the year of death. In that case, you can ask us to adjust the deceased's return for the preceding year to include the unused part of these gifts.

Sometimes, a gift can be capital property. At the time the deceased gives the property, its fair market value may be more than its adjusted cost base. We define fair market value and adjusted cost base on page 19.

When the fair market value is more than the adjusted cost base, you can choose, as the amount of the gift, an amount that is not more than the fair market value but not less than its adjusted cost base. The amount you choose is the deceased's proceeds of disposition for the gift. Use this amount to determine the credit for the gift. Note that this may result in a capital gain.

For more information about charitable donations, see the pamphlet called *Gifts and Income Tax.*

If the gift is a gift to Canada, a province, or a territory, or a gift to a designated institution of property certified by the Canadian Cultural Property Export Review Board, see line 342 in the *General Income Tax Guide* and the pamphlet called *Gifts and Income Tax.*

Step 6 – Refund or balance owing

You will find the details you need about tax and credits in the section called "Refund or balance owing" in the guide that came with the income tax return.

Minimum tax does not apply to a person for the year of death. However, the deceased may have paid this tax in one or more of the seven years before the year of death. If this is the case, you may be able to deduct from the tax owing for the year of death, part or all of the minimum tax the deceased paid in those years. To do this, complete Part VIII of Form T691, *Calculation of Minimum Tax.* Include Form T691 with the return.

Provincial and territorial tax credits

Both territories and some provinces have tax credits that are available through the federal tax system. See the provincial or territorial forms in the income tax package you are using.

Chapter 2 – Optional returns

Optional returns are returns on which you report some of the income that you would otherwise report on the final return. By filing one or more of the optional returns, you may reduce or eliminate tax that you would otherwise have to pay for the deceased. This is possible because you can claim certain amounts more than once, split them between returns, or claim them against specific kinds of income.

You can choose to file up to three optional returns (also known as "elective" returns). The optional returns are for income from:

- rights or things;
- *activity as a partner or proprietor;* or
- a testamentary trust.

Note
Do not confuse the optional return for income from a testamentary trust with Form T3, *Trust Income Tax and Information Return*. After someone dies, a will may create a trust. You report income earned after the date of death on a T3 form. For more information, see the *T3 Guide and Trust Return*.

What are the three optional returns?

1. Return for rights or things

Rights or things are amounts that were not paid at the time of death and that, had the person not died, would have been included in his or her income when received. There are rights or things from employment and other sources.

You can file a return for rights or things to report the value of the rights or things at the time of death. However, if you file a return for rights or things, you have to report **all** rights or things on that return, except those transferred to beneficiaries. You **cannot** split rights or things between the final return and the rights or things return.

If you **transfer** rights or things to a beneficiary, you have to do so within the time limit for filing a return for rights or things. Report the income from the transferred rights or things on the beneficiary's return. Do not include the income from the rights or things on the deceased's return.

Employment rights or things

Employment rights or things are salary, commissions, and vacation pay, as long as **both** of these conditions are met:

- the employer owed them to the deceased on the date of death; and
- they are for a pay period that ended before the date of death.

Other rights or things

Other rights or things include the following:

- uncashed matured bond coupons;
- bond interest earned to a payment date before death, but not paid and not reported in previous years;
- unpaid dividends declared before the day the person died;
- supplies on hand, inventory, and accounts receivable if the deceased's business used the cash method;
- harvested farm crops; and
- livestock that is not part of the basic herd.

For more details about rights or things, see Interpretation Bulletins IT-212, *Income of Deceased Persons – Rights or Things*, and its Special Release, IT-234, *Income of Deceased Persons – Farm Crops*, and IT-427, *Livestock of Farmers*.

Some items that are **not** rights or things include:

- amounts that accrue periodically, such as interest from a bank account;
- bond interest accrued between the last interest payment date before the person died and the date of death;
- eligible capital property and capital property;
- resource properties;
- land in the deceased's business inventory; and
- income from an income-averaging annuity contract.

How to file – If you decide to file a return for rights or things, you will need to:

- get a General return;
- write "70(2)" in the top right corner of page 1 of the return; and
- follow the instructions for completing a return in this guide and the guide that came with the income tax return.

