The Law Society of Upper Canada | Barreau du Haut-Canada

20TH ANNUAL
Estates and Trusts Summit

CHAIRS

Sheila Crummey, C.S., TEP
Miller Thomson LLP

Thomas Grozinger, C.S., TEP
RBC Wealth Management
Estate & Trust Services

DAY TWO
October 17, 2016

cpd Continuing Professional Development

The Law Society of Upper Canada | Barreau du Haut-Canada

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20TH ANNUAL
Estates and Trusts Summit – DAY TWO

Chair: **Sheila Crummey, C.S., TEP**
Miller Thomson LLP

Thomas Grozinger, C.S., TEP
RBC Wealth Management, Estate & Trust Services

October 17, 2017
9:00 a.m. to 4:30 p.m.

Total CPD Hours = 5 h 30 m Substantive + 1 h Professionalism

Sheraton Centre Toronto Hotel
123 Queen Street West
Toronto, ON

CLE17-0110101

Agenda

DAY TWO:

9:00 a.m. – 9:10 a.m. **Welcome and Opening Remarks**

Sheila Crummey, C.S., TEP, *Miller Thomson LLP*

Thomas Grozinger, C.S., TEP
RBC Wealth Management, Estate & Trust Services

9:10 a.m. – 9:35 a.m. **Update on Estates and Trusts Cases**

David Freedman, C.S., TEP, *Faculty of Law, Queen's University*

9:35 a.m. – 9:55 a.m.	**Estate Administration Tax Issues** Lori Duffy, *WeirFoulds LLP*
9:55 a.m. – 10:15 a.m.	**Posthumous Conception: Recent Changes to the *Succession Law Reform Act* and their Impact on Estate Law** Krystyne Rusek, *Pallett Valo LLP*
10:15 a.m. – 10:25 a.m.	**Question and Answer Session**
10:25 a.m. – 10:45 a.m.	**Coffee and Networking Break**
10:45 a.m. – 11:05 a.m.	**Charity Law Update** Terrance Carter, *Carters Professional Corporation*
11:05 a.m. – 11:25 a.m.	**Garnishment by a Third Party** Benjamin Arkin, *Arkin Estate Law Professional Corporation*
11:30 a.m. – 11:50 a.m.	**Scary Situations Where Estate Solicitors May Get Sued by Estate Litigators** Justin de Vries, *de VRIES LITIGATION LLP*
11:50 a.m. – 12:10 p.m.	**Conflict of Laws Issues for Wills and Estate Administration** Carla Figliomeni, *Miller Thomson LLP*
12:10 p.m. – 12:20 p.m.	**Question and Answer Session**

12:20 p.m. – 1:20 p.m.	**Lunch Provided`**
1:20 p.m. – 1:50 p.m.	**Tax Law Update** Joan Jung, *Minden Gross LLP*
1:50 p.m. – 2:10 p.m.	**Jurisdictional Issues in Powers of Attorney** Paul Taylor, *Borden Ladner Gervais LLP*
2:10 p.m. – 2:35 p.m.	**U.S. Tax Law Update** Katherine Cauley, Esq., *Hodgson Russ LLP*
2:35 p.m. – 2:45 p.m.	**Question and Answer Session**
2:45 p.m. – 3:05 p.m.	**Coffee and Networking Break**
3:05 p.m. – 3:25 p.m.	**Life Insurance Update for** **Trusts and Estates Practitioners** Florence Marino, *Manulife*
3:25 p.m. – 3:30 p.m.	**Question and Answer Session**
3:30 p.m. – 4:20 p.m.	**Disclosure of Wills, File Storage, What to** **Include in the File, etc.** **(50 Minutes Ⓟ)** **POLLING** Jordan Atin, C.S., TEP, *Atin Professional Corporation* Sean Lawler, *Shibley Righton LLP* Susan Sack, *Rosen Sack LLP*

4:20 p.m. – 4:30 p.m. **Question and Answer Session**

4:30 p.m. **End of Day Two**

20TH ANNUAL
Estates and Trusts Summit – DAY TWO

October 17, 2017

SKU CLE17-0110101

Table of Contents

TAB 1 **Case Law Update ....1 - 1 to 1 - 86**

David Freedman C.S., TEP, Faculty of Law, *Queen's University*
& Counsel, *Hull & Hull LLP*

TAB 2 **Estate Administration Tax Issues..2 - 1 to 2 - 18**

Lori Duffy, *WeirFoulds LLP*

TAB 3 **Posthumous Conception:**
Recent Changes to the *Succession Law Reform Act*
And their Impact on Estate Law ....3 - 1 to 3 - 18

Krystyne Rusek, *Pallett Valo LLP*

TAB 4 **Update on Charity Law ....4 - 1 to 4 - 56**

Terrance Carter, *Carters Professional Corporation*

TAB 5 **Mind if I Cut In? When a Beneficiary's Creditor Joins the Trustee-Beneficiary Dance .... 5 - 1 to 5 - 42**

Benjamin Arkin, *Arkin Estate Law Professional Corporation*

TAB 6 **Why I Am Going to Sue You .... 6 - 1 to 6 - 18**

Justin de Vries
Anna Alizadeh
de VRIES LITIGATION LLP

TAB 7 **Conflict of Laws Issues for Wills and Estate Administration .... 7 - 1 to 7 - 22**

Carla Figliomeni, *Miller Thomson LLP*

TAB 8 **Tax Update .... 8 - 1 to 8 - 28**

Joan Jung, *Minden Gross LLP*

TAB 9 **Jurisdictional Issues in Powers of Attorney......................... 9 - 1 to 9 - 12**

Paul Taylor, *Borden Ladner Gervais LLP*

TAB 10 **Musings on the Effects of Trump's Tax Proposals on Canada-U.S. Cross Border Estate Planning .... 10 - 1 to 10 - 24**

Katherine Cauley, Esq.
Graham Leonard, Esq.
Hodgson Russ LLP

TAB 11 **Life Insurance Update for Trusts and Estates Practitioners .... 11 - 1 to 11 - 28**

Florence Marino, TEP, Assistant Vice-President Tax, Retirement & Estate Planning Services, *Manulife*

TAB 12 **Disclosure of Wills, File Storage, What to Include In the File, Etc.**
PANEL MATERIALS

LawPRO: Landmines for Lawyers When Drafting Wills....... 12 - 1 to 12 - 8
LawPRO: Wills & Estates Claims, Malpractice Fact Sheet . 12 - 9 to 12 - 10

"One Less Witness": Getting Evidence from Lawyers
In Estate Disputes .... 12 - 11 to 12 - 36

Sean Lawler, *Shibley Righton LLP*

Will Plan Meetings – A Model .... 12 - 37 to 12 - 42

Jordan Atin, C.S., TEP, *Atin Professional Corporation*

The Law Society of Upper Canada | Barreau du Haut-Canada

TAB 1

20TH ANNUAL
Estates and Trusts Summit

Case Law Update

David Freedman C.S., TEP
Faculty of Law, *Queen's University*
& Counsel, *Hull & Hull LLP*

DAY TWO
October 17, 2017

cpd Continuing Professional Development

CASE LAW UPDATE

20TH ANNUAL ESTATES AND TRUSTS SUMMIT
(DAY TWO)

C. David Freedman[*]

I. Dependants' Support

(a) *Dagg v. Cameron Estate*, 2017 ONCA 366 (Ont. C.A.) …….. 3

(b) *Habberfield v. Sciamonte*, 2017 ONSC 4332 (Ont. S.C.J.) …….. 8

(c) *Shaw v. Barber*, 2017 ONSC 2155 (Ont. S.C.J.) …….. 10

(d) *Ly v. Chiofalo*, 2017 ONSC 2444 (Ont. S.C.J.) …….. 11

II. Unjust Enrichment / Constructive Trusts

(a) *Granger v. Granger*, 2016 ONCA 945 (Ont. C.A.) …….. 12

(b) *McDonald v. McDonald*, 2017 BBCA 255 (B.C.C.A.) …….. 13

(c) *Sweet v. Moore*, 2017 ONCA 182 (Ont. C.A.) …….. 16

III. Gifting

(a) *Jansen v. Niels Estate,* 2017 ONCA 312 (Ont. C.A.) …….. 29

(b) *Morreale v. Romanino,* 2017 ONCA 359 (Ont. C.A.) …….. 31

(c) *Texeira v. Markgraf Estate*, 2017 ONSC 427 (Ont. S.C.J.) …….. 34

IV. Validity and Interpretation of Wills & Powers of Attorney

(a) *Koziarski v. Sullivan*, 2017 ONSC 2704 (Ont. S.C.J.) …….. 34

(b) *Vanier v. Vanier*, 2017 ONCA 561 (Ont. C.A.). …….. 39

(c) *Melendy v. Drodge*, 2017 NLCA 46 (Nfld. & Lab. C.A.) …….. 41

(d) *Garwood v. Garwood*, 2017 MBCA 67 (Manitoba C.A.) …….. 44

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[*] LLB, MA, PhD, TEP. Certified Specialist (Estates & Trust Law). Faculty of Law, Queen's University & Counsel, Hull & Hull LLP.

(e) *Johnston Estate v. Johnston*, 2017 BCCA 59 (B.C.C.A.) …….. 44

V. Procedure

(a) *Seepa v. Seepa*, 2017 ONSC 5368 (Ont. S.C.J.) …….. 47

(b) *Roulston v. McKenny*, 2017 ONCA 9 (Ont. C.A.) …….. 53

(c) *Armitage v. Salvation Army*, 2016 ONCA 971 (Ont. C.A.) …….. 55

(d) *Barcham v Barcham*, 2017 ONSC 813 (Ont. S.C.J.) …….. 58

VI. Trustees

(a) *Cahill v. Cahill*, 2016 ONCA 962 (Ont. C.A.) …….. 61

(b) *Craven v. Osidacz*, 2017 ONSC 1757 (Ont. S.C.J.) …….. 63

(c) *Akers v. Samba Financial Group,* [2017] UKSC 6 (U.K.S.C.) …….. 69

(d) *Tyrell v. Tyrell*, 2017 ONSC 4063 (Ont. S.C.J.) …….. 73

VII. Real Property

(a) *Blackmore v. Bower*, 2016 ONSC 6644 (Ont. S.C.J.) …….. 75

VIII. Remedies

(a) *Easy Loan Corporation v. Wiseman*, 2017 ABCA 58 (Alta. C.A.) …….. 77

IX. Rectification

(a) *Canada (Attorney General) v. Fairmont Hotels Inc.*, 2016 SCC 56 (S.C.C.) …….. 81

(b) *McLauglin v. McLaughlin*, 2016 ONCA 899 (Ont. C.A.) …….. 85

I. DEPENDANTS' SUPPORT

(a) Dagg v. Cameron Estate, **2017 ONCA 366 (Ont. C.A.)**

This case was heard by the Court of Appeal notwithstanding that the parties had settled and the appeal was moot. At issue was the proper meaning and application of Section 72(7) of the *Succession Law Reform Act* which had until this matter gone without judicial consideration. Sections 72(1)(f) and 72(7) provide:

> **Value of certain transactions deemed part of estate**
>
> 72. (1) Subject to section 71, for the purpose of this Part, the capital value of the following transactions effected by a deceased before his or her death, whether benefitting his or her dependant or any other person, shall be included as testamentary dispositions as of the date of the death of the deceased and shall be deemed to be part of his or her net estate for purposes of ascertaining the value of his or her estate, and being available to be charged for payment by an order under clause 63 (2) (f),
>
> …
>
> (f) any amount payable under a policy of insurance effected on the life of the deceased and owned by him or her;
>
> …
>
> Rights of Creditor
>
> 72. (7) This section does not affect the rights of creditors of the deceased in any transaction with respect to which a creditor has rights.

The agreed statement of facts submitted by the parties set out a dispute between the separated wife of the Deceased and his partner with whom he was living and was pregnant with his child. The Deceased died while the child was *in utero* and a dependants' support application was commenced on behalf of the child and his mother after the child's birth. The question for the Court was in respect of a policy of life insurance owned by the Deceased on his own life. The

separated wife argued that the proceeds fell outside the notional estate (as provided by s.72(1)(f)) as a consent Order made between the Deceased and his wife in Family Court provided that he designate her irrevocably on any life insurance. Before his death, the Deceased changed the beneficiary designation from the separated wife to name the wife, their two children, and the Deceased's new partner as beneficiaries. The fly in the ointment was that there was nothing in the consent Order and no separation agreement that required the Deceased to carry life insurance nor that specifically provided that the proceeds of the insurance were to act as security against spousal and child support owed to the Deceased's first family.

The importance of the case generally has less to do with the facts of the case and more to do with the intersection of the dependants' law regime in the *Succession Law Reform Act* and the support regime in the *Family Law Act* which may continue against the estate of a support payor. Thus the Court put the issue for resolution as follows:

> *Where a support payor owns a life insurance policy and has been required by court order to name the spousal or child support recipient as the irrevocable beneficiary of the policy, upon the payor's death what rights does the support recipient have to the policy's proceeds in the face of a competing claim by another dependant of the deceased brought under Part V of the SLRA?*

In resolving the issue that Court of Appeal accepted a number of propositions as correct:

First, the rationale behind the so-called "claw back" provisions set out in s.72(1) of the *Succession Law Reform Act* which swell the value of the estate for dependants' support purposes is less about intentional evasion of support obligations by the deceased and more about the proper maintenance of dependants. Brown J.A. held that "…s. 72(1) captures transactions even if they are not made by a testator with the specific intention of evading obligations to support dependants. However, the legislative history of s. 72 certainly identifies preventing the evasion of support obligations on death as the mischief the section seeks to address. Or, as this court described the section's purpose in *Madore-Ogilvie (Litigation Guardian of) v. Ogilvie Estate*, 2008 ONCA 39 (CanLII), 88 O.R. (3d) 481, at para. 39, it

operates to prevent arrangements that "jeopardise the maintenance of the deceased's dependants."[1]

Second, there is a policy interest in maintaining the integrity of the support regime set out in the *Family Law Act* and the *Divorce Act* in their testamentary effect and particularly with respect to security in the form of life insurance on the life of the payor spouse. Brown J.A. held:[2]

> [56] The *Family Law Reform Act*, S.O. 1978, c. 2 ("FLRA"), was enacted on March 16, 1978, four months after the *SLRA* came into force. Section 19(1)(j) of the *FLRA* provided that on an application for support, a court may order that "a spouse who has a policy of life insurance as defined in Part V of The Insurance Act designate the other spouse or child as the beneficiary irrevocably." Section 19(1)(k) also empowered a court to order "the securing of payment under the order, by a charge on property or otherwise."
>
> [57] Those provisions have been carried forward, in slightly modified form, as ss. 34(1)(i) and (k) of the Family Law Act…
>
> [58] The jurisprudence commonly treats the purpose of a beneficiary-designation order under s. 34(1)(i) of the FLA as securing the support obligation of a spouse in the event of his or her death: *Smylie v. Smylie*, 2006 CarswellOnt 7456 (S.C.), at para. 77; *Thomas v. Thomas*, [2003] O.J. No. 5401 (S.C.), at para. 96.
>
> [59] As to s. 34(1)(k), in *Katz v. Katz*, 2014 ONCA 606 (CanLII), 377 D.L.R. (4th) 264, this court held, at para. 69, that the sub-section "is broad enough to permit a court to order a spouse to obtain an insurance policy to secure payment of the order following the payor spouse's death. The concluding words 'or otherwise' in s. 34(1)(k) afford the court broad scope for securing the payment of a support order."
>
> The court continued, at para. 70:

---

[1] 2017 ONCA 366 at para. 54 (Ont. C.A.)
[2] 2017 ONCA 366 at paras. 56-59 (Ont. C.A.)

