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TAX MATTERS

Avoid leaving your heirs a nasty tax surprise on your RRIF assets when you die

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Last year my wife and I were travelling in Europe. We rented a car, and everything was going our way, until I discovered we were driving the wrong way on a one-way street – then nothing was going our way, literally. It’s not hard to make mistakes when you’re in unfamiliar territory.

For many folks, the world of personal finance is unfamiliar territory. And if you’re not careful, mistakes can be costly. Today, I want to talk about registered retirement income funds (RRIFs), share a story about a costly mistake, and how to avoid the same fate.

[Why all the fuss over mandatory RRIF withdrawals?](#)

The story

In January, 2020, CTV reported the news of a Calgary woman – call her Mrs. P – who was in a battle with the CRA over \$270,000 in taxes owing on her late husband’s RRIF. Mr. P had passed away at the age of 74 in 2017.

In the year Mr. P turned 71, he visited his bank to convert his RRSP to a RRIF. As you might know, an RRSP matures by the

end of the year you reach the age of 71. To avoid paying tax on the RRSP, most people will convert the plan to a RRIF by Dec. 31 of that year (another option is to convert to an annuity, but most people don’t choose this because it’s less flexible in terms of how much cash you can access in any given year).

When Mr. P visited his bank, the bank employee failed to raise the issue of naming a beneficiary on the newly opened RRIF. While Mrs. P had been the beneficiary of his [RRSP](#), a RRIF is a new contract, and the beneficiary must be designated again. Without a beneficiary named, Mr. P’s estate was entitled to his RRIF assets upon his death, and about \$270,000 was owing to the taxman.

The rules

The general rule, when someone dies, is that the deceased owner of the RRIF (called the annuitant) is deemed to have received the fair market value of the RRIF assets held at the time of death. It’s as though the deceased made a withdrawal of the RRIF assets immediately prior to death, with taxes owing on the final tax return.

There are a couple of exceptions to this rule. The deceased person will not be deemed to have received the amount from the RRIF – and therefore will avoid tax – if he or she had a spouse (or common-law partner) at the time of death and the following two conditions are met:

- the spouse is designated in the RRIF contract or the will of the deceased as the sole beneficiary of the RRIF, and
- the RRIF assets are directly transferred to an RRSP, RRIF or another qualifying plan, or used to buy an annuity, for the surviving spouse (the transfer has to take place by Dec. 31 of the year after the year of death).

If these conditions are met, the surviving spouse will receive a T4RIF slip with the amount of the RRIF showing in box 16, which means that the RRIF amount is now taxable to the surviving spouse, not the deceased. But the surviving spouse will also receive a receipt for the amount that was transferred to his or her own RRSP, RRIF or other plan, and that receipt can be used to claim a deduction for the amount transferred. The net effect of these two slips is that there should be no tax owing by the surviving spouse on the RRIF amount. Rather, taxes will be owing in the future when amounts are withdrawn from the plan.

Mr. P should have named his wife as beneficiary under his RRIF contract. He could have also named her as beneficiary of the RRIF in his will – which apparently didn't happen either. Mrs. P did have one other option available (although she apparently missed the deadline for this):

If the exception above doesn't apply, it's possible for the legal representative of the deceased person to jointly elect, with the surviving spouse, that the RRIF assets should be taxable to the surviving spouse instead of the deceased person (to do this, use Form 1090 – Death of a RRIF Annuitant). Then, the surviving spouse can transfer the RRIF assets to, most commonly, his or her own RRSP or RRIF and claim a deduction for the amount transferred. This will defer the tax until amounts are withdrawn from the spouse's plan.

[Why early RRIF withdrawals don't work for most retirees](#)

The moral

You should periodically check with your financial institution to make sure you've named a beneficiary of your RRIF (or RRSP) and include the same beneficiary in your will. And always get good tax advice before and immediately after a loved one dies to avoid nasty surprises. If Mrs. P had obtained good advice immediately after Mr. P died, she could have elected to avoid the taxes owing.

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