You have to file this return and pay any amount owing by the later of:

- 90 days after we mail any *Notice of Assessment* or *Notice of Reassessment* for the final return; or
- one year after the date of death.

In some cases, you can delay paying part of the amount due. For instance, you can delay paying part of the amount owing from rights or things. Remember that we charge interest on any unpaid amount, from the due date to the date you pay the amount in full.

If you want to delay payment, you will have to give us security in place of the amount owing. You also have to complete Form T2075, *Election to Defer Payment of Income Tax, under Subsection 159(5) of the Income Tax Act by a Deceased Taxpayer's Legal Representative or Trustee*. For more details, contact the Revenue Collections Division of your tax services office.

How to cancel a return for rights or things – You may file a return for rights or things before the due date, but later want to cancel it. We will cancel the return if you send us a note asking us to do this. You have to send the note by the due date for the rights or things return.

2. Return for a partner or proprietor

A deceased person may have been a partner in, or the sole proprietor of a business. The business may have a fiscal year that does not begin or end on the same dates as the calendar year. If the person died after the business's fiscal period ended but before the end of the calendar year in which the fiscal period ended, you can file an optional return for the deceased.

On this return, report the income for the time from the end of the fiscal period to the date of death. If you choose not to file this optional return, report all income on the final return.

Example
A person who had a business died on May 28, 1996. The business has a March 31 fiscal year end. You have two choices when you report the person's 1996 income:

- One choice is to file only a final return. You would include on it the business income from April 1, 1995, to May 28, 1996.

- The other choice is to file a return for a partner or proprietor in addition to the final return. On the final return, include business income from April 1, 1995, to March 31, 1996. On the return for a partner or proprietor, report the business income from April 1, 1996, to May 28, 1996.

How to file – If you decide to file a return for a partner or proprietor, you will need to:

- get a General return;
- write "150(4)" in the top right corner of page 1 of the return; and
- follow the instructions for completing a return in this guide and the *General Income Tax Guide.*

You have to file this optional return and pay any amount owing, when the final return is due. See the sections called "What date is the final return due?" and "What is the due date for a balance owing?" on page 5.

3. Return for income from a testamentary trust

You can file an optional return for a deceased person who received income from a testamentary trust. This kind of trust is set up as a result of another person's death. The trust may have a fiscal period that does not begin or end on the same dates as the calendar year.

A person getting income from a testamentary trust may die after the trust's fiscal period ends. If this happens, you can file a return for the deceased's income from this trust for the time from the end of the trust's fiscal period to the date of death.

Example
A husband gets income from a testamentary trust. The trust was formed as a result of his wife's death. The fiscal year of the trust is from April 1 to March 31. The husband died on June 11, 1996. You have two choices when you report the husband's income from the trust:

- One choice is to include the trust income from April 1, 1995, to June 11, 1996, on the final return.
- The other choice is to file a return for income from the trust in addition to the final return. On the final return, include the trust income from April 1, 1995, to March 31, 1996. On the return for income from the trust, report the trust income from April 1, 1996, to June 11, 1996.

How to file – If you decide to file a return for income from a testamentary trust, you will need to:

- get a General return;
- write "104(23)(d)" in the top right corner of page 1 of the return; and
- follow the instructions for completing a return in this guide and the guide that came with the income tax return.

You have to file this optional return and pay any amount owing by the later of:

- April 30, 1997; or
- 6 months after the date of death.

Amounts for optional returns

There are three groups of amounts you can claim on the optional returns. They are amounts you can:

- claim in full on each return;
- split between returns; and
- claim only against certain income.

Amounts you can claim 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 spousal amount;
- the equivalent-to-spouse amount; and
- amounts for infirm dependants age 18 or older.

Amounts you can split between returns

There are certain amounts you cannot claim in full on the final return and optional returns. However, you can split these amounts between the returns.