> Because a support payor's estate is bound by a support order following the payor's death, the court making a support order is entitled to secure the payments to be made in the event of the payor's death by requiring the payor to obtain and maintain life insurance for a specified beneficiary while the support order is in force and to give directions concerning the extent to which the payout of the insurance proceeds will discharge the support obligation: see *Laczko v. Laczko* (1999), 1999 CanLII 14998 (ON SC), 176 D.L.R. (4th) 507 (Ont. S.C.), at pp. 511-12.

Third, notwithstanding that the relevant Family Court order at issue in the case did not specifically identify the use of the insurance to secure the Deceased's support obligations in the facts of the case, the Court of Appeal accepted that the separated wife had a legitimate interest and a "right" within the meaning of Section 72(7) regardless of whether she was a "secured" creditor in the ordinary sense.[3]

Last, the resolution of the issue was thus identified by Brown J.A.:[4] "I conclude that where, at the time of his death, a spousal or child support payor owns a policy of insurance that is subject to a court order requiring the designation of the support recipient as the irrevocable beneficiary of the policy, s. 72(7) protects from the claw back of s. 72(1) that part of a policy's proceeds needed to satisfy the deceased's obligations to the spousal and child support recipients, calculated in accordance with the support orders in place at the time of his death." Brown J.A. continued:

> **[76] Under both the *FLA* and the *Divorce Act*, a court can secure the payment of support obligations by formally granting a charge against property. However, the jurisprudence discloses that the more common practice is for a court to order a support payor to designate the support recipient as the irrevocable beneficiary under a life insurance policy. While colloquially such an order is described as one that "secures" payment of the support obligations in the event of the payor's death, it would be more accurate to say that such an order makes available a pool of money – the proceeds of the life insurance policy – to satisfy the support payor's**

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[3] 2017 ONCA 366 at para. 73 (Ont. C.A.)
[4] 2017 ONCA 366 at para. 75 (Ont. C.A.)

obligations calculated in accordance with the support orders in place at the time of his death.

[77] Where such a beneficiary-designation order is made ancillary to a spousal or child support order, the support recipient is a creditor of the deceased in a "transaction with respect to which a creditor has rights." The transaction is the purchase or maintenance by the deceased of a policy of insurance on his life, which stands available, by operation of court orders, to satisfy the deceased's spousal or child support obligations on his death by designating the support recipient as the beneficiary of the policy. For the purposes of s. 72(7), the support recipient is a creditor of the deceased because, as the court-ordered designated beneficiary under the policy of insurance, the support recipient has the legal right to look to the policy's proceeds to satisfy the deceased's support obligations calculated as at the time of his death. Those obligations can include (i) any existing arrears and (ii) the present value of any future support obligations, calculated by reference to the terms and duration of the support order in place at the time of his death.

[78] Such an interpretation of s. 72(7) is faithful to the scheme and object of Part V of the *SLRA*, which places limits on the reach of the claw backs contained in s. 72(1). It also harmonizes the operation of Part V of the SLRA with the insurance beneficiary-designation powers granted to courts under family law legislation: Ruth Sullivan, *Sullivan on the Construction of Statutes*, 6th ed. (Toronto: LexisNexis Canada Inc., 2014), at §11.2 – 11.5. The interpretation recognizes that although a policy of insurance ordered to stand available to satisfy a deceased's family law support obligations may fall within the language of s. 72(1)(f), it is not a transaction by the deceased designed to avoid his responsibilities to his dependants. On the contrary, it is a transaction intended to provide for family law support-order dependants. By "clawing back" into the deceased's net estate only that portion of the proceeds of a life insurance policy in excess of the amount required to satisfy the deceased's family law support obligations, funds may be made available to support his other dependants while, at the same time, discharging his existing family law support obligations.

[Emphasis added.]

At the end of the day, both family law and estates lawyer should be interested in *Dagg v. Cameron Estate* to make the point that Family Court orders that provide for security in the form of life insurance proceeds will take the proceeds of a dependants' support application made by other dependants to the extent that the proceeds relate to the support obligation; that is, funds in excess of the security against the support obligation may fall into the notional estate of the deceased. Certainly the parties to family law litigation can design ways for such proceeds to fall completely outside Section 72(1)(f) of the *Succession Law Reform Act* but where they do fall into the notional estate a balancing of interests in required. Estates lawyers will be interested in future in the quantification of support obligations with specificity to identify what part of insurance proceeds may be attacked.

(b) Habberfield v. Sciamonte, 2017 ONSC 4332 (Ont. S.C.J.)

This case deals with the limitation period provisions set out in Section 61 of the *Succession Law Reform Act* respecting dependants' support obligations:

> **Limitation period**
> 61. (1) Subject to subsection (2), no application for an order under section 58 may be made after six months from the grant of letters probate of the will or of letters of administration.
>
> Exception
> (2) The court, if it considers it proper, may allow an application to be made at any time as to any portion of the estate remaining undistributed at the date of the application.

While no new ground is broken, the judgment of Justice Lofchik usefully sets out the relevant criteria that ought to inform the Court's exercise of its discretion in allowing an application to continue against the undistributed assets of an estate:

(a) The Court has the discretion to allow the application to proceed at any time as to any portion of the estate remaining undistributed at the date of the application.

(b) The discretion of the Court under section 61(2) to allow an application to proceed although it is brought after the time limit has expired under the SLRA must be exercised judicially, with considerations of the delay involved, the reasons for the delay, and the extent of prejudice in the Estate's defence of the claim.

(c) The Court's discretion to extend the limitation period under section 61(2) is to be exercised in a broad and liberal manner.

(d) In deciding whether to grant the extension, the court must determine whether the situation bears review of whether or not the Deceased made adequate provision in his Will for the proper maintenance and support of his dependents.

(e) The question is not whether the Deceased has in fact done so, but whether there is a sufficient basis for review. This requires a consideration of what is equitable (in relation to the "proper" support of dependents as contemplated by the SLRA).

(f) While delay (including the reason for delay) is a factor to consider, a request for an extension is not grounded solely in "good cause" being shown for the delay. The discretion to extend or refuse is a question of what is equitable between the parties, in all the circumstances.

(g) In the absence of prejudice to the Estate, equity tends to favour granting an extension:

The judge is thus given a discretion to be exercised on the principle of promoting justice between those interested in the estate. It is clear that he must refuse an application if the delay in applying would work an injustice. Further than that it would seem that he must find that justice, in so far as the principle of the Act defines the

> kind of justice that the Legislature had in mind, requires that the application should be heard.

In the case itself, the application was brought by an elderly lady years after the death of her alleged spouse. The reason for delay was said to be family dynamics and a late realization that the support provided to her under the testator's Will was inadequate. Justice Lofchik emphasized the lack of prejudice that would arise in the circumstances of the case in exercising his discretion to allow the application to continue in relation to the estate which had about $2,000,000 still undistributed in the form of realty.

(c) *Shaw v. Barber*, 2017 ONSC 2155 (Ont. S.C.J.)

This case deals with limitations and dependants' support application and particularly the interaction with Rule 7 of the *Rules of Civil Procedure*. In this case the application was made on behalf of an incapable person by her statutory guardian, the Public Guardian & Trustee. Was the application statute barred where it was made beyond the 6-month limitation period set out in Section 61 of the *Succession Law Reform Act?* Regional Senior Justice McNamara held it was not:[5]

> [23] … As the affidavit of counsel at the Office of the Public Guardian and Trustee discloses, once they are appointed statutory guardian of property in a factual situation such as existed here, they begin an investigation into the entire matter. That can be, as the affidavit discloses, a time consuming process because there are usually information gaps because of the client's incapacity which require the OPGT to be reliant on third party information with a need to be verified. The initial investigation is done by a client representative and if the situation warrants it, the matter is then referred to counsel in the OPGT's office which in this case occurred in October of 2015. According to the evidence, further investigation continued under counsel's direction exploring options available. Outside counsel was formally retained by the OPGT on May 6, 2016. The application was brought in August.

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[5] 2017 ONSC 2155 at paras. 23-26 (Ont. S.C.J.).

> [24] Moving carefully and cautiously prior to commencing litigation at public expense would require a thorough investigation of the facts and legal options available. As counsel in his affidavit points out, the client they act for has little capacity to properly advise them of her circumstances, so they have to rely on third party information which may support or not support or be neutral towards the incapable person's position. I agree with counsel that imposing a limitation period commencing as of the OPGT's appointment as guardian of property is not only contrary the wording of the *Limitations Act*, but would also create impossible timelines thus creating the potential for injustice being done to vulnerable individuals.
>
> [25] It is important to remember in all this that the respondent was not in any way prejudiced by delay. While there is no provision in the Limitations Act for self-appointment there is provision in Section 9(2) for a potential defendant to take steps to have a litigation guardian appointed. That Section provides as follows: "9 (2) If the running of a limitation period in relation to a claim is postponed or suspended under section 6 or 7, a potential defendant may make an application or a motion to have a litigation guardian appointed for a potential plaintiff. 2002, c. 24, Sched. B, s.9 (2)."
>
> [26] The defendant in this case was aware that the OPGT was looking into its options vis-à-vis a claim against the estate from shortly after its appointment as statutory guardian. The defendants were at liberty in those circumstances to bring an application under Section 9(2) and had they been successful, a litigation guardian would have been appointed for Ms. Shaw.

One notes again that the question of prejudice seems to drive the Court's decision.

(d) Ly v. Chiofalo, 2017 ONSC 2444 (Ont. S.C.J.)

This case concerns the test for interim support in a dependants' support application. Again, while no new ground is broken, the judgment of Justice Pattillo usefully sets out the nature of

the application and the relevant criteria that ought to inform the Court's exercise of its discretion. Thus Justice Pattillo held:[6]

> This application is essentially an interlocutory motion. It seeks "interim" relief pending the hearing of the main application for dependants' relief. The parties agree that the test is as set out in *Kalman v. Pick and* Katz, 2013 ONSC 304 (CanLII) at para. 5. The party seeking interim relief must establish three things: impecuniosity or financial difficulties such that the party would otherwise not be able to proceed with the case; a *prima facie* case of sufficient merit to warrant pursuit; and special circumstances to satisfy the court that the case is within the narrow class of cases where such an extraordinary exercise of its powers is appropriate.

In this case, "spousal" status was disputed and Justice Pattillo held that the case was not one in which interim support should be ordered. Credibility was in issue and no independent evidence before the Court such that it could not be said that "a *prima facie* case of sufficient merit" was established.

II. UNJUST ENRICHMENT / CONSTRUCTIVE TRUSTS

(a) *Granger v. Granger*, 2016 ONCA 945 (Ont. C.A.)

This was an appeal taken in relation to a claim in unjust enrichment made by a son against his mother seeking a beneficial interest in her house; the son had lived in the house with his spouse without paying rent, and thus the case was one of mutual benefits having been exchanged. A narrow point was highlighted by the Court: the application judge had wrongly considered the value of the benefits exchanged as part of the analysis testing the claim advanced rather than in relation to defences to the claim and/or the question of remedy (and set-off) as mandated by the Supreme Court of Canada in *Kerr v. Baranow*, 2011 SCC 10 (S.C.C.). The case is note worthy in that the careful analysis of Jurisz J.A. should be of assistance to counsel making and defending such claims against estates.

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[6] 2017 ONSC 2444 at para. 4 (Ont. S.C.J.)

(b) *McDonald v. McDonald*, 2017 BCCA 255 (B.C.C.A.)

This case deals with a claim made by three children to contributions they made through the provision of services, *inter alia*, while they were teenager. There was no dispute the work conferred a benefit without pay; rather, the point of contention was whether there was a reasonable expectation of payment. Groberman J.A. described the positions taken by the parties:[7]

> [67] It is common ground that none of the "established categories" of juristic reason for enrichment are present in this case: the plaintiffs did not have contracts of employment with the defendants during their teen years, nor did they manifest an intent that their work on the farm constitute a "gift". Their work was not performed pursuant to a statutory or equitable obligation.
>
> [68] The defendants contend, however, that as a matter of public policy, "work done by a teenager for a family enterprise should not be accorded a remedy in unjust enrichment absent extraordinary circumstances". In their factum they express the policy as follows:
>
> Virtually all children, particularly as they get older, are expected to contribute to the family enterprise in one fashion or another, whether it is doing chores inside the house, painting a fence, mowing the lawn or helping in the family business. It seems likely that much of the work done by teenagers will provide some economic benefit to their parents. In exchange, however, their parents provide them with the necessities of life such as food and shelter and provide them with the opportunity to learn life skills which they can take with them into adulthood. To afford teenagers the right to sue their parents for work done as teenagers simply because it is of benefit to the parents sets a dangerous precedent and ignores the substantial benefits which teenagers receive from their parents at that age.
>
> [69] The plaintiffs dispute the idea that there is any public policy reason why teenaged children doing work for their parents should be excluded from unjust

[7] 2017 BCCA 255 at paras. 67-72 (B.C.C.A.).

enrichment remedies. Among other things, they point out that children (including teenaged children) are a vulnerable group. Where parents exploit their children for economic gain, it is important that the children have a civil remedy.

[70] Despite their contrasting arguments, there is, in fact, a great deal of common ground between the parties. The plaintiffs accept that not every chore done by a teenager (even if it has some economic value to the parents) will found a claim in unjust enrichment. At some level, it is a normal societal expectation that children (particularly older children) will assume responsibility for household tasks. They do not have a legal entitlement to be paid every time they perform routine chores.

