Backfiring Donations

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Mom passed away late last year. It's late March. You sit in the accountant's office expecting to quickly clear up the estate and turn that stock portfolio and those mutual funds into gold or real estate or pay off your mortgage by next month.

You can't believe what you are hearing. Your mom donated 5 percent of the remainder of her estate to charity. Mom was a consistent donor to all kinds of charities. You were proud of her record of donations and volunteerism. The charity she has left her 5 percent to demands a review of the accounting for your mother's estate. Not just post date of death, but they want to open up her old tax returns and verify that she received all the tax credits she deserved. You are not sure what a tax credit is and the accountant explains that your mom might qualify for the disability tax credit. The charity wants a comprehensive accounting of her estate including the investment portfolio to ensure that the adjusted cost base calculated on the date of death is accurate. They want to ensure that Mom did not pay too much tax. They want to ensure that the 5 percent they are receiving is a fair representation of their portion of the remainder of the estate.

You remember back to a couple of years ago. Mom came over one day. You remember how upset she was at the accountant she had visited on the recommendation of her banker. That accountant had asked to see her investment portfolio since its inception. Mom had been very annoyed with the accountant. It was none of her business how much I own and what I have invested in, she said. I declared the income from the information slips that were sent to me, she said. You commiserated with her about what "nosy parkers" some people are and about what right that accountant had to see those investment statements.

As executor you hired a new accountant to oversee the final tax returns and the return for the estate. You expect it will only take a month and it will all be cleared up. It is six months later and you are annoyed with how long this is taking. This news about the charity's insistence on a complete accounting really throws a loop into your plans.

The accountant is explaining that you will need to produce all of the old tax returns since your mom's portfolio was set up when your dad passed away. You will need to provide the final returns for your dad's estate to verify that the assets were transferred at cost to your mom's investment accounts or if the values were bumped to fair market value and, in fact, you might even have to find your dad's paperwork to determine that those values were calculated correctly. You panic as you remember you shredded those records just last year. The accountant is explaining that you will have to pay the bank and the brokerage firm for copies of those reports if they have been destroyed. You must dredge up all the old tax returns. If you don't have copies, obtaining copies of the schedules that show details of capital gains and losses from Canada Revenue Agency will take time as those records are not stored on the computer.

The income and capital gains and losses for each asset in the portfolio will need to be tracked through to your mom's date of death in order to compare the income to the tax returns for prior years. If there are discrepancies between the calculations and what was reported, you might have to do something called a voluntary disclosure to report the unreported income or losses in order to clean up this mess.

The accountant explains that this is April and that they are far too busy to do this work until at least August. The accountant explains that to account for a portfolio of investments when it is likely that the person did not declare their capital transactions might cost hundreds of dollars per year. You visualize the size of your inheritance shrinking.

What could have prevented this, you ask. If your mother had accounted for the portfolio and calculated the adjusted cost base to include returns of capital, dividends reinvested and reported her capital gains and losses from dispositions of assets in her portfolio on her tax return and paid the tax, we wouldn't be sitting here having this conversation today. The charity has the right to ask for an accounting as they are a recipient of a percentage of the estate. Just like any other beneficiary, they have rights.

You receive the reassessments necessary to file for a Clearance Certificate in May of the next year, about 14 months after this conversation. The accountant completed the voluntary disclosure for unreported income from unreported gains in October. The unreported income was offset in part by losses on the mutual funds portfolio and a claim for the disability tax credit for several years because she had not been able to walk a block for quite a while. You pay a substantial accounting bill and have gained an appreciation of what is required to account for a portfolio. You settle the estate and distribute the remainder to the beneficiaries, including the 5% to the charity almost two years after Mom died.

Sound familiar? I find that accounting for investment portfolios is highly underrated by most taxpayers. Not only is the investment industry not responsible for calculating your adjusted cost base of your portfolio, they have no way of knowing if you decided to make an election to defer a capital gain or loss on the sale of a mutual fund within a group of funds until the ultimate disposition of funds out of the group of funds. Most of the time your investment company reports your current fair market value and compares it to last year rather than report how much you originally invested, how much you have earned and how much your portfolio has actually appreciated that is an unrealized gain or loss.

Investment companies know that this information might discourage you, so they go to great lengths to avoid the painful reminder that the money you entrusted to their care has not grown in value since you left it with them to manage. Am I cynical? I don't think so. I have a pet theory about the $100,000 wall. I have seen far too many portfolios where the $100,000 so carefully saved over 20 years at $5,000 a year does not grow beyond the $100,000. You put in $5,000 and the portfolio value does not grow by $5,000. Sometimes it even drops more than $5,000 in the year you added $5,000.

If you don't have an accounting of your investment portfolio, you might want to consider finding an accountant who uses Quicken to help you set up a record-keeping system for your portfolio. (This coming fall I will be offering an instruction set on how to account for your portfolio on my website at www.taxdetective.ca. You see it's tax time. I am far too busy to work on that project right now.)

Looking for more details? Here are additional reference materials for more in-depth coverage of the subject:

➡ Capital Gains Guide
http://www.cra-arc.gc.ca/E/pub/tg/t4037/README.html

➡ How to Account for Mutual Funds
http://www.cra-arc.gc.ca/E/pub/tg/rc4169/rc4169-e.html

➡ Preparing Tax Returns for Deceased Persons
http://www.cra-arc.gc.ca/E/pub/tg/t4011/README.html

➡ T3 Trust Tax Return Guide
http://www.cra-arc.gc.ca/E/pub/tg/t4013/t4013-e.html

➡ What to do When Someone Dies
http://www.cra-arc.gc.ca/E/pub/tg/rc4111/README.html
http://www.cra-arc.gc.ca/tax/individuals/life-events/death/menu-e.html

The Canadian Gift Planner Association (888-430-9494 or www.cagp-acpdp.org) has guidelines for charities in the form of a $30 booklet that explains what the charity is entitled to do when they are the recipient of a percentage of an estate.

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