When you split an amount, the total of the claims cannot be more than what would have been allowed if you were only filing the final return. Amounts you can split are:

- disability amount for the deceased;
- disability amount for a dependant other than a spouse;
- tuition fees and education amount for the deceased;
- tuition fees and education amount you transfer from a child;
- cultural, ecological, and government gifts;
- under proposed changes, charitable donations that are not more than 100% of the net income you report on that return; and
- medical expenses, which you can split any way you want between the final return and any optional returns. However, you have to reduce the total expenses by the lower of $1,614 or 3% of the total net income you report on all returns.

Example
In the year a woman died, her total medical expenses were $8,000. You decide to file a rights or things return in addition to the final return. The total of her net income on the two returns is $40,000. Of this, $30,000 is on the final return and $10,000 is on the rights or things return.

You calculate 3% of the total net income ($40,000) as $1,200. Because $1,200 is less than $1,614, you reduce the medical expenses claim by $1,200. You decide to split the expenses to claim $6,000 on the final return, and $2,000 on the rights or things return. Reduce these claims by $900 on the final return, and by $300 on the rights or things return. Therefore, the deductions for medical expenses are $5,100 ($6,000 – $900) on the final return, and $1,700 ($2,000 – $300) on the rights or things return.

Amounts you can claim only against certain income

There are some amounts you can only claim on those returns on which you report the related income. The amounts are:

- Canada Pension Plan or Quebec Pension Plan (CPP or QPP) contributions;
- Employment Insurance premiums;
- pension income amount;
- employee home relocation loan deduction;
- stock option and shares deduction;
- social benefits repayment; and
- vow of perpetual poverty deduction.

Example
Suppose the deceased person's total employment income in the year of death was $30,000, and the person's CPP amount was $800. Of the $30,000, $1,000 is a right or thing. Of the $800, $27 is the CPP contribution the person paid on the $1,000. You decide to file a return for rights or things.

On the final return, you report income of $29,000 and claim a CPP amount of $773. On the return for rights or things, you include income of $1,000 and claim a CPP amount of $27.

The amounts you **cannot** claim on an optional return include:

- amounts you transfer from a spouse;
- the capital gains deduction;
- child care expenses;
- losses from other years;
- the northern residents deductions;
- withdrawals from the accumulated-averaging amount; and
- refunds of investment tax credits.

You may be able to claim these amounts on the final return.

Chapter 3 – Deemed disposition of property

In this chapter, we discuss the tax treatment of capital property the deceased owned at the date of death. We deal with capital property in general, as well as the particular treatment of depreciable and farm property. We discuss only property acquired after December 31, 1971.

There are special rules for property that a deceased person owned before 1972. For details about these rules and for information about other property such as eligible capital property, resource property, or an inventory of land, contact us.

We define some of the terms we use in this chapter on page 18.

General information

When a person dies, we consider that he or she has disposed of all capital property right before death. We call this a **deemed disposition**.

Also, right before death, we consider the person to have received the **deemed proceeds of disposition**. Even though there was not an actual sale, there can be a capital gain or (except for depreciable property) a capital loss.

For depreciable property, in addition to a capital gain, there can also be a recapture of capital cost allowance. Also, for depreciable property, instead of a capital loss there may be a terminal loss.

What is a capital gain?

When the deemed proceeds of disposition of a capital property are more than its adjusted cost base, the result is a capital gain. Three-quarters of the capital gain is the taxable capital gain. Report the taxable capital gain on the final return. You may be able to claim a capital gains deduction.

What is a capital gains deduction?

This is a deduction you can claim for the deceased person against eligible taxable capital gains realized from the disposition and deemed disposition of capital property.

The $75,000 capital gains deduction is no longer available for dispositions or deemed dispositions of capital property after February 22, 1994. However, if the deceased owned capital property at the end of February 22, 1994, and has not used all of his or her $75,000 capital gains deduction, you may be able to file a special election for the deceased.

This election allows you to report a capital gain that accrued before February 23, 1994, on the deceased's 1994 income tax return and to claim a capital gains deduction, even though the deceased did not actually sell the property. In most cases, this election had to be filed by April 30, 1995. However, we will accept a late election up to April 30, 1997, if you estimate and pay a penalty when you file the election.