[71] On the other hand, the defendants accept that in “extraordinary circumstances”, a teenager will be entitled to compensation. At some point, parental demands on teenagers to perform unpaid “chores” will exceed the level of societal tolerance and be properly characterized as exploitative. It is obvious that there is no public policy in favour of allowing parents to engage in the economic exploitation of their children.

[72] The question, then, is not whether public policy and reasonable societal expectations can provide a juristic reason to deny an unjust enrichment to a teenager in respect of unpaid chores. Clearly they can. Rather, the question is the articulation of the public policy. How far does the juristic reason extend?

Groberman J.A. went on to hold:[8]

[77] In general, we see the performance of chores by children in a family as positive. Such work fosters a sense of responsibility and of family. Ideally, in doing chores, children gain valuable work experience in an environment that is not overly competitive or taxing. They can learn and experience the importance of doing tasks for others without expecting monetary compensation.

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[8] [8] 2017 BCCA 255 at paras. 77-82 (B.C.C.A.).

> [78] These public policy considerations mean that the performance of unpaid chores by children in a family setting will not usually raise issues of unjust enrichment. There are, however, limits that must be observed. While unjust enrichment principles should not interfere with the ability of parents to assign routine chores to their children, they will ensure that children do not fall prey to exploitation.
>
> [79] The parties to this appeal have not, in argument, fully explored the issue of what boundaries ought to be applied in deciding when the law will grant unjust enrichment remedies in respect of chores performed by children. In the absence of full argument, it would be unwise for the court to attempt any exhaustive enumeration of what features might make chores "exploitative". I would suggest, however, that exploitation may be characterized by economic benefits to the parents that are grossly disproportionate to the benefits that the children have as members of the family, or by work by the children that is manifestly detrimental to their health or wellbeing.
>
> [80] In the present case, the judge specifically found that the work assigned to the plaintiffs was "not so extraordinary in the context of [a] farming household where the social norm [is] that all family members pitch in and perform chores for which strangers would have expected compensation". The judge noted that the children engaged in leisure and outside social activities. While the family lived frugally, there was no suggestion of economic deprivation, nor was it suggested that the children were treated by the parents as "profit centres".
>
> [81] Neither Julie nor Brian refers, in their argument, to any circumstances that could amount to exploitation. Dean did not take part in this appeal, and there is no finding in the court below that he suffered exploitation at the hands of his parents.
>
> [82] On that basis, I would allow the defendants' appeal from the orders awarding the plaintiffs damages for unjust enrichment.

The Court, it is submitted, took a pragmatic, principled, and common sense view of the point and the remarks of Groberman J.A. are useful in delineating between the reasonable

expectations of both parents and children as a matter of public policy (and the avoidance of frivolous claims).

(c) ***Sweet v. Moore*, 2017 ONCA 182 (Ont. C.A.)**

This case is an interesting one dealing with unjust enrichment and remedial constructive trusts. It should be noted at the outset that leave to appeal has been granted by the Supreme Court of Canada; 2017 CanLII 53388 (S.C.C.).

Here the proceeds of a policy of life insurance on the life of the deceased were at issue. The proceeds were originally designated in favour of the deceased's separated wife and later the deceased's common law spouse. The separated spouse paid the premiums, and thus the facts are somewhat reminiscent of *Richardson Estate v. Mew*, 2009 ONCA 403 (Ont. C.A.). The separated spouse and the deceased agreed orally that the proceeds would go to the wife if she were to maintain the policy, which she did. It is notable that a written separation agreement between the deceased and his wife which post-dated the oral agreement was silent on the question of the policy of insurance. In any case, the later change in beneficiary designation was not surreptitious and was made by the deceased (according to the applicant) to ensure the applicant's support.

The majority of the Court of Appeal, Strathy C.J.O. and Blair J.A., held that the appeal must be allowed as the Application Judge had decided the case based on the application of the doctrine of equitable assignment which was not raised by either side and was not subject of argument. Beyond, on the question of unjust enrichment, the majority held that the separated wife had no interest in the proceeds of the policy arising by way of unjust enrichment but did have a meritorious claim for return of the premiums that she had paid. Blair J.A. provided an overview:[9]

> **Constructive Trust**
>
> [62] I begin this portion of the analysis with the observation that this is not one of those cases – in spite of what it may seem at first impression – where the "equities" are heavily weighted in favour of one party or the other.

[9] 2017 ONCA 182 at Paras. 62-69 (Ont. C.A.).

[63] It is the case that Ms. Moore had an oral agreement with Mr. Moore that if she paid the premiums she would receive the proceeds of the Policy. It is the case that she paid the premiums. And it is the case that Mr. Moore breached the agreement by designating Ms. Sweet as the irrevocable beneficiary under the Policy.

[64] On the other hand, Mr. Moore was a man of limited means, living in the post-separation period on a disability pension, and suffering from the disabilities associated with his physical, mental and substance abuse issues. Ms. Sweet – who is herself disabled – took care of Mr. Moore and, for practical purposes, provided him with a home, a place to live, and a supportive family during the 13 years of their relationship.

[65] There is little, if any, evidence on the record as to Ms. Moore's present financial needs. She continues to live in the former matrimonial home after Mr. Moore's transfer of his one-half interest at the time of separation. Ms. Sweet would appear from the record to be in financial need. Indeed, her evidence is that she was made a beneficiary of the Policy because Mr. Moore wanted to ensure that she would be able to remain in the apartment home that she had occupied for 40 years by the time of his death.

[66] On these facts, it cannot be said that Ms. Sweet is no more than a volunteer who gave nothing in exchange for being named irrevocable beneficiary, or that she is simply the recipient of a windfall. She was a 13-year spouse with heavier than normal caregiving duties (both she and Mr. Moore were disabled in varying degrees) and was the person primarily responsible for the home that they lived in.

[67] On the application, Ms. Moore's position was that she was entitled to the Policy proceeds on the basis of unjust enrichment. On appeal, her approach was more nuanced. She continued to rely on unjust enrichment but embraced the application judge's finding of equitable assignment in support of the claim, as well. She submitted that the application judge was correct in holding that the irrevocable designation of beneficiary provisions in the Insurance Act did not provide a juristic

reason for Ms. Sweet's receipt of the proceeds. In the end, she fell back upon the more expansive view that a constructive trust may be imposed "where good conscience requires it".

[68] I have already concluded that, on the way the case was framed and argued before the application judge and on the record as it currently exists, it is not open for the court to determine whether the oral agreement constituted an equitable assignment. I turn, then, to a consideration of whether the claim for unjust enrichment can otherwise stand or, if not, whether a remedial constructive trust should be found on some other "good conscience" basis in these circumstances.

[69] In my view, Ms. Moore's claim cannot succeed on either basis.

As to the claim in unjust enrichment, the argument fails on the same basis that it did in *Richardson Estate v. Mew*:[10] the beneficiary designation in favour of the common law spouse was an adequate juristic reason to explain why the proceeds should be paid to the designated beneficiary. As to a "good conscience" trusts, Blair J.A. held:[11]

"Good Conscience" Trusts

[100] There has been considerable debate in the jurisprudence and in academia about whether resort to the remedial constructive trust in Canada is now limited to two categories since the Supreme Court of Canada's decision in *Soulos* – unjust enrichment and wrongful acts – thereby eliminating resort to a more elastic "good conscience" trust, i.e., one based on no more than a sense of fairness to the effect that it would be "against all good conscience" to deny a plaintiff recovery in the circumstances of a particular case. At the end of the day, Ms. Moore submits that good conscience is satisfied by giving effect to the oral agreement without which the Policy would not have continued to exist…

[101] It has long been accepted that equity is quintessential never-say-never terrain, and that concepts respecting its application develop with the times and to

[10] 2009 ONCA 403 (Ont. C.A.).
[11] 2017 ONCA 182 at Paras. 100-107 (Ont. C.A.).

meet the needs of particular circumstances. This long-standing principle may work against establishing a completely closed set of categories as the foundation for imposing a remedial constructive trust.

[102] At the same time, McLachlin J. was pretty clear in *Soulos* that, while a constructive trust "may be imposed where good conscience so requires" (para. 34), "[t]he situations which the judge may consider in deciding whether good conscience requires imposition of a constructive trust may be seen as falling into two general categories" (unjust enrichment and situations where property had been obtained by a wrongful act) (para. 36). It was her view that "[w]ithin these two broad categories, there is room for the law of constructive trust to develop and for greater precision to be attained, as time and experience may dictate" (para. 43). Rothstein J. re-affirmed this view in *Professional Institute of the Public Service of Canada v. Canada (Attorney General)*, 2012 SCC 71 (CanLII), [2012] 3 S.C.R. 660, at paras. 144-145.

[103] I do not think it is necessary to resolve this debate for purposes of this appeal.

[104] Most of the authorities in which courts have been willing to override a beneficiary designation can be explained on the basis of an agreement between one of the claimants and the insured that removed the insured's ability to designate a later beneficiary. As noted earlier, Shannon involved a separation agreement in which the insured undertook to name his first spouse as a beneficiary irrevocably. In Bielny, the separation agreement required the insured to name the children of the first marriage as irrevocable beneficiaries. In Fraser v. Fraser, the trial judge found on the facts that the terms of the separation agreement requiring the insured to maintain the plaintiff as beneficiary were tantamount to an irrevocable designation.

[105] Whether these authorities need to be re-examined in light of *Soulos*, as suggested in some authorities – see, for example, *Love v. Love*, 2013 SKCA 31 (CanLII), 359 D.L.R. (4th) 504 – is not something that need be determined here. As I have concluded above, it was not open to the application judge on this record to hold that the oral agreement between the Moores constituted an equitable assignment, or that it was tantamount to an irrevocable beneficiary designation.

> [106] Absent those considerations, I do not see anything in the circumstances of this case that would place it in some other "good conscience" category not caught with the rubric of either wrongful act (not asserted here) or unjust enrichment. For that reason, I do not see the need to resolve the foregoing debate about whether *Soulos* has restricted the categories for imposing a remedial constructive trust to unjust enrichment or wrongful act or whether there remains some additional "good conscience" basis.
>
> [107] Simply because wrongful act is not asserted, and unjust enrichment is unsuccessful, does not mean that some other "good conscience" basis must exist on the facts. To engage in such an exercise, on this record at least, it seems to me, would undermine the rationale for creation of the juristic reason element in the first place.
>
> [Footnote omitted.]

Upon this point, Lauwers J.A. dissented. Justice Lauwers wrote:[12]

> [144] In order to contextualize the ruling in *Soulos*, it is necessary to acknowledge a perennial tension in the common law tradition between, on the one hand, the formal demands of the law as dispensed by the old common law courts, and, on the other hand, the mercies of equity dispensed by the old chancery courts. (Indeed, this tension helps explain some of the differences between my colleague and me.)
>
> [145] The way equity operated is well known. When the common law courts reached a particularly harsh result flowing from the demands of formality and rigorous logic, chancery courts could intervene and mitigate the result in certain circumstances by exercising authority over the defendant's conscience and compelling the defendant not to act on his or her full legal rights.

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[12] 2017 ONCA 182 at Paras. 144-149 (Ont. C.A.).

[146] Law claims the virtues of certainty and predictability, while equity claims the virtues of doing justice and upholding fairness in particular cases. As my colleague observes, the ancient criticism of equity is that its mercies varied arbitrarily with the length of the Chancellor's foot. The fundamental tension lives on, even though law and equity have been fused in Ontario since the late 19th century.

[147] The constructive trust cases show this tension. Judges imposing constructive trusts sometimes cite the magnanimous words of Lord Denning in *Hussey v. Palmer*, [1972] 3 All E.R. 744 (C.A.), who spoke of a constructive trust, at p. 747, as:

[A] trust imposed by law whenever justice and good conscience require it. It is a liberal process, founded on large principles of equity, to be applied in cases where the defendant cannot conscientiously keep the property for himself alone, but ought to allow another to have the property or a share in it.

[148] The tension between the legal and equitable impulses is evident in *Pettkus v. Becker*, 1980 CanLII 22 (SCC), [1980] 2 S.C.R. 834. Dickson J., at pp. 847-848, speaking for the majority, described the attributes of a remedial constructive trust:

The principle of unjust enrichment lies at the heart of the constructive trust. "Unjust enrichment" has played a role in Anglo-American legal writing for centuries. Lord Mansfield, in the case of *Moses v. Macferlan* [(1760), 2 Burr. 1005] put the matter in these words: " the gist of this kind of action is, that the defendant, upon the circumstances of the case, is obliged by the ties of natural justice and equity to refund the money". It would be undesirable, and indeed impossible, to attempt to define all the circumstances in which an unjust enrichment might arise.... The great advantage of ancient principles of equity is their flexibility: the judiciary is thus able to shape these malleable principles so as to accommodate the changing needs and mores of society, in order to achieve justice. The constructive trust has proven to be a useful tool in the judicial armoury. [Citations omitted and emphasis added.]

[149] However, Martland J., in dissent, saw the majority's extension of the constructive trust remedy in Pettkus as undesirable, because he found, at p. 859, that: "It would clothe judges with a very wide power to apply what has been

> described as 'palm tree justice' without the benefit of any guidelines." He then asked: "By what test is a judge to determine what constitutes unjust enrichment?" He answered: "The only test would be his individual perception of what he considered to be unjust." This was what he resisted.

Lauwers J.A. went on to describe the creative nature of equity and a reading of the jurisprudence in the Supreme Court of Canada that should not be read as limiting constructive trusts to wrongs and unjust enrichment. Lauwers J.A. wrote:[13]

> [175] In *Soulos*, McLachlin J. worked through the history of constructive trusts in order to discern whether and how to recognize a remedial constructive trust for wrongful acts, which was the particular problem in the case before her. In my view she did not purport to restate and reframe the law of constructive trusts for all purposes, and she said nothing to close the categories of constructive trusts. Had she intended to abolish good conscience constructive trusts beyond the categories of unjust enrichment and wrongful acts, then one would have expected clear and definitive language to that effect, but there is none. Instead, McLachlin J.'s choice of language justifies the conclusion that the court expected constructive trust law to continue to develop beyond the categories of unjust enrichment and wrongful act.
>
> [176] Justice McLachlin disagreed with the position that a constructive trust cannot be imposed where there has been no unjust enrichment, at para. 16, which was the real issue in the case. She stated, at para. 17:
>
> The history of the law of constructive trust does not support this view. Rather, it suggests that the constructive trust is an ancient and eclectic institution imposed by law not only to remedy unjust enrichment, but to hold persons in different situations to high standards of trust and probity and prevent them from retaining property which in "good conscience" they should not be permitted to retain.
>
> [177] Justice McLachlin made several other pertinent observations of more general application, at paras. 20-22:

[13] 2017 ONCA 182 at Paras. 175-187 (Ont. C.A.).

