

The Application of Alternative Minimum Tax in the Year of Death

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The Federal alternative minimum tax (“**AMT**”) regime is intended to ensure that individuals, including certain trusts, pay a certain minimum level of tax where income tax calculated under the regular rules is reduced by significant deductions, exemptions, or tax credits. In such a case, a special formula is used to calculate the AMT amount payable by the individual.[1]

However, there are several instances where AMT will not apply, two of which will be discussed here.

No AMT in the Year of Death

Generally, when a taxpayer dies, the taxpayer is deemed to have disposed of each capital property owned by the taxpayer immediately before death for proceeds equal to fair market value.[2] This may trigger accrued capital gains or recapture on capital properties owned by the taxpayer and the taxable capital gain and/or recapture must be included in the taxpayer’s final T1 Income Tax and Benefit Return (the “**Terminal Return**”). For many individuals, this can create a significant tax liability. However, there may be instances where an individual’s death will not create a tax liability. For example, if the taxpayer dies with no income in a year and leaves their entire estate to a spouse, the taxpayer’s estate will be transferred to the spouse at cost on a rollover basis (unless an election is filed to the contrary), deferring any tax on capital gains or recapture until the death of the spouse.[3] This could potentially put the taxpayer in a position where their income is low enough that AMT would normally be a concern.

Recognizing this, Canada Revenue Agency (“**CRA**”) has published guidance specifying that AMT does not apply to an individual for the year of death, even where no tax (or minimal tax) would otherwise be owing.[4] The same CRA guidance also states that if the deceased paid AMT in one or more of the seven years prior to death, part or all of that AMT may be available to be carried forward and deducted on the deceased’s Terminal Return.

When considering the AMT on death, the deceased individual’s legal representatives does not need to consider whether AMT is triggered on the Terminal Return, but should consider whether AMT from prior years may be carried forward to offset taxes owing in the year of death, if any.[5] The individual’s legal representatives should consider the best way to utilize any unused AMT carryforward, including electing out of a spousal rollover to trigger capital gains on death and thereby raise the adjusted cost base of the particular asset(s) passing to the surviving spouse.[6]

Of note, CRA audit guidance provides that AMT carryforward amounts may only be claimed on the deceased’s principal Terminal Return (excluding any other available returns, for example a return for rights or things).[7]

No AMT for Graduated Rate Estates

A graduated rate estate (“**GRE**”) is the estate of a deceased individual where certain statutory conditions are met, including that a GRE can only exist for 36 months following the death of the deceased.[8] GREs are subject to the same graduated income tax rates as individuals, rather than taxed at the highest marginal rates applied to most trusts.[9]

Historically, GREs were subject to the AMT, but with the availability of an exemption. For taxation years beginning after 2023, the AMT rules were amended so that a GRE is specifically excluded from the application of AMT.[10] AMT is not applicable even if the GRE has no (or minimal) income.

Conclusion

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The income taxes that arise on the death of an individual can be particularly onerous. However, given the recent changes to the AMT regime, death avoids the AMT in the year of death and preserves the ability to use AMT carryforward on an individual's Terminal Return. An individual's estate that is a GRE will also not be subject to AMT. A PDF of this blog is available for download [here](#).

[1] *Income Tax Act*, R.S.C., 1985, c. 1 (5th Supp.) at s. 127.5 [ITA].

[2] ITA, at ss. 70(5)

[3] ITA, at ss. 70(6)

[4] <https://www.canada.ca/en/revenue-agency/services/tax/individuals/life-events/doing-taxes-someone-died/prepare-returns/report-income.html>

[5] The AMT carryforward rules can be found in the ITA at ss. 120.2(1)

[6] ITA, at ss. 70(6.2)

[7] <https://www.canada.ca/en/revenue-agency/services/tax/technical-information/income-tax-audit-manual-domestic-compliance-programs-branch-dcpb-17.html>

[8] ITA, at ss. 248(1) "graduated rate estate"

[9] ITA, at ss. 122(1)

[10] ITA, at cl. 127.55(f)(i)

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