To find out more about the special election and how to calculate the penalty, see the *Capital Gains Election Package*. The package includes Form T664, *Election to Report a Capital Gain on Property Owned at the End of February 22, 1994*. Do not submit an amended 1994 income tax return. Instead, complete and submit Form T664 along with payment of the estimated penalty to the Enquiries and Adjustments Section at the tax centre where the deceased filed his or her return.

The $375,000 capital gains deduction for dispositions and deemed dispositions of qualified small business corporation shares and qualified farm property is still available. To find out what we consider to be qualified small business corporation shares and for details about the capital gains deduction, see the income tax guide called *Capital Gains*. We discuss the meaning of qualified farm property in the income tax guide called *Farming Income*.

What is a capital loss?

Except for depreciable property, when the deemed proceeds are less than the adjusted cost base of a capital property, the result is a capital loss. Three-quarters of the capital loss is the allowable capital loss. Report the allowable capital loss on the final return. You cannot have a capital loss on the disposition of depreciable property.

For more details on claiming a capital loss, see the section called "Net capital losses incurred in the year of death" on page 17.

Recaptures and terminal losses

For depreciable property, when the deemed proceeds are more than the undepreciated capital cost, you will usually have a **recapture of capital cost allowance**. Include the recapture in income on the final return.

For depreciable property, when the deemed proceeds are less than the undepreciated capital cost, the result is a **terminal loss**. Deduct the terminal loss on the final return.

For more details about a recapture of capital cost allowance or a terminal loss, see Interpretation Bulletin IT-478, *Capital Cost Allowance – Recapture and Terminal Loss.*

Capital property other than depreciable property

In this section, we explain how to determine the deemed proceeds for capital property, other than depreciable property and some transfers of farm property. If there is a transfer of depreciable property, read the section called "Depreciable property" on this page. If there is a transfer of farm property to a child, read the section called "Farm property transferred to a child" on page 15.

Deceased's deemed proceeds – Transfer to spouse or spousal trust

There may be a transfer of capital property (including farmland) to a spouse or a spousal trust.

For a transfer to a spouse, the deemed proceeds are the *same as the property's adjusted cost base right before* death, if **both** of these conditions are met:

- The spouse was a resident of Canada right before the person's death.
- The property becomes locked in for the spouse within 36 months of the date of death. If you need more time to meet this condition, you can make a written request to the Minister of National Revenue for an extension. For the definition of **locked in**, see page 19.

For a transfer to a spousal trust, the deemed proceeds are the same as the property's adjusted cost base right before death, if **both** of these conditions are met:

- The spousal trust is resident in Canada right after the property becomes locked in for the spousal trust.
- The property becomes locked in for the spousal trust within 36 months of the date of death. If you need more time to meet this condition, you can make a written request to the Minister of National Revenue for an extension.

In most cases, the deceased will not have a capital gain or loss. This is because the transfer defers any gain or loss to the date the beneficiary disposes of the property.

Example
Suppose the will transfers non-depreciable capital property to the spouse, and both of the conditions for transfer to a spouse are met. Right before death, the adjusted cost base of the property was $35,000. Therefore, the deemed proceeds are $35,000. You would not report any capital gain or loss on the deceased's final return.

Tax tip
You can choose not to have the deemed proceeds equal the adjusted cost base. If you make this choice, the deemed proceeds equal the property's fair market value right before death. You have to make this choice when you file the final return for the deceased.

You may want to do this to use a capital gains deduction (see page 13) or a net capital loss on the final return. It may be best to report a capital gain or loss on the final return instead of deferring it to the spouse or spousal trust.

Deceased's deemed proceeds – All other transfers

For all other transfers, the deemed proceeds are equal to the property's fair market value right before death.

Depreciable property

In this section, we explain how to determine the deemed proceeds for depreciable property, except for some transfers of farm property. If there is a transfer of farm property to a child, read the section called "Farm property transferred to a child" on page 15.

Deceased's deemed proceeds – Transfer to spouse or spousal trust

There may be a transfer of depreciable property (including depreciable farm property) to a spouse or a spousal trust. For such transfers, you may be able to use a special amount for the deemed proceeds. In most cases when you use this special amount, the deceased will not have a capital gain, recapture of capital cost allowance, or a terminal loss. When you do this, you defer any gain, recapture, or terminal loss to the beneficiary when the beneficiary disposes of the property.