Canadian courts have never abandoned the principles of constructive trust developed in England. They have, however, modified them.

…

This Court's assertion that a remedial constructive trust lies to prevent unjust enrichment in cases such as *Pettkus v. Becker* should not be taken as expunging from Canadian law the constructive trust in other circumstances where its availability has long been recognized. The language used makes no such claim. A. J. McClean, … describes the ratio of *Pettkus v Becker* as a "a modest enough proposition". He goes on: "It would be wrong ... to read it as one would read the language of a statute and limit further development of the law".

Other scholars agree that the constructive trust as a remedy for unjust enrichment does not negate a finding of a constructive trust in other situations.

[Emphasis added.]

[178] Justice McLachlin also noted, at para. 17, that the law of England and Canada could well be diverging:

In England, the trust thus created was thought of as a real or "institutional" trust. In the United States and recently in Canada, jurisprudence speaks of the availability of the constructive trust as a remedy; hence the remedial constructive trust.

She embarked on a review of English law, noting, at para. 24: "In sum, the old English law remains part of contemporary Canadian law and guides its development."

[179] Justice McLachlin was well aware that English law was evolving. She described the opposition in England to Lord Denning's expansive view of constructive trust, at paras. 30-31. She added, at para. 37, that: "In England the law has yet to formally recognize the remedial constructive trust for unjust enrichment, although many of Lord Denning's pronouncements pointed in this direction." She also surveyed the law in New Zealand and the United States.

[180] Justice McLachlin expressed a critical conclusion, at para. 25:

I conclude that the law of constructive trust in the common law provinces of Canada embraces the situations in which English courts of equity traditionally found a constructive trust as well as the situations of unjust enrichment recognized in recent Canadian jurisprudence.

[181] This led McLachlin J. to the heart of the matter, at paras. 34-35:

It thus emerges that a constructive trust may be imposed where good conscience so requires. The inquiry into good conscience is informed by the situations where constructive trusts have been recognized in the past. It is also informed by the dual reasons for which constructive trusts have traditionally been imposed: to do justice between the parties and to maintain the integrity of institutions dependent on trust-like relationships. Finally, it is informed by the absence of an indication that a constructive trust would have an unfair or unjust effect on the defendant or third parties, matters which equity has always taken into account. Equitable remedies are flexible; their award is based on what is just in all the circumstances of the case.

Good conscience as a common concept unifying the various instances in which a constructive trust may be found has the disadvantage of being very general. But any concept capable of embracing the diverse circumstances in which a constructive trust may be imposed must, of necessity, be general. Particularity is found in the situations in which judges in the past have found constructive trusts. A judge faced with a claim for a constructive trust will have regard not merely to what might seem "fair" in a general sense, but to other situations where courts have found a constructive trust. The goal is but a reasoned, incremental development of the law on a case-by-case basis.

[Emphasis added.]

[182] These statements, in my view, decisively refute the appellant's argument that a court can impose a constructive trust now in only two categories of cases: to remedy an unjust enrichment or a wrongful act.

(5) Concluding Observations on *Soulos*

[186] In my view, the Supreme Court left open four routes by which a court could impose the "ancient and eclectic institution" of a constructive trust: (1) unjust enrichment; (2) wrongful acts or wrongful gain; (3) circumstances where its availability has long been recognized" (para. 21), such as "situations where a constructive trusts have been recognized in the past" (para. 34) or "other situations where courts have found a constructive trust" (para 35); and (4) otherwise, where good conscience requires it. In relation to this last point, the *Soulos* court anticipated that the law of remedial constructive trusts would continue to develop, consistent with the words of Dickson J. in *Pettkus*, at p. 847-848: "the judiciary is thus able to shape these malleable principles so as to accommodate the changing needs and mores of society, in order to achieve justice."

[187] I see no other way to give meaning to the words of McLachlin J. in *Soulos*, at para. 21: "This Court's assertion that a remedial constructive trust lies to prevent unjust enrichment in cases such as *Pettkus* should not be taken as expunging from Canadian law the constructive trust in other circumstances where its availability has long been recognized." See also BNSF Railway Company v. Teck Metals Ltd., 2016 BCCA 350 (CanLII), 89 B.C.L.R. (5th) 274, at paras. 45-55.

[Emphasis in original; footnotes omitted.]

After reviewing some of the jurisprudence on constructive trusts and particularly remedial constructive trusts, Lauwers J.A. held as follows:[14]

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[14] 2017 ONCA 182 at Paras. 265-276 (Ont. C.A.).

Analysis

[265] The disappointed beneficiary cases utilize the rubric of unjust enrichment but gloss over the structural difference. This approach exemplifies the common law's inclination to use old tools for new tasks, even if they do not quite fit. We will always be feeling our way. As McLachlin J. noted in *Soulos* at para. 35: "The goal is but a reasoned, incremental development of the law on a case-by-case basis." That method is part of the genius of the common law.

[266] In managing the deployment of remedial constructive trusts in aid of good conscience, the discipline of particularity is important, as McLachlin J. noted. To repeat her words in para. 35 of *Soulos*: "Particularity is found in the situations in which judges in the past have found constructive trusts." She noted: "A judge faced with a claim for a constructive trust will have regard not merely to what might seem 'fair' in a general sense, but to other situations where courts have found a constructive trust." She saw this careful approach as essential to "a reasoned, incremental development of the law on a case-by-case basis."

[267] I recapitulate the findings that must be made for a court to impose a constructive trust on life insurance proceeds, which have emerged so far in the cases involving disappointed beneficiaries. These serve as limits to discipline judicial discretion. First, the defendant has been enriched and the plaintiff deprived in a family context, not in the market world. Second, the deceased's ruling intent, before resiling, was to benefit the plaintiff. That intent can be found in an oral agreement, a separation agreement or in a court order, but it must comprise an obligation. Third, there is a proprietary link between the plaintiff and the life insurance proceeds. It is this life insurance policy that is in issue, not some other. Finally, providing the plaintiff with the remedy of a constructive trust does not breach any law. Experience with constructive trusts in the disappointed beneficiary context would undoubtedly add other refinements.

[268] The disappointed beneficiary cases represent a distinct type of case in which the constructive trust remedy is disciplined by the common structure and elements of the dispute, which ought to serve to assuage the concern that equity is off on a

frolic of its own, paying no attention to the law. Equity follows the law; the imposition of a constructive trust does not block the law's operation, which in this case is the operation of the Insurance Act; it imposes an obligation in conscience on the appellant the moment her entitlement to the proceeds attaches, one that requires her to hold the proceeds in trust for the respondent.

[269] To my mind, the disappointed beneficiary cases constitute a genus in which a constructive trust can be imposed on life insurance proceeds consistently with the reasoning of McLachlin J in *Soulos*. They are situations in which courts have found a constructive trust.

[270] I do not agree with the appellant's argument that those disappointed beneficiary cases in which the court granted a remedial constructive trust have been overtaken by *Soulos* and are not good law, for several reasons.

[271] First, I am not persuaded by the obiter in *Ladner* and *Love* that the British Columbia Court of Appeal's reasoning in *Roberts* is to be doubted in light of *Soulos*. Neither court explained the basis for the doubt apart from the lack of a mention of *Soulos* in the decisions under review.

[272] Second, I would distinguish *Ladner* itself on two bases. The case proceeded under the rubric of wrongful act, which has a detailed set of elements according to *Soulos* that do not apply to the unjust enrichment rubric. Further, the proprietary connection between the new and old insurance policies that was missing in Ladner was very much present in this case between the policy and the payment of the premiums by the respondent.

[273] Finally, in light of the limits I discussed earlier, I do not share the *Ladner* court's underlying concern that constructive trusts would become unmanageable.

[274] Equity asks a pertinent question in the difficult dilemma posed in the disappointed beneficiary cases: which of the two claimants has the superior claim to the life insurance proceeds? Equity's answer, all things being equal, is to assist the

one with the superior right in equity, as McKinlay J. pointed out in *Shannon*. In this case, that is the respondent, as the application judge found.

(3) Conclusion on Unjust Enrichment

[275] In my view, the application judge did not err in finding that the respondent's deprivation consisted of the life insurance proceeds. He also did not err in finding that the deceased's irrevocable designation in the appellant's favour under s. 191 of the *Insurance Act*, given his prior oral agreement with the respondent, did not provide a juristic reason to oust the availability of a constructive trust over the life insurance proceeds, despite the *Richardson Estate* decision.

[276] But I would go further and add that, to the extent that they fit awkwardly under the rubric of unjust enrichment, the disappointed beneficiary cases are perhaps better understood as a genus of cases in which a constructive trust can be imposed via the third route in *Soulos* – circumstances where the availability of a trust has previously been recognized – and the fourth route – where good conscience otherwise demands it, quite independent of unjust enrichment.

Moore v. Sweet will be a very important decision when it is heard and decided by the Supreme Court of Canada. What divided the majority and dissent in the Court of Appeal goes to the heart of the developing jurisdiction in unjust enrichment and how to approach the development of the remedial constructive trust outside of wrongs and straight-forward unjust enrichment claims. The difficulty, however, may be that the state of the record does not provide adequately to enable one to base the outcome on the nature of the oral agreement between the deceased and the separated spouse. Regardless, it will be interesting to see whether the Supreme Court of Canada sees fit to provide controlling criteria to the use of constructive trusts outside controlling categories.

III. GIFTING

(a) *Jansen v. Niels Estate,* 2017 ONCA 312 (Ont. C.A.)

This appeal concerned an *inter vivos* conveyance by the testator of her home into joint tenancy with her son, daughter-in-law, and herself. The conveyance was challenged after the testator's death by one child on various bases. The judgment on appeal considered whether the joint tenancy had been severed and whether the conveyance was a proper gift. The former ground was dismissed at trial and appeal for want of evidence. The latter ground was dismissed on the basis that there was a good gift notwithstanding that words of gift were not used. In a *per curiam* judgment, the Court held on the latter point:[15]

> [40] The application judge applied the proper test for a gift, as set out in McNamee and summarized in *Foley* [*Foley v. McIntyre*, 2015 ONCA 382 (Ont. C.A.)] at para. 25: "To establish a gift, one must show intention to donate, sufficient delivery of the gift, and acceptance of the gift".
>
> [41] As the application judge noted, it was not necessary for Theadora to state that she was gifting the property. Her intention to gift the property was evident from her instructions to her solicitor and his assistant and the executed documents, all of which supported this finding. This included:
>
> - her advice to her solicitor that she would take title alone and add Richard to the deed later;
> - the codicil to her will, making it clear that the home would not form part of her estate;
> - her request that the joint tenancy between herself and Richard be created on his return to Canada;
> - the absence of any request to revert the title to tenancy in common; and
> - her call to Carol Harding seeking assurance that her home would pass to Richard and Ingrid on her death.

[15] 2017 ONCA 312 at Paras. 40-49 (Ont. C.A.).

[42] Furthermore, the application judge found that Theadora received legal advice from a lawyer who knew her well; that she understood the consequences of joint tenancy as opposed to tenancy in common; and that she was mentally engaged and cognitive until her death.

[43] The application judge did not wrongly rely on evidence of notes documenting Theadora's visit to her lawyer's office in September 2004 and a phone call made to the office in November, 2004, in determining her intention concerning the gift. The application judge's reasons, and in particular para. 148, do not reflect acceptance of the notes on Theadora's visit as evidence of intention. Rather, the notes were part of the narrative explaining the steps that led to title being in the names of Theadora and Richard and the contents of the codicil. This would also help explain why the appellant took no objection at trial to the admission of the notes.

…

Was Theadora Subject to Undue Influence?

[45] Marjolein submits that the application judge erred by, in effect, requiring her to establish undue influence rather than simply demonstrate that the relationship of the parties gave rise to a potential for undue influence.

[46] There is no merit to this submission.

[47] The application judge applied the law as set out in *Foley*, in which this court noted, at para. 28, that the presumption of undue influence applies "[w]here the potential for domination inheres in the relationship between the transferor and transferee", citing *Goodman Estate v. Geffen*, 1991 CanLII 69 (SCC), [1991] 2 S.C.R. 353, at p. 378. Where the presumption applies, the transferee must establish that a gift was the result of the full, free, and informed thought of the transferor. Evidence that the transferor received qualified and independent advice can be used to rebut the presumption, although it is not required in every case. But corroborating evidence is required in order to rebut the presumption, whether direct or circumstantial in nature.

> [48] The application judge applied the presumption that undue influence was exerted, but based on his factual findings concluded, at para. 184, that "the potential for domination and therefore undue influence is completely rebutted." The application judge emphasized the independence of Theadora. He found that her advanced age was not a trigger for domination. This was not a case in which a totally new estate plan had been entered by a person facing a terminal illness. Theadora was pursuing an intention to gift the property that she developed in 2004 and never wavered from. She was cognitively engaged and unfettered by persuasion.
>
> [49] Although the application judge said that Marjolein provided no evidence of undue influence, when his decision is read as a whole, it is clear that he did not reverse the burden of proof and require Marjolein to prove undue influence. On the contrary, the application judge acknowledged the operability of the presumption but found that it was rebutted. As the application judge put it, at para. 179: "Nothing in the evidence causes me any concern that the direction and eventual registration of the tri joint tenancy deed, was done with anything less than the full acquiescence, acceptance and complete concurrence of Mrs. Niels."

While no new ground is broken, the judgment provides comfort that intention to gift remains a question of fact that can be inferred from the evidence and that a caregiver is not precluded from receiving a gift from a frail and vulnerable older adult. The possibility of exploitation may itself raise a presumption of undue influence which was rebutted on the evidence.

(b) *Morreale v. Romanino*, 2017 ONCA 359 (Ont. C.A.)

Here the presumption of undue influence respecting a giuft from an elderly parent to a child was also at issue. The asset was the proceeds of sale of the deceased's home which were then used to purchase another home with title being taken by the deceased's daughter and son-in-law. The deceased was ill with cancer and the daughter and her husband lived with the deceased and provide care services. The deceased did not receive independent legal advice. Gillese J.A. helpfully reviewed the law on point:[16]

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[16] 2017 ONCA 359 at Paras. 19-26 (Ont. C.A.)

1. The Presumption of Undue Influence Did not Arise

[19] At para. 73 of her reasons, the trial judge stated:

I find that in these circumstances, and despite the "special" relationship that existed, it is not possible to find any specific act of coercion or domination that would lead to a presumption of undue influence.

