How Much Tax Do I Pay When I Die?

As the old saying goes, "The only two guarantees in life are death and taxes." Many of our clients often ask how much will be lost to taxes upon death. It is a challenge to try to answer this question in 500 words or less, but hopefully this will provide some insight. We have included some tips and strategies below to help reduce estate taxes in BC.

There are two main tax burdens when an individual passes away:

i) Probate taxes: Apply to all assets that fall into the estate. This typically excludes assets in joint names and those with a named beneficiary. Probate laws vary across provinces and territories in Canada.

ii) Income taxes: In Canada, a person is deemed to have disposed of all assets upon death and may be subject to income tax. These must be paid upon completing their terminal tax return.

Generally speaking, when someone passes away, the surviving spouse is often the beneficiary and would typically inherit all assets tax-free as a spousal rollover. These include: real estate, bank accounts and other investments kept in joint names as well as Registered Retirement Savings Plans (RRSPs), Registered Retirement Income Funds (RRIFs) and Tax-Free Savings Accounts (TFSAs) that have the surviving spouse named as beneficiary.

The larger tax bill often applies when the surviving spouse passes away. This is also typically the case for single or divorced individuals.

For illustration purposes, let's consider a scenario where Jane, a widow, has two adult children and passes away with the following assets:

- $800,000 Principal Residence paid $400,000 in sole name
- $400,000 Rental Property paid $300,000 in sole name
- $500,000 RRSP/RRIF beneficiaries are 2 children
- $100,000 Tax Free Savings Account beneficiaries are 2 children
- $100,000 Investment Account sole name $50,000 cost base
- $100,000 Vehicle and Bank Accounts
- $ 0 Debt

$2,000,000 Total Assets & Net Worth

Probate tax in BC is approximately 1.4% on all assets that fall into estates valued over $50,000. Assets such as RRSPs, RRIFs, Tax Free Savings Accounts and Life Insurance with direct beneficiaries generally fall outside of BC probate.
For Jane's estate, everything except the TFSA + RRSP would be subject to probate. This would result in 1.4% x $1,400,000= $19,600 that her executor would need to pay prior to distributing the estate.

The larger bill comes from Jane's terminal tax return. Assuming she passed away on January 1st and had no pension or other income, she would owe the following:

- $0 tax on Principle residence since capital gains are exempt on primary residence
- $100,000 capital gain on rental property of which 50% is taxable
- $500,000 RRSP is fully taxable despite having named beneficiaries
- $0 on TFSA!
- $50,000 Investment capital gain of portfolio of which 50% is taxable
- Nothing on bank accounts or personal assets

Total Income= $50,000 + $500,000+ $25,000 = $575,000

Using the Ernst & Young BC online tax calculator (www.ey.com) and assuming no other credits nor deductions, the deceased would owe about $263,290 in taxes or an average of 46%.
All said, the kids would be inheriting an incredible legacy valued at $2,000,000 - $19,600 - $263,290= $1,717,110 or $858,555 each, assuming the estate was divided equally between the two children.

We purposely left out private corporations due to their complex nature. New BC rules exist where it could make sense for shareholders to implement a secondary Will specific to only their corporation. Given the unique nature of this, we recommend seeking trusted legal advice.

We often talk with clients who had the best intentions when trying to reduce estate taxes but were unaware of the potential ripple effects. Given the world of blended families, ever-changing tax rules and the sensitivity of money, we always feel it is best to review these with an estate/tax specialist.

Our next article will go over some of these potential tips and strategies to help reduce taxes.

Until next time…Invest Well. Live Well.
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