In the case of a transfer to a spouse, **both** of these conditions have to be met:

- The spouse was a resident of Canada right before the person's death.
- The property becomes locked in for the spouse within 36 months of the date of death. If you need more time to

meet this condition, you can make a written request to the Minister of National Revenue for an extension.

In the case of a transfer to a spousal trust, **both** of these conditions have to be met:

- The spousal trust is resident in Canada right after the property becomes locked in for the spousal trust.
- The property becomes locked in for the spousal trust within 36 months of the date of death. If you need more time to meet this condition, you can make a written request to the Minister of National Revenue for an extension.

The special amount (deemed proceeds) is the **lower** of:

- the capital cost of the property for the deceased; or
- the result of the following calculation:

$$\frac{\text{Capital cost of the property}}{\text{Capital cost of all the property in the same class that had not been disposed of previously}} \times \text{Undepreciated capital cost of all of the deceased's property in the same class}$$

Example
A woman had two trucks that were used in her business. The woman died in July 1996, and the will transferred truck A to her husband. Both of the conditions stated above for transfer to a spouse are met. You have the following details:

Undepreciated capital cost of the two trucks right before death	$33,500
Capital cost of truck A	$22,500
Capital cost of the two trucks	$50,000

The woman's deemed proceeds on truck A are the lower of:

- $22,500; or
- $\frac{\$22{,}500}{\$50{,}000} \times \$33{,}500 = \$15{,}075.$

Her deemed proceeds are $15,075.

When there is more than one property in the same class, you can choose the order in which the deceased is deemed to have disposed of the properties. When you calculate the special amount, adjust the undepreciated capital cost and the total capital cost of the properties in the class to exclude previous deemed dispositions.

Note
When you determine the special amount, you will need to recalculate the capital cost of any property in the class when:

- the property was acquired at non-arm's length,
- the property was previously used for other than gaining or producing income; or
- the portion of a property used for gaining or producing income changed.

For more information, contact your tax services office.

Tax tip
You can choose not to use the special amount for the deemed proceeds. If you choose not to use the special amount, the deemed proceeds are equal to the property's fair market value right before death. You have to make this choice when you file the final return for the deceased.

You may want to make this choice to use the capital gains deduction, see page 13, on the final return. It may be best to report a capital gain, recapture, or terminal loss on the final return instead of deferring it to the spouse or spousal trust.

Deceased's deemed proceeds – All other transfers

For all other transfers, the deemed proceeds are equal to the property's fair market value right before death.

Farm property transferred to a child

In this section, we explain how to determine the deemed proceeds when there is a transfer of farm property to a child. For this kind of transfer, you may be able to use a special amount for the deemed proceeds.

In this chapter, when referring to the transfer of farm property, the terms **farm property** and **child** have the following meanings:

Farm property includes land or other depreciable property used for farming.

A **child** includes:

- the deceased's natural or adopted child;
- the deceased's spouse's child;
- the deceased's grandchild or great-grandchild;
- a person who, while under 19, was in the deceased's custody and control and was wholly dependent on the deceased for support; and
- the spouse of any of the above.

Conditions

To use the special amount for the deemed proceeds, all four of the following conditions have to be met:

- The farm property is in Canada.
- The deceased, the deceased's spouse, or any child of the deceased was using the farm property mainly for farming, on a regular and ongoing basis, before the deceased's death.
- The child was a resident of Canada right before the deceased's death.
- The farm property becomes locked in for the child within 36 months of the date of death. If you need more time to meet this condition, you can make a written request to the Minister of National Revenue for an extension.

You may also be able to use a special amount for the deemed proceeds when a share of the capital stock of a family farm corporation or an interest in a family farm partnership is transferred to a child. For details, see

Interpretation Bulletin IT-349, *Intergenerational Transfers of Farm Property on Death*, and its Special Release.

Deceased's deemed proceeds – Transfer of land

If all four of the above conditions are met, you can choose to have the deemed proceeds equal the adjusted cost base of the land right before death. Therefore, the deceased will not have a capital gain or loss.