[20] The appellant points to this sentence and submits that it demonstrates an error in law on the part of the trial judge because there is no need for a finding of a "specific act of coercion or domination" in order for the presumption to arise.

[21] I agree. In this regard it is important to distinguish between the presumption of undue influence and actual undue influence. In this case, the trial judge was addressing the question of whether the presumption of undue influence arose, not whether there had been undue influence exerted by the respondent over her parents. There is no need for a finding of a specific act of coercion or dominion in order for the presumption to arise. Whether a person's free will was overborne by an act of coercion or fraud is a question of actual undue influence: *Keljanovic Estate v. Sanseverino* (2000), 2000 CanLII 5711 (ON CA), 186 D.L.R. (4th) 481 (Ont. C.A.), at para. 61.

[22] In the case of voluntary gifts, whether the presumption of undue influence arises begins with an examination of the relationship between the parties and the first question to be addressed, in all cases, "is whether the potential for domination inheres in the nature of the relationship itself": Geffen, at p. 378. This test embraces those relationships that equity has already recognized as giving rise to the presumption, including parent and child: Geffen, at p. 378.

[23] However, while the test embraces relationships that have been recognized as giving rise to the presumption, it is not enough to simply show that such a relationship exists. Even for such relationships, the presumption

> **does not arise unless it has been established that there is the potential for one person to dominate the will of another. The test requires the trial judge to consider the whole of the relationship between the parties to see if there is the potential for domination, rather than looking for a specific act of coercion or domination**.
>
> [24] Despite the impugned statement, in light of the trial judge's findings, I would not interfere with the trial judge's determination that the presumption did not arise in this case. Far from the respondent having the potential to dominate the will of her parents, the trial judge saw Mr. Ruccia as the dominant party in the financial transactions between the Ruccias and the respondent.
>
> [25] The trial judge was very aware of the family dynamic. She recognized that the respondent lived with her parents all of her life and that, as the Ruccias aged, they became more and more dependent on the respondent and, eventually, her husband as well. However, the trial judge found that Mr. Ruccia told the appellant that she would receive less from their estate than would her sister and that he wanted to ensure that her husband would get no money from his estate. And, importantly, the trial judge found that Mr. Ruccia was a strong-willed individual who made all the financial decisions as between him and his wife and that he was so meticulous in respect of his personal financial affairs that he required the respondent to provide him with receipts for all bank transactions that she performed on his behalf.
>
> [26] Given that Mr. Ruccia's mental capacity was not in issue and in light of the trial judge's findings as to the strength of his will in all things, including those financial, the trial judge made no error in concluding that the presumption of undue influence did not arise in this case.
>
> [Emphasis added.]

Thus while a relationship between an adult child providing care to an elderly parent may in some cases give rise to a presumption of undue influence, there is no categorical necessity to presume undue influence where the evidence is to the contrary. Here the evidence would have

rebutted the presumption if it did operate but the refusal to regard it applying categorically operates as a break on frivolous litigation.

(c) *Texeira v. Markgraf Estate*, 2017 ONSC 427 (Ont. S.C.J.)

In the case, the testator wished to gift money to a friend. She prepared a cheque and had her step-son deliver it. The friend cashed the cheque but there were insufficient funds in the testator's account although she had other assets on deposit in the bank. The cheque was returned to the friend; the testator died. Whitten J.. held that this was not a case where the Court ,ay perfect an imperfect gift:[17] "The gift was not perfected. It is not a valid inter vivos gift. This Court, like other Courts, does not have the power to be a financial deity who magically transfers funds to make everything good. The gift is unenforceable." An argument based on estoppel by convention was also rejected.[18]

IV. VALIDITY AND INTERPRETATION OF WILLS & POWERS OF ATTORNEY

(a) *Koziarski v. Sullivan*, 2017 ONSC 2704 (Ont. S.C.J.)

Like *Spence v. BMO Trust Company*,[19] this case raises the question of the Court's ability to interfere with the operation of a Will on grounds of public policy. In the Spence case it was racial discrimination that was at issue. Here it was an outmoded and artificial interpretation of the word "issue" in a Will that does not align with contemporary social policy respecting family structures.

The facts in this case are simple. A 1977 Will provided the following residuary bequest: "[t]o divide the remainder of my estate equally among such of my children as shall be living at the time of my death; provided that if any of my children shall predecease me, leaving issue him or her surviving, such issue shall take in equal shares *per stirpes* the share that such deceased child would have taken if living." The *Succession Law Reform Act* was enacted in 1978 and provided that "a reference to a person in terms of a relationship to another person determined

[17] 2017 ONSC 427 at para. 20 (Ont. S.C.J.).
[18] See *Ryan v. Moore*, 2005 SCC 38 (S.C.C.); *Neuberger v. York*, 2016 ONCA 191 (Ont. C.A.).
[19] 2016 ONCA 196 (Ont. C.A.); leave refused, 2016 CanLII 34005 (S.C.C.).

by blood or marriage shall be deemed to include a person who comes within the description despite the fact that he or she or any other person through whom the relationship is traced was born outside marriage."[20] This reversed the common law rule that "issue" was restricted to children born to a married couple.[21] The statute, however, did not apply to the Wills made after March 31, 1978. Could the Court allow an "illegitimate" grand-child into the class of "issue" on the basis of policy alone?

Justice Gray held as follows:[22]

> [1] In 1824 Burrough J. said the following about public policy: "it is a very unruly horse, and when once you get astride it you never know where it will carry you": see Richardson v. Mellish (1824), 2 Bing. 229, at p.252; 130 E.R. 294, at p.303.
>
> [2] The dictum of Burrough J. is just as valid today as it was in 1824. That is not to say that judges do not make policy choices – they must make policy choices all the time. However, those policy choices are constrained by decisions of higher courts and, most importantly, by policy choices made by the legislature.
>
> [3] In this case, what is raised is the entitlement of a child born out of wedlock to share in an estate. On one level, the policy choice would appear to be obvious – a child born out of wedlock is just as much the child of his or her parents as a child born to married parents. There should be no reason in principle why such a child should be treated differently. However, in this case the court is confronted with a policy choice that appears to have been made by the legislature that is contrary to the intuitive result.
>
> [4] With a good deal of regret, I hold that in this case the respondent, who was a child born out of wedlock, is not entitled to share in the estate of his grandmother.
>
> …

[20] Presently, Section 1(3).
[21] See 2017 ONSC 2704 at Paras. 39-61 (Ont. S.C.J.)
[22] 2017 ONSC 2704 at Paras. 1-4, 63-73 (Ont. S.C.J.)

[63] The conundrum presented by these provisions is apparent: in view of s.1 (4), is it open to the court to apply the presumption spelled out in s.1(3) to wills made before March 31, 1978? With considerable regret, I do not think so.

[64] In the absence of s.1(4), and indeed in the absence of s.1(3), I would have little difficulty in arriving at the same policy choice made by the judges who decided the British Columbia cases. I say that, notwithstanding the authoritative judgment of the Supreme Court of Canada in Millar. One cannot overlook the changes in social norms since the Hill case was decided in 1873, and the Millar case in 1938. For the policy reasons outlined by Laskin C.J.C. in Brule, it makes little sense to construe the word "child" and similar terminology in anything but its ordinary meaning. If the court were free to apply its own notions of public policy, I would have little difficulty construing Jadwiga's will as proposed by Jesse's counsel. While public policy may be an unruly horse, there are times when it can be safely ridden to produce an appropriate result.

[65] However, where policy choices are made by the legislature they must be respected by the courts.

[66] Counsel for Jesse relies on the legislative debates that led up to the enactment of the Succession Law Reform Act in 1978. In my view, those debates actually appear to reflect a deliberate decision to restrict the interpretive change to wills made after March 31, 1978.

[67] When the bill leading to the Act received first reading, it does not appear that the presumption was to apply only to wills made after the effective date of the Act. The Attorney General, the Honourable Mr. Roy McMurtry (as he then was) stated:

By removing the consequences of illegitimacy in inheritance matters, the bill before the House introduces the additional principle of equality between children of a deceased person whether those children were born within or outside marriage.

[68] Prior to second reading of the bill, it appears that there were representations made by a special committee established by the Wills and Trusts Subsection of the Ontario Branch of the Canadian Bar Association. In the course of moving second reading, the Attorney General stated:

Perhaps the most important change that I propose to make at this time is the adoption of the Bar Committee's recommendation concerning s.1. That section would equalize the position of children within or outside marriage for the purposes of estates and would deem all references to a child in a will to include a child born outside the marriage.

Now, the Bar Committee pointed out that there may be many persons who have drawn their wills in reliance on the existing law under which a reference to a child is deemed to include only a child born within marriage. It has been stated that it would put these persons through a great deal of time, trouble and expense to rewrite their wills under the new law. And some of these persons may even, for example, have lost the mental capacity to revise their wills. I should say that I am not convinced, but on balance it perhaps would be fair to restrict the application of s.1 to wills made after the Act comes into force.

[69] It would appear that at the Committee stage, the recommendation of the Bar Committee was accepted, and the bill was amended so that the change in the presumption was to be effective only as of the date the Act came into force, as is now reflected in section 1(4) of the Act.

[70] The amendment was opposed by the Opposition. Mr. Albert Roy (Lib., Ottawa East) said:

We're dealing here basically with illegitimate children. The wise and honoured members of the committee suggested that should be changed and should apply only to wills made after July 1, 1977.

[71] He also stated:

I think the amendment, as contemplated by the hon. members and as proposed by the Attorney General, is in some ways offensive to the whole package of this new legislation, the family property legislation, the Marriage Act and so on, because you know we seek, in Ontario, after this legislation, to legitimize children born out of wedlock. We proceed further to give some status and some obligations and rights to common-law relationships and children flowing from that type of relationship. Yet under this we may be 50 years down the way where we're still saying that certain illegitimate children will be denied because the wills were made before July 1, 1977.

[72] Notwithstanding these concerns, the bill was enacted with s.1(4) included, as it now reads. The prediction made by Mr. Roy has come true. While 39 years have elapsed rather than 50, it remains the case that wills made before the effective date of the Act are treated differently than those made after that date.

[73] In my view, to give effect to the argument of Jesse's counsel would to be read s.1(4) out of the *Succession Law Reform Act*. Notwithstanding the clear intention of the legislature that the change in the presumption should apply only to wills made after March 31, 1978, the change in the presumption would apply to all wills, whether made before or after that date. I know of no principle of law that would allow me to read out of the Act a provision that has been duly enacted by the legislature.

Thus the Application Judge held that his hands were tied. The legislative history made it clear that reading down the language of the statute would be improper given the point was clearly before the legislature. I understand that an appeal has been taken to the Court of Appeal. If the opportunity to consider public policy in *Spence v. BMO Trust Company* was plagued by a sparse evidential record, the circumstances of this case pose no such difficulties. One hopes that the appellate judgment will take advantage of the opportunity to explore the nature of the Court's inherent jurisdiction respecting the supervision of trusts and trustees as well as its statutory jurisdiction in matters of probate to develop the law on this point otherwise a result that surely cannot be rationalized on a basis other than adherence to precedent can be resolved in a more principled manner.

(b) *Vanier v. Vanier*, 2017 ONCA 561 (Ont. C.A.).

This was a contested guardianship case in relation to a 90 year-old lady. The litigants were her two sons and the issues included the validity of a Continuing Power of Attorney made in favour of one son replacing an existing CPOAP naming the two sons jointly and severally. The donor participated in the proceedings to defend the CPOAP. One son alleged that the CPOAP was procured by undue influence. Thus the question became the standard applicable to the application of undue influence to the making of such documents. That is, whether the *inter vivos* approach (looking to presumptions to shift the burden to the party defending the document in certain cases) or the testamentary approach (requiring the party alleging undue influence to provide it) applied. After noting that the issue was presented improperly for the first time on appeal, Epstein J.A. held:[23]

> [38] Raymond submits that the test relied upon by the motion judge, set out above - the test for "testamentary undue influence" - is not the appropriate test for the granting of a power of attorney. The test the motion judge ought to have used is the test for inter vivos equitable undue influence, either actual or presumed. The effect of the inter vivos test would be to shift the onus to Pierre to prove that Rita signed the 2015 CPOAP, willingly and without undue influence.
>
> [39] **Raymond relies on the decision of the House of Lords in *Royal Bank of Scotland v. Etridge (No. 2)*, [2001] UKHL 44, that explains how equity identifies two forms of unacceptable conduct in the context of inter vivos transactions. One involves overt acts of improper pressure or coercion (actual undue influence). The other arises out of a relationship between two people, where one acquires a measure of influence or ascendancy over another, of which the ascendant person takes unfair advantage. The law has long recognized the need to prevent abuse of influence in these "relationship" cases despite the absence of evidence of overt acts of persuasive conduct (presumed undue influence).**

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[23] 2017 ONCA 561 at Paras. 38-39, 50-55 (Ont. C.A.).

…

[50] However, I need not decide whether it is in the interests of justice for this issue to be dealt with, as the inter vivos equitable undue influence test has no application on the facts of this case. **As noted by the House of Lords in *Eltridge*, at paras. 21-22, there are two prerequisites to the evidential shift in the burden of proof from the complainant (Raymond, arguing on behalf of Rita) to the other party (Pierre). First, the complainant reposed trust and confidence in the other party. Second, the transaction is not readily explicable by the parties' relationship. This second part of the test has been held by the House of Lords to mean that the evidence must support a finding that the transaction is "immoderate and irrational".**

[51] In oral argument, Pierre candidly conceded the first part of the test, in other words that Rita reposed trust and confidence in him. However, he submits that Raymond cannot meet the second part, in other words show that the 2015 CPOAP was "immoderate and irrational".

[52] I agree. There is nothing "immoderate or irrational" about the 2015 CPOAP. The record supports a finding that Rita's decision to give the power of attorney to one son over the other was an emotionally difficult but totally rational decision. Rita was very clear in what she said to the police and to Ms. Silverston, none of which evidence was challenged. She knew her money was out of reach. She needed her funds to pay basic expenses such as rent. She understood that Raymond was interfering with her access to the fund and that the solution had to lie with Pierre.

[53] Moreover, far from being "immoderate", the 2015 CPOAP conferred little, if any, benefit on Pierre. He was left with the same power as he had under the 2013 CPOAP. The minor "benefit", if one could call it that, is that the 2015 CPOAP protected Pierre from the stress and inconvenience of Raymond's being in a position to interfere with Rita's finances.

> [54] For these reasons, I am of the view that the motion judge was fully justified in applying the testamentary undue influence test.
>
> [55] I add, that even if the inter vivos equitable undue influence test were applicable, the record does not support a finding of undue influence.
> [Emphasis added.]

