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TAX MATTERS

Set a goal this year of updating your estate plan

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If it's okay with you, I'm going to share my key goals for 2022: 1) While my shirt collection for Zoom calls has grown since the pandemic started, my array of pants has not, so I would like to add some new pants in 2022 (preferably some without buttons or a zipper); 2) relearn social cues after nearly two years of being at home; 3) read more fiction (does turning on the subtitles during movies count?); and 4) revise my estate planning now that my kids are adults.

When it comes to your estate plan, your will is probably the most important document that should be prepared. If your will is drafted properly, you'll minimize tax, and your heirs will receive more. As I contemplate my own will, here's what I'm considering, to reduce taxes when I'm gone:

Don't pass away without a will. If you die without a will, it's called dying intestate, and your province or territory will step in and dictate who gets what. This may not align with your wishes. To make things worse, this could result in much more tax owing when you pass away than if you carefully think about and direct who should get certain assets.

Take advantage of the spousal rollover. When you die, you're deemed to have disposed of most of your assets (your capital property). If you leave any of these assets to a spouse, you'll be deemed to have sold them at your adjusted cost base, not at fair market value. The result? No tax to pay. Leaving your spouse with highly taxed assets, such as a registered retirement savings plan or registered retirement income fund, or assets that have appreciated in value, will result in a deferral of tax thanks to the rollover.

Leave non-appreciated assets to the kids. Some people choose to leave some assets to their children even if they have a surviving spouse. Leaving cash, or assets that have not appreciated in value, will not create a tax bill when leaving children (or someone other than a spouse) with assets.

Donate appreciated securities to charity. If you plan to donate to charity in your will, you'd be wise to allow your executor(s) to make a donation in-kind of publicly traded securities (most commonly stocks, bonds and mutual funds) that have appreciated in value. This will eliminate the tax on the capital gain and provide a donation tax credit on top of that.

Deal with a TFSA properly. If you have a tax-free savings account, you'd be wise to name your spouse as a "successor holder" rather than a beneficiary (which I've written about before). This can be done in your will, or in the TFSA documentation itself. This will allow your spouse to step into your shoes as the new owner of your TFSA without having to use his or her TFSA contribution room to put the amount into their plan. Alternatively, you can name your kids as beneficiaries of your TFSA and there will be no tax to pay on the value of the plan when it's distributed to the kids.

Use up available exemptions. There are two primary exemptions that could save you tax when you pass away: 1) the principal residence exemption (to shelter all or part of your home from tax); and 2) the lifetime capital gains exemption (to shelter all or part of the gains on qualified small business corporation shares, or qualified farm or fishing property, from tax).

Track your adjusted cost base. When you die, capital gains taxes may be owing on your final return, as I mentioned earlier. Those capital gains are calculated as the fair market value when you pass away less your adjusted cost base (ACB) of the asset. The higher your ACB, the less tax owing. So, keep track of your ACB on assets, which can be affected by capital improvements on real estate, purchases of the same security at different values over time, inherited or gifted assets, reinvested distributions or dividends from mutual funds or stocks, or the 1994 capital gains election that might have bumped up your ACB on certain assets.

File multiple tax returns. When you're gone, your executor may be able to file up to four different tax returns for your final year. The advantage? A claim can be made for some personal tax credits, such as the basic personal amount, multiple times – once on each tax return. Further, each tax return is eligible for the lower graduated tax rates on lower tax brackets. The four potential returns are: 1) your final, or terminal, tax return; 2) a return for rights or things (income owing to you but not yet collected at the time of your death – dividends and accrued vacation pay are examples); 3) a return for a graduated rate estate (GRE) – if you received income from a GRE; and 4) a return for a partner or sole proprietor.

If revising your will in 2022 is a goal for you, be sure to visit an experienced estate lawyer and talk over these things when drafting your will.

Tim Cestnick, FCPA, FCA, CPA(IL), CFP, TEP, is an author, and co-founder and CEO of Our Family Office Inc. He can be reached at tim@ourfamilyoffice.ca