Tax tip
You can choose not to have the deemed proceeds equal the adjusted cost base. You can transfer the land at any amount between its adjusted cost base and fair market value right before death. Make this choice when you file the final return for the deceased.

You may want to do this to use the capital gains deduction, see page 13, or to use a net capital loss on the final return. It may be best to report a capital gain or loss on the final return instead of deferring it to a child.

Deceased's deemed proceeds – Transfer of depreciable property

If there is a transfer of depreciable property, you may be able to use a special amount for the deemed proceeds. To use this special amount, the four conditions we stated above have to be met.

The special amount (deemed proceeds) is the **lower** of:

- the capital cost of the property for the deceased; or
- the result of the following calculation:

$$\frac{\text{Capital cost of the property}}{\text{Capital cost of all the property in the same class that had not been disposed of previously}} \times \text{Undepreciated capital cost of all of the deceased's property in the same class}$$

Example
A man who owned three tractors died in May 1996. His will transferred one tractor to his son. The four conditions for transfer of farm property are met. You have the following details:

Undepreciated capital cost of the three tractors right before death	$ 90,000
Capital cost of the transferred tractor	$ 45,000
Capital cost of all three tractors	$100,000

The deceased's deemed proceeds on the transferred tractor are the lower of:

- $45,000; or
- $\frac{\$\ 45{,}000}{\$100{,}000} \times \$90{,}000 = \$40{,}500.$

The deemed proceeds are $40,500.

When there is more than one property in the same class, you can choose the order in which the deceased is deemed to have disposed of the properties. When you calculate the special amount, adjust the undepreciated capital cost and the total capital cost of the properties in the class to exclude previous deemed dispositions.

Usually when you use the special amount, the deceased will not have a capital gain, a recapture of capital cost allowance, or a terminal loss. When you do this, you defer any gain, recapture, or terminal loss to the beneficiary when the beneficiary disposes of the property.

Note
When you determine the special amount, you will need to recalculate the capital cost of any property in the class when:

- the property was acquired at non-arm's length,
- the property was previously used for other than gaining or producing income; or
- the portion of a property used for gaining or producing income changed.

For more information, contact your tax services office.

Tax tip
You can choose not to use the special amount for the deemed proceeds. You can transfer the property for any amount between the special amount and its fair market value right before death. Make this choice when you file the final return for the deceased.

You may want to do this to use the capital gains deduction, see page 13, on the final return. It may be best to report a capital gain, recapture, or terminal loss on the final return instead of deferring it to a child.

For more details, see Interpretation Bulletin IT-349, *Intergenerational Transfers of Farm Property on Death*, and its Special Release, or contact us

In some cases, you can delay paying part of the amount due. For instance, you can delay paying part of the amount owing from the deemed disposition of capital property. Remember that we charge interest on any unpaid amount, from the due date to the date you pay the amount in full.

If you want to delay payment, you will have to give us security in place of the amount owing. You also have to complete Form T2075, *Election to Defer Payment of Income Tax, under Subsection 159(5) of the Income Tax Act by a Deceased Taxpayer's Legal Representative or Trustee*. For more details, contact the Revenue Collections Division of your tax services office.*In most cases, you have to pay any* amount owing on a return when the return is due.

Chapter 4 – Net capital losses

In this chapter, we discuss how to apply a net capital loss incurred in the year of death, as calculated on the final return. We also explain how to apply net capital losses from earlier years to the final return and the return for the year before the year of death.

We define some of the terms we use in this chapter on page 18.

What is a net capital loss?

An allowable capital loss is three-quarters of a capital loss. A taxable capital gain is three-quarters of a capital gain. When allowable capital losses are more than taxable capital gains, the difference is a net capital loss.

Net capital losses incurred in the year of death

You can use either Method A or Method B to apply a net capital loss incurred in the year of death.

Method A – You can carry back a net capital loss to reduce any taxable capital gains in the three years before the year of death. The loss you carry back cannot be more than the taxable capital gains in those years.

After you carry back the loss, there may be an amount left. If there is, you may be able to use some of it to reduce other income on the final return, the return for the year before the year of death, or both returns. However, before you can do this, you have to calculate the amount you can use.