While Epstein J.A. did not rule out the use of the *inter vivos* approach, it would appear that the normal disposition of the issue will be through the proof of actual undue influence. One expects that the issue will return before the Court of Appeal sooner rather than later.

(c) *Melendy v. Drodge*, 2017 NLCA 46 (Nfld. & Lab. C.A.)

In this case fraud and undue influence were proved in relation to the making of a Will. The court of first instance held that the bequests do procured were void. On appeal, the factual findings of the trial judge were attacked but so was the remedy. In respect of the latter, Welsh J.A. held that the selection of remedy should leave in place the testator's testamentary intentions which were not affected by the wrongful conduct in place to the extent that it is possible to do so:[24]

> [46] As a general principle, the courts will strive to give effect to a testator's stated intention. The failure of a particular bequest will not result in the will being set aside as a whole, with a consequent intestacy, where such an outcome can be avoided by a proper interpretation of the will. Accordingly, where a gift in a will fails, the property in question will revert to the residue clause, provided that result is consistent with the testator's intention upon a reading of the will as a whole. (See *Feeney's Canadian Law of Wills*, supra, at paragraph 13.32.)
>
> [47] **Where the gift that fails is in the residue clause, it will not be possible to determine the testator's intention regarding that gift since, when the will was executed, the testator believed the residue would be disposed of as**

[24] 2017 NLCA 46 at Paras. 46-52 (Nfld. & Lab. C.A.)

stipulated. The appropriate remedy in such a situation will depend on the particular circumstances, with the object being to give effect to the testator's intention. If possible, effect should be given to gifts that have not failed. (See *Feeney's Canadian Law of Wills*, supra, at paragraph 13.32.)

[48] In this case, the bequests to the Melendys are found only in the residue clause, which provides:

I direct my Trustee to divide the rest and residue of my estate then remaining, both real and personal, of whatsoever kind and wheresoever situate into three equal shares, and to pay one such equal share to each of:

(i) my granddaughter, Lisa Mary Green, of Australia;

(ii) my niece, Judy Melendy, of the City of St. John's, in the Province of Newfoundland and Labrador; and

(iii) my nephew-in-law, Lloyd Melendy, of the City of St. John's, in the Province of Newfoundland and Labrador.

If any of Lisa Mary Green, Judy Melendy or Lloyd Melendy predecease me, but leave issue, then their share of my estate will go to their issue to share and share alike.

[49] There are four possible remedies to consider as a result of the invalidity of the bequests to the Melendys: (1) setting aside the will in its entirety and disposing of the estate on an intestacy; (2) setting aside the residue clause in its entirety and disposing of the whole of the residue on an intestacy; (3) setting aside the bequests to the Melendys and disposing of the property bequeathed to them on an intestacy; and (4) deleting the bequests to the Melendys from the residue, leaving the whole of the residue to Lisa Green.

[50] **These options must be assessed in light of the trial judge's finding that the fraud and undue influence exerted by the Melendys related only to the**

> **bequests to the Melendys in the residue. It did not extend to affecting the testator's independent intentions regarding the specific bequests to the other beneficiaries. In that circumstance, to set aside the will in its entirety would be inconsistent with the general principle that the courts will strive to give effect to a testator's stated intention, and will eschew an intestacy where that can be avoided.**
>
> [51] For the same reasons, the second and fourth options must be rejected. It clearly was Myrtle Kennedy's intention to bequeath one-third of the residue to Lisa Green. Effect can and should be given to that gift. However, it cannot be said that the testator intended that Ms. Green would inherit the residue in its entirely. Two-thirds of the residue, that which was gifted to the Melendys, fails without a disposition under the will. In the absence of a direction by Myrtle Kennedy in that situation, the property gifted to the Melendys must be disposed of on an intestacy. As discussed in *Feeney's Canadian Law of Wills*, supra, at paragraph 13.32:
>
> **… If the property is already part of the residue, it passes on an intestacy unless there is a contrary intention. As the Court of Appeal for British Columbia has made clear, the courts will not manufacture a gift out of the air where the will maker has been silent or ambiguous.**
>
> **[52] Accordingly, I am satisfied that the third option, setting aside the bequests to the Melendys and disposing of the property bequeathed to them on an intestacy, is the proper result in this case.** Applying the *Intestate Succession Act*, RSNL 1990, c. I-21, the net effect is that Lisa Green would be entitled to one-third of the residue plus one-half of the remaining two-thirds of the residue. Tonia Rowe and Nakita Drodge, as children of Myrtle Kennedy's grandson, would each be entitled to one-quarter of the two-thirds of the residue that had been bequeathed to the Melendys.
>
> [Emphasis added.]

While no new ground is broken, the judgment highlights the need for the remedial analysis to avoid a mechanical application of the law in favour of a contextualized one.

(d) *Garwood v. Garwood*, 2017 MBCA 67 (Manitoba C.A.)

What is required of the solicitor who drafts a Will for a visually impaired solicitor and supervises its execution? "[P]roof of a verbatim reading of a Will is not a prerequisite to establishing knowledge and approval. In many cases, it will be sufficient to show that the lawyer summarized and explained the contents of the Will to the testator prior to execution. Ultimately, it is a question of fact as to whether the particular words in question were brought to the attention of the testator and adopted by him as his words."[25]

(e) *Johnston Estate v. Johnsto*n, 2017 BCCA 59 (B.C.C.A.)

Here the British Columbia Court of Appeal held that the duty of care of a solicitor drafting a Will does not extend to beneficiaries under a previous Will, as did Justice Eberhard in *Harrison v. Fallis*, 2006 CanLII 19457 (Ont. S.C.J.). MacKenzie J.A held:[26]

> 33 In *Graham v. Bonnycastle* [2004 ABCA 270], the court undertook a comprehensive review of the existing jurisprudence on solicitor negligence, including *Earl v. Wilhelm* (2000), 189 Sask. R. 71 (Sask. C.A.); and *Worby & Ors v. Rosser*, [1999] E.W.J. No. 3133 (Eng. C.A.). The majority recognized that imposing a duty of care on solicitors in favour of beneficiaries under a former will would create untenable conflicts of interest and make solicitors reluctant to act for elderly testators looking to change their testamentary arrangements. The court declined to impose such a duty, saying:
>
> [31] . . . several decisions have recognized the untenable situation that would be created by extending solicitors' duty of care to include beneficiaries under a former will. <u>Beneficiaries under a former will have other remedies available to them, and may block probate of the will where testamentary capacity is not established.</u> The estate also has a remedy available where it suffers a loss as a result of solicitor negligence. There is no justification for imposing a duty on solicitors taking instruction from a testator for a new will to protect the interests of beneficiaries under a former will. There is not a sufficient relationship of proximity and there are strong

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[25] 2017 MBCA 67 a Para. 22 (Man. C.A.) per Lemaistre J.A.
[26] 2017 BCCA 59 at Paras. 33-39 (B.C.C.A.).

policy reasons for refusing to recognize the existence of a duty. It is not fair, just and reasonable to impose a duty.

[Emphasis added.]

(See also *Harrison v. Fallis* [2006 CarswellOnt 3545 (Ont. S.C.J.)], 2006 CanLII 19457.)

34 I note that in the present case, David is indeed pursuing other remedies including a claim that Norman lacked testamentary capacity.

35 In *Korpiel v. Sanguinetti*, the court considered, among other issues, whether a solicitor owed a duty to beneficiaries named in a client's former will. The plaintiffs in Korpiel were relatives of an elderly testator who had instructed his solicitor to prepare a will bequeathing his home to the plaintiffs; some years later, the testator changed his mind and instructed the solicitor to draft a new will leaving the plaintiffs only a small bequest. The plaintiffs challenged the new will and brought suit against the solicitor for breach of fiduciary duty. Mr. Justice Taylor canvassed the relevant jurisprudence from a number of common law countries. He concluded that it was clear from the case law that solicitors owe no duty to beneficiaries beyond the competent fulfillment of the testator's testamentary instructions. As to the allegation of a breach of fiduciary duty alleged by the plaintiffs, the court said this:

> 37 A fiduciary relationship is determined upon an examination of the nature of the relationship and its characteristics. [As observed] by LaForest J. in *Lac Minerals Ltd. v. International Corona Resources Ltd*., [1989] 2 S.C.R. 574 at 646:
>
> [t]he obligation imposed may vary in its specific substance depending on the relationship, though compendiously it can be described as the fiduciary duty of loyalty and will most often include the avoidance of a conflict of duty and interest and a duty not to profit at the expense of the beneficiary.

> 38 Were a solicitor to conduct herself as proposed by plaintiffs' counsel, it would be impossible to avoid a conflict of duty and interest if the solicitor refused to follow the client's interest and instructions in preference to that of the potential beneficiary at least so far as the interest is concerned. Similarly, this would also occur if the solicitor was to advocate for inclusion of persons or terms of disposition contrary to specific instructions of the client. Such a duty to the public, being those who might potentially be beneficiaries (an indeterminate class of persons), by any measure would clearly result in a conflict of the solicitor's primary duty to his client. It is only in the fulfillment of the duty of care to the client that a resulting duty can be said to be owed to those the client desires to benefit through his testamentary dispositions. Thus, the duty owed to beneficiaries is the duty to properly fulfill solicitor's instructions and where he or she fails, to recompense those who would otherwise benefit.

36 In my opinion, the judge was correct in law when she found David's claims were bound to fail to the extent they were based on a duty owed to him as a beneficiary under a former will. The judge properly considered the decision in *Graham v. Bonnycastle* and was persuaded that a solicitor cannot owe a duty of care to a beneficiary to not take instructions from a testator that might adversely affect the beneficiary's interest.

37 I agree with the reasoning in *Graham v. Bonnycastle* and I would adopt it: there is no justification for imposing a duty on solicitors taking instructions from a testator for a new will to protect the interests of beneficiaries under a former will. To impose such a duty would put the solicitor in an obvious and untenable conflict of interest; the result would be unsustainable and unsupportable at law. As a duty of care is a crucial element of a negligence claim, it was "plain and obvious" David's claims in negligence, based on the duty described, were bound to fail. The judge was correct in concluding that his claim was hopeless in law.

38 Similarly, a claim for breach of fiduciary duty has no prospect of success in the absence of a recognized fiduciary duty. I agree with Taylor J.'s conclusion in

Korpiel that it is only in discharging a solicitor's duty to his client that it can be said that a parallel duty is owed to those persons the client wishes to benefit. In other words, any duty owed by a solicitor to a beneficiary in a will must mirror the duty owed to the testator: the duty to competently fulfill the testator's instructions. Thus, a solicitor cannot owe an independent fiduciary duty to the beneficiary of a will, for, if the testator's instructions were to conflict with the beneficiary's interests, the solicitor would be unable to avoid conflicting duties to both parties.

39 It follows that I would not accede to this ground of appeal.

[Emphasis added expect where indicated.]

V. PROCEDURE

(a) *Seepa v. Seepa*, 2017 ONSC 5368 (Ont. S.C.J.)

Somehow it is always the procedural cases that become important quickly. In a recent decision on a motion for an order giving directions, Justice F.L. Myers was asked to order the conventional relief at the outset of a Will contest – orders for information and records and the like. The decision begins:[27]

The Motion

[1] In the estates court in Toronto motions for directions are routinely brought on consent in will challenges. The fact pattern in these cases is almost always the same. The applicant has been cut out of a will or has been gifted less than he or she believes was due. Of course, the beneficiary who obtains "more" is usually the one who cared for, or at least spent comparatively more time with the deceased. This lets the disgruntled applicant allege, virtually on that basis alone, that the caretaker beneficiary exercised undue influence to induce the deceased to make an unfair distribution of the estate.

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[27] 2017 ONSC at Paras. 1-6 (Ont. S.C.J.).

> [2] The standard form orders for directions routinely granted on consent in these cases consign the parties to lengthy, intrusive, expensive documentary collection and investigation proceedings that can last for the better part of a year or more. The orders are all or nothing. There are few orders that seem to be tailored to the needs of the individual case. Ongoing case management is generally not provided for.
>
> [3] One wonders whether, in the absence of evidence supporting the causes of action and a need for such extensive processes, there is good reason to subject not just the parties but all of the beneficiaries in these cases to the cost, delay, and distress of lengthy proceedings. The disputes delay distribution of bequests to all of the beneficiaries while a disgruntled relative conducts a fishing expedition and often a deep dive through the deceased's privileged legal files and most private, personal medical records.
>
> [4] Is it time for a culture shift?
>
> [5] On May 26, 2017, I declined to sign a consent order for directions in chambers in this matter and required the issues to be argued. In particular, I held that if the parties want to obtain an order of the court, "there must be some evidentiary basis to meet an applicable legal test."
>
> [6] The parties have now argued the issue on the merits. For the reasons that follow the order as requested is granted.

What, then, is the test for "some evidentiary basis"? After reviewing some of the dicta of Gillese J.A. in *Neuberger v. York*,[28] the judge held:[29]

> [27] The issue in this case involves the implementation of the emphasized phrase "some minimal evidentiary threshold." The Court of Appeal recognized that it is simple for a disgruntled relative to make an allegation. If that were enough to

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[28] 2016 ONCA 191 (Ont. C.A.).
[29] 2017 ONSC at Paras. 27-35, 38-40, 49 (Ont. S.C.J.).

cause an estate to go through formal proof in solemn form, smaller estates could be wiped out just by the process alone. That outcome might well serve the goals of the disgruntled relative who can thereby scorch the earth for all of the real beneficiaries. But it is hardly just.

[28] In addition, the law is replete with directives from the Supreme Court of Canada and all levels of courts in Canada concerning the fundamental importance of the confidentiality of the relationship between lawyers and their clients. No privilege at law is given greater protection than the privilege protecting the confidentiality between clients and their lawyers. Similarly no information is more personal and is accorded a higher standing in discussions of privacy law than a person's medial files. While one can have philosophical debates as to whether privilege or confidentiality rights ought to survive a person's death, a court giving voice to a testator's wishes can readily assume that the testator would not happily expose his or her legal and medical files to the relative whom the testator has chosen to exclude from his or her largesse. There is something innately offensive about the idea that an excluded relative can simply romp through a testator's most private legal and health information fishing for evidence on making the most meagre of allegations of impropriety on no real evidence.

[29] On the other hand, the reviewing of privileged or confidential files is not nearly so offensive if one is truly concerned that there may have been some wrongdoing committed against a vulnerable testator. The same facts that make a child the primary caregiver of an elderly parent also give that same child much opportunity for misconduct. Moreover, in the standard fact paradigm, the excluded child or relative has no real way to have personal knowledge of the full facts due to the very exclusion that can point equally and ambiguously to a loving or an abusive relationship between the caregiver and the testator.