From the net capital loss you have left, subtract any capital gains deductions the deceased has claimed to date. Use any loss left to reduce other income for the year of death, the year before the year of death, or for both years.

To ask for a loss carryback, complete Form T1A, *Request for Loss Carry Back,* and send it to us. You can get this form from us.

Method B – You can choose not to carry back the net capital loss to reduce taxable capital gains from earlier years. You may prefer to reduce other income on the final return, the return for the year before the year of death, or both returns. However, before you can do this, you have to calculate the amount you can use.

From the net capital loss, subtract any capital gains deductions the deceased has claimed to date. Use any loss remaining to reduce other income for the year of death, the year before the year of death, or for both years.

The following example shows how the two methods work.

Example
A man died in 1996. You have the following details about his tax matters:

Net capital loss – 1996	$20,000
Taxable capital gains – 1995	$ 4,000
Taxable capital gains – 1994	$ 2,000
Total capital gains deductions claimed to date	$ 8,000

He did not claim any capital gains deductions for 1994 or 1995.

You can use Method A or Method B.

		Method A	Method B
Net capital loss	– 1996	$20,000	$20,000
Subtract:			
Taxable capital gains	– 1995	4,000	0
Taxable capital gains	– 1994	2,000	0
Subtotal		$14,000	$20,000
Subtract:			
Capital gains deductions		8,000	8,000
Amount left to subtract from other income		$ 6,000	$12,000

If you use Method A, you can reduce the 1994 and 1995 gains to zero. You still have $6,000 left to reduce the man's other income for 1996 or 1995, or for both years.

If you use Method B, you can use $12,000 to reduce the man's other income for 1996 or 1995, or for both years.

Note
If you apply a 1996 net capital loss to a previous year, any capital gains deductions the deceased claimed in that year or a following year may be reduced. For more information, see the income tax guide called *Capital Gains.*

Net capital losses incurred before the year of death

The deceased may have had a net capital loss before the year of death but never applied it. If so, you can apply the loss against taxable capital gains on the final return. If there is still an amount left, you may be able to use it to reduce other income on the final return, the return for the year before the year of death, or both returns.

To apply the loss against taxable capital gains on the final return, depending on when the loss happened, you may have to adjust it to bring it up to the rate for 1990 and later years. You do not have to adjust a loss that happened in 1990 or later years. However, you have to adjust a loss that happened before 1990, as follows:

- For a net capital loss from **1987 or earlier**, multiply the net capital loss by **3/2**.
- For a net capital loss from **1988 or 1989**, multiply the net capital loss by **9/8**.

When you do these calculations, you get the **adjusted net capital loss.**

Now you can reduce taxable capital gains in the year of death. To do this, use the **lower** of:

- the adjusted net capital loss; or
- the taxable capital gains in the year of death.

After you reduce the taxable capital gains, some of the loss may be left. You may be able to use this amount to reduce other income for the year of death, the year before the year of death, or for both years. However, before you can do this, you may have to calculate the amount you can use.

If the amount you have left includes net capital losses from a year before 1990, readjust it as follows:

- Multiply the amount of any adjusted net capital losses from **1987 or earlier** by 2/3.
- Multiply the amount of any adjusted net capital losses from **1988 or 1989** by 8/9.

The result is your **readjusted balance.** From this balance, subtract the total of all capital gains deductions claimed to date (including those on the final return). If there is an amount left, you can use it to reduce other income for the year of death, the year before the year of death, or for both years.

The following example shows how to handle a net capital loss incurred before the year of death.

Example
A woman died in 1996. You have these details about her tax matters:

Net capital loss, never applied	– 1989	$20,000
Taxable capital gain	– 1996	$ 4,000
Capital gains deductions claimed to date		$ 3,000

You decide to use the 1989 loss to reduce the 1996 gain, and to use any amount left to reduce other income for 1996.

You have to adjust the pre-1990 loss before you can apply it. Because the loss happened in 1989, multiply it by 9/8 to get the adjusted net capital loss:

$20,000 × 9/8 = $22,500

To reduce the 1996 gain, use the lower of:

- $22,500 (adjusted net capital loss); or
- $4,000 (1996 taxable capital gain).

After you use $4,000 of the loss to reduce the gain to zero, you still have $18,500 ($22,500 - $4,000) left. You can use this amount to reduce the woman's other income for 1996.

To determine the amount to use, you have to readjust the $18,500. Again, because the loss happened in 1989, you multiply the amount left by 8/9 to get the readjusted balance:

$18,500 × 8/9 = $16,444

From the readjusted balance, subtract the total of all capital gains deductions claimed to date:

$16,444 - $3,000 = $13,444

You can use $13,444 to reduce the woman's other income for 1996. If you decide not to use the total of this balance in 1996, you can use the amount that is left to reduce other income for 1995.

Note
If you claim a capital gains deduction for the year of death or the year before the year of death, subtract it from the balance of net capital losses you have available to reduce other income in those years. For more details about capital gains and losses, as well as the capital gains deduction, see the income tax guide called *Capital Gains.*

Disposition of estate property by the legal representative

As the legal representative, you may continue looking after the deceased's estate through a trust. In the trust's first tax year, if you dispose of capital property, the result may be a net capital loss. Also in the first year, if you dispose of depreciable property, the result may be a terminal loss.

Usually, you would claim these losses on the trust's return. However, you may be able to claim all or part of these losses on the deceased's final return. For more information, contact us.

Definitions

Adjusted cost base – In most cases, this is the price paid for a property, plus the expenses incurred to buy it. Expenses *include commissions, legal fees, and taxes. You also add the* cost of any additions.

Example
Suppose you buy a building for $50,000, and you pay legal fees of $3,500. The building's adjusted cost base is $53,500. Later you build a $15,000 addition. The adjusted cost base is now $68,500 ($53,500 + $15,000).

If the deceased filed Form T664 or T664(Seniors), *Election to Report a Capital Gain on Property Owned at the End of February 22, 1994,* the adjusted cost base of the property may change. For more information, see the income tax guide called *Capital Gains.*

Capital cost allowance (CCA) – In the year you buy a depreciable property, you usually cannot deduct its whole cost. Instead, because the property will wear out or become obsolete over time, you can deduct its cost over a period of several years. This deduction is called capital cost allowance. You cannot claim it for the fiscal period that ends on the date of death.

Capital property – This includes depreciable property, and any property which, if sold, would result in a capital gain or a capital loss. You usually buy it for investment purposes or to earn income. Some common types of capital property include cottages, securities such as stocks and bonds, and land, buildings, and equipment used in a business or rental operation.

Deemed disposition – This is the term we use when we consider that a person disposes of a property, even though a sale did not take place.

Deemed proceeds of disposition – When we consider that a person disposes of a property, the deemed proceeds are the amount we consider the person to have received for that property, even though the person did not receive this amount.

Depreciable property – This is capital property, used to earn income, on which you can claim capital cost allowance.

Fair market value – This is the highest dollar value that you can get for your property in an open and unrestricted market, where the parties of the transaction deal at arm's length with each other and are not forced to buy or sell.

Locked in – In this guide, locked in means that the beneficiary who is to receive the property has a right to absolute ownership of it. No future event or development can take this right away. For deaths that occur after December 20, 1991, in order for a property to be locked in:

- for a spousal trust, it has to become locked in before the surviving spouse dies; and
- for an individual, it has to become locked in before the individual dies.

In legal terms, we say the property becomes **vested indefeasibly**. For more details, see Interpretation Bulletin IT–449, *Meaning of "Vested Indefeasibly."*

Spousal trust – This is a trust set up under the deceased's will, or a court order, for the surviving spouse. It has to be resident in Canada right after the property becomes locked in for the trust. The surviving spouse is entitled to all the income of the spousal trust that arises before he or she dies. No one else can receive or use the trust's income or capital before the surviving spouse's death.

Undepreciated capital cost – Generally, it is equal to the total capital cost of all the property of a class minus any capital cost allowance that has been claimed in previous years. Also, when property of the class is disposed of, you reduce the undepreciated capital cost by the lower of the following two amounts:

- the proceeds of disposition of the property (either actual or deemed) less expenses incurred to sell it; or
- the capital cost of the property.