[30] No one wants to assume that an adult who cares for a vulnerable person, especially a relative, does so out of ill motive. But motive is not the issue in most cases. In fact, it may well be that the caregiver truly believes himself or herself entitled to extra largesse in light of the extra effort and commitment that he or she has made. Such is the insidiousness of conflict of interest that when faced with a

possibility of personal enrichment, people can rather readily fail to see the ignobility of self-serving misconduct.

[31] Justice Gillese resolved the tension between the difficulty faced by an excluded relative proving undue influence or suspicious circumstances and the risk of an excluded relative subjecting all others to the delay, expense, and inappropriateness of a fishing expedition through private information. She held that the court will only require proof in solemn form where the applicant provides proof of some minimal evidentiary threshold.

[32] Counsel were not able to locate any cases in which this phrase has been considered in light of the goals of the civil justice system or at all.

[33] Justice Gillese provided some further guidance in Neuberger as to how the issue is to be approached. At para. 89, she wrote:

In my view, an applicant or moving party under rule 75.06 must adduce, or point to, some evidence which, if accepted, would call into question the validity of the testamentary instrument that is being propounded. If the applicant or moving party fails in that regard or if the propounder of the testamentary instrument successfully answers the challenge, then the application or motion should be dismissed. If, on the other hand, the applicant or moving party adduces or points to evidence that calls into question the validity of the testamentary instrument which the propounder does not successfully answer, the court would generally order that the testamentary instrument be proved. In determining the manner in which the instrument be proved, the court would have recourse to the powers under rule 75.06(3).

[34] Rule 75.06(3) to which Gillese J.A. refers lists the types of directions that the court may make if it decides to exercise its discretion to require proof of a will in solemn form. Before that happens though, the applicant must “adduce, or point to, some evidence which, if accepted, would call into question the validity” of the will or other testamentary instrument in issue. However, it is not enough that the applicant just adduces or points to something that could call the will into question. As noted by

Gillese J.A., the proponent has the opportunity to answer the evidence adduced or pointed to by the applicant. It is only where the proponent of the will "does not successfully answer" the evidence adduced or pointed to by the applicant, that the court will give directions under Rule 75.06(3).

[35] While the tests are clearly and succinctly set out by the Court of Appeal, there remains much room for uncertainty in their application. What is the standard of proof at play? What does the applicant have to do to answer the minimal evidentiary threshold? Is it enough that the proponent denies the applicant's evidence? In my view, it cannot be enough to just join issue. Issues beg for resolution. Need there be a "genuine issue requiring a trial?" That phrase, of course, is drawn from Rule 20.04 (2)(a) that governs summary judgment. Need a proponent show that he or she would be entitled to summary judgment in order to avoid proof in solemn form? That too cannot be right. At this preliminary stage, the issue is not whether the applicant has proven his or her case but whether he or she ought to be given tools, such as documentary discovery, that are ordinarily available to a litigant before he or she is subjected to a requirement to put a best foot forward on the merits. Normally, a litigant must just plead facts that support a cause of action to become entitled to use the full panoply of fact-finding tools provided by the Rules. In estates cases, more is required. Some evidentiary basis to proceed is required in order to address the specific policy concerns that are discussed above.

…

[38] The rule provides the court with a tremendous breadth of input to shape the proceeding that goes forward. Normally, the identification of parties and issues in litigation is left solely to the parties. The other applicable processes are dictated by the Rules. But civil litigation cases generally are adversarial disputes among the parties. As noted by Justice Gillese, estates cases are more inquisitorial. The court plays an important role because the outcome binds the world and not just the parties. Moreover, the court always maintains its special responsibility to the testator who cannot be present to express his or her own wishes. Therefore, under Rule 75.6(3) the court

exercises discretion as to the very structure of the case that will be heard and decided.

[39] The scope of the court's discretion under Rule 75.06(3) helps to assess the sufficiency of an "answer" to the "minimal evidentiary threshold." I cannot offer much desirable certainty in this case. But discretionary decisions are generally not certain of outcome by definition. In my view, the court ought to measure the evidence adduced by the applicant challenger against the evidence answered by the proponent of the will and assess what, if any, processes are required to resolve any conflicts that the court cannot fairly resolve on the record before it. The court will be guided in making directions, as always, by the primary dictate to fashion a process that provides a fair and just resolution of the civil dispute. A fair and just resolution process is one that is developed to meet the goals of efficiency, affordability, and proportionality that underpin all civil cases as directed by the Supreme Court of Canada in Hryniak.

[40] It must be borne in mind at all times that what is at issue is whether the court should exercise its discretion to require proof in solemn form. The applicant will not likely be able to prove the case on the merits. This is not summary judgment. The question is whether the applicant ought to be able to put the estate and the beneficiaries to the burden of proof, expense, and delay by requiring proof in solemn form and, if so, what process of proof in solemn form will best achieve that outcome, be consonant with the goals of the civil justice system, and recognize the particular concerns that are to be balanced in the estates litigation context.

…

[49] The Court of Appeal decided Neuberger two years into the culture shift heralded by Hryniak. The appellate courts require this court to always be mindful of the goals of the civil justice system so as to implement the law to achieve fair and just outcomes through processes that are efficient, affordable, and especially proportional in light of the facts and circumstances of each case. In my view, the practice under Rule 75.06(3) serves the interests of the parties well when directions are made on a bespoke basis to fit the measurements of the case. Judicial oversight

> through case conferences and case management techniques are available under Rules 75.06(3)(g) and 50.13 among others. The court should be very reluctant to consign estates and beneficiaries to intrusive, expansive, expensive, slow, standard form fishing expeditions that do not seem to be planned to achieve the goals of civil justice for the parties. But processes that show some thought to customize a process to the evidence so as to promote efficiency, affordability, and especially, proportionality, with use of a scalpel rather than a mallet, use of summary proceedings where possible, use of case management, mediation, and similar efforts to minimize the expense, delay, distress, and the overwhelming disruption caused by the process itself, are to be greatly encouraged.
>
> [Emphasis added.]

What results is that counsel must be prepared to deal with the particular issues in the contest early on and lead affidavit evidence that speaks to the need for evidence – in other words, a discovery plan as might be conventional with an action. Indeed, one might well infer that Will contests should proceed by way of action with conventional pleadings and the like, rather than rely exclusively on a Notice of Objection. Certainly a motion for directions will still be required and still require evidence, but the greater level of specificity in conventional pleadings may assist the Court in ensuring that the litigation is not frivolous and the estate in question is not being dragged through court processes to the detriment of beneficiaries and the justice system alike.

(b) *Roulston v. McKenny*, 2017 ONCA 9 (Ont. C.A.)

This is a limitations case. The deceased had a separation agreement with his former spouse obligating him to maintain life insurance on his life in favour of the former spouse else a charge on the assets of the estate would arise in favour of the former spouse. After the deceased's death, his present spouse was appointed Estate Trustee and withheld from the former spouse the fact that life insurance was not maintained by the deceased. More than two years after the

death, the former spouse brought an action on the separation agreement. The Court of Appeal held that the action was not statute based on the doctrine of fraudulent concealment:[30]

> [11] Ms. Roulston submits the application judge made two main errors in applying the doctrine of fraudulent concealment. First, the trial judge erred in finding a special relationship existed between the estate trustee and Ms. McKenny. Second, he erred in finding that the conduct of the estate trustee was such as to attract the operation of the doctrine of fraudulent concealment.
>
> [12] We are not persuaded by either submission.
>
> [13] First, we see no error in the application judge's finding that a special relationship existed between Ms. Roulston, as estate trustee, and Ms. McKenny. In the present case, the special relationship arose from a combination of the duties owed at law by an estate trustee to estate creditors and Ms. Roulston's control over information about any insurance policies owned by the deceased.
>
> [14] The law imposes on estate trustees duties to the deceased's creditors. Property of a deceased that vests in his estate trustee is subject to the payment of his debts: *Estates Administration Act*, R.S.O. 1990, c. E.22, s. 2(1). As a result, one of the fundamental duties of an estate trustee is to ascertain the debts and liabilities owing by the estate and to pay them: Carmen S. Thériault, ed., *Widdifield on Executors and Trustees*, loose-leaf (2011-Rel. 1), 6th ed., (Toronto: Thomson Reuters, 2016), at p. 3-1.
>
> [15] In addition, in the present case information about any insurance policies in place at the time of the deceased's death lay within the control of the estate trustee. Following Mr. Penner's death, counsel for Ms. McKenny wrote to counsel for the estate asking for particulars of any policy of insurance under the separation agreement. Estate counsel responded on June 4, 2013 that the estate trustee was "currently making investigations with respect to the insurance policy." Ms. McKenny's counsel then contacted the insurer, Sun Life Financial, seeking

[30] 2017 ONCA 9 at Paras. 11-16 (Ont. C.A.).

> information about any policy. Sun Life advised it could only release information to the estate trustee and therefore was "unable to confirm the status of any policy [Mr. Penner] may have been insured under."
>
> [16] Ms. McKenny was unable to obtain information about a policy directly from the insurer. Therefore we see no error in the application judge's findings that (i) "the estate trustee had exclusive possession of knowledge and information of whether Ms. McKenny's debt actually existed" and (ii) "since the estate trustee was in a unique and privileged position to obtain information, it was reasonable for Ms. McKenny to rely on what she was being told."

Given that the limitation period arises under the *Trustee Act*, s.38(3), the judgment helpfully confirms the availability of the doctrine of fraudulent concealment and the obligations of an estate trustee to creditors.

(c) *Armitage v. Salvation Army*, 2016 ONCA 971 (Ont. C.A.)

This is another limitations cases, dealing with compensation claims by attorneys. The Court of Appeal held:[31]

> [18] As noted above, the application judge was of the view that the running of the general two-year limitation period under the *Limitations Act, 2002* was triggered on the death of Mr. Wiltse. As the respondent brought the application to pass her accounts within two years of the death of Mr. Wiltse, her claim was not time barred.
>
> [19] While I agree with the result reached by the application judge, I disagree with his conclusion that the *Limitations Act, 2002* had any application in the circumstances of this case. As I will discuss below, in my view, the *Limitations Act, 2002* does not apply because compensation for an attorney for property through the passing of accounts process does not constitute a "claim" within the meaning of the Limitations Act, 2002.

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[31] 2016 ONCA 971 at Paras. 18-29 (Ont. C.A.).

[20] It is useful to briefly consider the nature of compensation for attorneys for property and how the passing of accounts process works. An attorney for property is a fiduciary and has an obligation under s. 32(6) and 38(1) of the SDA to, among other things, keep accounts of all transactions involving the property.

[21] The attorney for property may bring an application to the Superior Court to have his or her accounts approved. Through that process, the attorney for property may also seek court approval of compensation for his or her services. The responding parties to the application have an opportunity to file a notice of objection to the accounts, and to object to the compensation that the attorney for property proposes to take or has taken.

[22] Where the attorney for property has not commenced an application for the passing of accounts, an interested party may bring an application under s. 42(1) of the SDA to compel the passing of accounts.

[23] As noted by Matthew Furrow and Daniel Zacks in their very recent article "The Limitation of Applications to Pass Accounts" (2016) 46 Adv. Q. 2, historically in Ontario there was no statutory limitation period for the passing of accounts. The only bars were the equitable defences of laches and acquiescence. The question becomes whether the enactment of the *Limitations Act, 2002* changed the law and imposed the general two-year limitation period on claims for compensation for attorney for property.

[24] At first blush it would appear that such claims might be captured by the general limitation period. The *Limitations Act, 2002* was designed to comprehensively deal with all manner of civil claims, whether grounded in equity, law, or statute. There are specific carve outs in the legislation for claims that are not subject to the Act. It is arguable, therefore, that if compensation for attorneys for property was intended to be exempted from the general limitation period it would have been specifically exempted under the Limitations Act, 2002.

[25] The difficulty with that argument is that the Limitations Act, 2002 applies only to the assertion of a "claim", and a claim is defined in the Act as follows: "a claim to remedy an injury, loss or damage that occurred as a result of an act or omission."

[26] The appellant submits that the right under the SDA to seek compensation is a new statutory right and, as with all rights, where there is a right there must be a remedy. Further, the appellant argues that the respondent's claim for compensation fits within the statutory definition of a claim. Counsel for the appellant submits that in seeking compensation at this time the respondent has suffered a loss because she chose not to seek self-help and take her compensation earlier. He goes on to argue that this loss is the result of the respondent's omission in failing to claim compensation earlier.

[27] I am unable to accede to this rather circular argument. The fact is that in seeking court approval of the passing of accounts, an attorney for property is not seeking redress for any loss, injury, or damage. Rather, he or she is seeking approval from the court of his or her actions in managing the property, including approval for compensation previously taken or now sought. A passing of accounts application is the opposite of remedial; it is a process that seeks a court order that no remedy is necessary with respect to the accounts: see Furrow and Zacks, at pp. 9-10. Thus, the passing of accounts does not fit within the first part of the Limitations Act, 2002 definition of claim.

[28] An application for the passing of accounts also does not fit within the second part of the statutory definition of claim. Where the definition speaks of an act or omission, it must surely refer to an action taken or not taken by a third party that has the effect of causing loss, injury, or damage. It would be a strange result if a limitation period could not be triggered until the party asserting the claim took an action or omitted to do something.

[29] The result, in my view, is that a passing of accounts under the SDA is not subject to the two-year general limitation period found in the Limitations Act, 2002.[footnote: I do not mean to categorically provide that the *Limitations Act, 2002* has no applicability to the passing of accounts process under the SDA. In particular,

> it may be that the filing by a beneficiary of a notice of objection after an attorney has sought a passing of accounts is a claim within the meaning of the Limitations Act, 2002. However, I leave this determination to another case where it arises directly on the facts.] The common law in that regard was not changed with the enactment of that legislation. Consequently, the only defences available are the equitable defences of laches and acquiescence, neither of which were asserted in the present case.

Notwithstanding that the attorney may seek to pass his or her accounts at any time, the realities of estate administration require the attorney to proceed expeditiously lest the estate's assets be distributed after a suitable time after the notice to creditors is made.

(d) ***Barcham v Barcham*, 2017 ONSC 813 (Ont. S.C.J.)**

The deceased's 1995 Will was admitted to probate in 2009. In 2015, the deceased's brother commenced an application seeking to call-in probate and have a Certificate of Appointment issued in respect of an alleged holographic Will made in 2000. The only real asset of the estate was some real estate which had since been distributed. The brother also had commenced an action in 2012 seeking an interest in the same property based on his alleged equitable interest in funds used to purchase the real estate. The brother asserted that he had known of the holographic Will but did not find it until 2014. He sought to amend his pleadings in the action; the motion to amend was dismissed on the basis that the claim was statute barred for limitations. The action was then discontinued in 2016. Cavanagh J. held that the application for administration of the Estate based on the alleged holographic Will was estopped by virtue of the order of the motion judge in the action:[32]

> [24] The Respondents' submission that the Applicant is impermissibly trying to relitigate a question that was decided by Lederman J. requires consideration of the doctrine of issue estoppel.

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[32] 2017 ONSC 813 at Paras. 24-30 (Ont. S.C.J.).

[25] In *Danyluk v. Ainsworth Technologies Inc*., 2001 SCC 44 (CanLII), [2001] 2 S.C.R. 460, Binnie J. described the rationale underlying the doctrine of issue estoppel, at para.18:

The law rightly seeks a finality to litigation. To advance that objective, it requires litigants to put their best foot forward to establish the truth of their allegations when first called upon to do so. A litigant, to use the vernacular, is only entitled to one bite at the cherry. … An issue, once decided, should not generally be relitigated to the benefit of the losing party and the harassment of the winner. A person should only be vexed once in the same cause. Duplicative litigation, potential inconsistent results, undue costs, and inconclusive proceedings are to be avoided.

In *Danyluk*, Binnie J., citing an earlier Supreme Court of Canada decision in *Angle v. Minister of National Revenue*, 1974 CanLII 168 (SCC), 1974 CanLII 168 (S.C.C.), set out, at paragraph 25, the preconditions to the operation of issue estoppel: (1) the same question has been decided; (2) the judicial decision which is said to create the estoppel was final; and (3) the parties to the judicial decision or their privies were the same persons as the parties to the proceedings in which the estoppel is raised or their privies.

[26] In *Danyluk*, at para. 24, Binnie J. quoted with approval the following passage from the decision in *McIntosh v. Parent*, 1924 CanLII 401 (ON CA), [1924] 4 D.L.R. 420 (Ont. C.A.):

When a question is litigated, the judgment of the Court is a final determination as between the parties and their privies. Any right, question, or fact *distinctly put in issue and directly determined* by a court of competent jurisdiction as a ground of recovery, or as an answer to a claim set up, cannot be re-tried in a subsequent suit between the same parties or their privies, though for a different cause of action. The right, question or fact, *once determined*, must, as between them, be taken to be conclusively established so long as the judgment remains. [Emphasis added [by Binnie J.]]

[27] On the Applicant's motion to amend the statement of claim in the Action, the question of whether the new cause of action founded upon the holographic will, if it were to be advanced in an entirely new statement of claim, would be statute barred was distinctly put into issue and directly decided by Lederman J. He decided that the Applicant had failed to demonstrate that there was even a triable issue of whether the Applicant, by the exercise of reasonable diligence, ought to have discovered the evidence which would support a new cause of action. Lederman J. decided that such a cause of action if advanced in a new action would be statute barred.

[28] This application raises the same question as the one that was decided by Lederman J., that is, whether the Applicant's claims founded upon the discovery of the holographic will are statute barred. The first precondition to the application of the doctrine of issue estoppel is satisfied.

[29] The decision of Lederman J. is, unquestionably, a judicial decision. It is also a final decision. A final decision for the purpose of the doctrine of issue estoppel is a decision which conclusively determines the substantive question between the parties (even though it may not be determinative of the entire action). The decision of Lederman J. conclusively determined whether the new cause of action founded upon the holographic will was statute barred. This decision was not appealed, and is final for the purpose of the doctrine of issue estoppel. The second precondition to the application of the doctrine of issue estoppel is satisfied.

[30] Finally, the parties to the Action are the same persons as the parties to this application, so the third precondition to the application of the doctrine of issue estoppel is also satisfied.

This is an interesting decision that blends limitations and estoppel principles in respect of a not uncommon situation, the finding of a document after an estate is fully distributed said to be a holographic Will. Those interested may also wish to read *Neuberger v. York*, 2016 ONCA 191 (Ont. C.A.) respecting estoppel principles and *Bermingham v. Bermingham Estate* (2007), 32 E.T.R. (3d) 292 (Ont. S.C.J.) respecting "calling in" probate.

VI. TRUSTEES

(a) *Cahill v. Cahill*, 2016 ONCA 962 (Ont. C.A.)

This case deals with the liability of a passive co-trustee who failed to supervise a wrong-doing co-trustee. The wrong was in respect of investment and specifically misappropriating funds in the form of an alleged mortgage on his business premises. The Application Judge found the passive trustee negligent through abdication of her responsibilities as a trustee. Pepall J.A. held:[33]

> [37] The application judge found that Sheila failed to discharge her obligations as an executor and trustee of the estate, because the trust fund for Patrick was never established. The application judge found, at para. 56, that "by her own admission, Sheila had virtually no involvement in the administration of the estate." Sheila had abdicated her duties. Again, the record supports that key finding. The fact that Sheila thought that she was acting responsibly does not excuse her inaction. Doing nothing was not a luxury available to her as a co-trustee. Justification supporting this conclusion is readily available.
>
> [38] First, the will reflects the testator's testamentary intention, and he appointed and entrusted two executors and estate trustees, not one. As the application judge noted, Sheila's appointment as executor and estate trustee reflects the testator's wish that both she and Kevin administer his estate.
>
> [39] Second, an executor or estate trustee is entitled to remuneration for his or her services, either pursuant to the terms of the will or, if the will is silent, under s. 61(1) of the *Trustee Act*. The existence of a statutory entitlement to compensation further demonstrates that an executor or estate trustee's responsibilities are to be taken seriously.
>
> [40] Third, if a party who is named as executor and trustee is unable, unwilling or incapable of accepting the responsibility, it is open to him or her to renounce the

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[33] 2016 ONCA 962 at Paras. 37-41 (Ont. C.A.).

appointment. As Sheila did not renounce the appointment, she was obligated to properly fulfill her duties as executor and estate trustee.

[41] Although the will did provide Kevin with the responsibility for investing the monies in the trust fund, this did not absolve Sheila, as co-trustee, of her responsibility to ensure that the trust fund was properly set up. Further, the testator directed that Patrick's trust fund be divided amongst his grandchildren who are living at the time of Patrick's death. This obligation to divide any remainder of the trust fund among the grandchildren was a continuing one; it bound Sheila and was not confined to Kevin (or his personal representative, should he die).

Pepall J.A. went on to hold that negligence was not reasonable and hence no defence arose in favour of the passive trustee:[34]

[50] The trustee has the burden of proof with respect to the three elements in s. 35(1): (1) that he or she acted honestly; (2) that he or she acted reasonably; and (3) that he or she ought fairly to be excused.

[51] Whether a trustee has acted honestly and reasonably will depend on the facts of the particular case. In *The Law of Trusts*, Gillese J.A. notes, at p. 190, "Generally, the courts have interpreted 'honestly' as an active involvement in the affairs and decisions of the trust administration." Whether a trustee's conduct is "reasonable" is generally determined on the basis of what an ordinary prudent business person would have done in the circumstances.

[52] Courts are to consider a trustee's breach of trust in the light of all of the circumstances. The relevant factors will include whether the breach was technical in nature or a minor error in judgment; whether the trustee was paid; and whether the trustee is a professional: see *Fales* [*Fales v. Canada Permanent Trust Co.*, 1976 CanLII 14 (SCC), [1977] 2 S.C.R. 302], p. 319; Gillese, J.A., p. 191.

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[34] 2016 ONCA 962 at Paras. 50-54 (Ont. C.A.).

> [53] In *Penman* [*The Children's Lawyer v. Penman*, 2013 ONSC 1471, aff'd (sub nom. *Penman (Litigation guardian of) v. Penman*) 2014 ONCA 83 (CanLII), 119 O.R. (3d) 128], at para. 86, the application judge held that the trustee had not acted reasonably:
>
> [The trustee] failed to consider all relevant criteria in determining whether the proposed investments were appropriate; she completely delegated the exercise of her discretion to [her co-trustee]; and she failed to make any reasonable inquiries about the proposed investments or to follow up regarding their status. Section 35 of the *Trustee Act* does not excuse a person who does nothing.
>
> [54] For similar reasons, the application judge in this case found that Sheila did not act reasonably. Sheila made no inquiries and took no steps to fulfill her duties owed to the beneficiaries. The application judge gave extensive and thoughtful reasons and was alert to the factual context. I see no basis on which to interfere with the application judge's decision.

(b) *Craven v. Osidacz*, 2017 ONSC 1757 (Ont. S.C.J.)

This case is painful to have to read. The strict legal issue is the indemnification for legal expenses claimed by an estate trustee in defending claims against the estate, which was denied. The deceased and his spouse were separated. He had been convicted of assault against her. The deceased killed his 8-year old child, forcibly confined his former spouse, and shot to death by the police who intervened to rescue the former spouse. The brother of the deceased was appointed his Estate Trustee and aggressively defended against litigation brought by the former spouse for damages. After settling liability for damages and other claims, Lofchik J. turned to the question of legal fees:[35]

> [63] Michael denies that he acted outside of his duties and was unreasonable in his role as estate trustee, and denies that he should be held personally liable to

[35] 2017 ONSC 1757 at Paras. 63-64, 68-76, 80-86 (Ont. S.C.J.).

repay the legal fees expended to defend the Estate. Further, he denies that he should be personally liable for all legal costs of Julie Craven.

[64] From the total value of the assets of the Estate of $408,912.76 as mentioned above, the Estate has made the following expenditures:

…

> 4. Estate litigation fees: Deborah Ditchfield of Waterous Holden Amey Hitchon LLP was retained by Andrew in and around April 2002 with respect to family law matters between himself and Julie Craven. Upon Andrew's death, Ms. Ditchfield continued to act for the Estate.
>
> In regards to the wrongful death/assaults action, the total amount of legal fees expended by the Estate trustee from the Estate was $71,000.00 with an additional $80,000.00 left owing. The defendant negotiated a reduction to $20,000.00 of these outstanding monies which has now been paid out of the Estate for a total payout of $91,000.00 in legal fees.

...

[68] The general principle that estate trustees are indemnified for all costs including legal fees that are reasonably incurred is codified in s. 23.1 of the *Trustee Act* which reads as follows:

> 23.1 (1) A trustee who is of the opinion that an expense would be properly incurred in carrying out the trust may,
>
> (a) pay the expense directly from the trust property; or
>
> (b) pay the expense personally and recover a corresponding amount from the trust property.

...

(2) The Superior Court of Justice may afterwards disallow the payment or recovery if it is of the opinion that the expense was not properly incurred in carrying out the trust.

[69] From this, I conclude that the executor is entitled, indeed, obliged to defend claims against the estate so long as the estate assets are expended reasonably.

[70] Where the reasonableness of expenses incurred by the trustee is in question, the estate trustee must show that they acted in good faith and had good reason to believe the expenditures were necessary for the benefit of the estate at the time the expense was incurred, and further, has the onus of proving that defending a proceeding is reasonable.

Carmen Theriault, *Widdifield on Executors and Trustees*, 6th Ed. (Toronto: Carswell, 2003), at 4-2.

[71] *Geffen v. Goodman* is the leading case on the role of an estate trustee in covering expenses of the estate, both during administration of the estate and with respect to litigation involving the estate. The court stated:

The courts have long held that trustees are entitled to be indemnified for all costs, including legal costs, which they have reasonably incurred. Reasonable expenses include the costs of an action reasonably defended: see Re Dingman (1915), 35 O.L.R. 51. In *Re Dallaway*, [1982] 3 All E.R. 118, Sir Robert Megarry V.C. stated the rule thus at p. 122:

In so far as such person [trustee] does not recover his costs from any other person, he is entitled to take his costs out of the fund held by him unless the court otherwise orders; and the court can otherwise order only on the ground that he has acted unreasonably, or in substance for his own benefit, rather than for the benefit of the fund.

Geffen v. Goodman Estate, 1991 CanLII 69 (SCC), [1991] 2 SCR 353 at para. 74

[72] It is the plaintiff's position that Michael Osidacz should be personally liable for repayment of the $91,277.98 (plus interest) in legal costs paid to Waterous Holden LLP without a court order.

[73] The courts have held that a trustee may risk the expense of litigation as part of discharging his duties to "collect the assets". However, if there is some question as to whether the proceedings are "meritorious" and whether it is "prudent or appropriate" for a trustee to pursue them, "the appropriate course of action is for the trustee to apply to the court for its directions".

Bank of Nova Scotia Trust et al. v. Pressman et al., 2006 CanLII 22143 (ON SC) at p. 12

[74] In the present case, the Estate trustee never sought directions from the Court concerning whether or not the defences and claims it was advancing were "meritorious" and whether or not it was "prudent or appropriate" to proceed; that is, embarking on a vigorous "tooth and nail" defence or denying significant claims without evidence (even after liability was established).

[75] There is considerable evidence, given Michael Osidacz's interactions with the plaintiff and her family, of significant personal animosity – dare I say hate – between Michael Osidacz and Julie Craven and her family. Such animosity, it would appear, prevented him from exercising the fair and impartial judgment necessary of an estate trustee. Michael Osidacz also appears to have personal opinions about the events of April 2002 and March 18, 2006 contrary to facts found by impartial parties that influenced his judgment and overall approach to the litigation. Thus motivated, Michael Osidacz soldiered on with his agenda of hostility and denial. Viewing the relevant facts objectively, this would seem to be anything but "prudent or appropriate", in clear violation of the principles established in Bank of Nova Scotia Trust et al. v. Pressman et al., 2006 CanLII 22143 (ON SC) at p. 12.

[76] As indicated in *Bank of Nova Scotia Trust et al. v. Pressman et al.*, supra, direction should have been immediately sought from the court as to whether or not the intended path of the estate trustee was "prudent or appropriate", especially

where, as here, the vigorous defence of the litigation was not specified in the will, an aggressive approach to same could (and did) lead to significant expense and circumstances where the estate trustee was both personally and emotionally involved.

…

[80] To incur approximately $160,000.00 in legal fees defending an action that was clearly likely to succeed with virtually no evidence upon which to base the defence was totally irrational and reckless conduct on the part of the Estate trustee, amounting to dissipation of the assets of the overall modest size of the Estate.

[81] Spending tens of thousands of dollars in legal fees advancing frivolous and groundless defences either to see to it that Julie Craven saw no or at least the minimal amount of the assets of the Estate or to prevent personal liability from attaching to Michael Osidacz for legal fees is not a valid basis to “preserve” estate assets and does nothing for the creditors or the beneficiaries of the Estate.

[82] The “modern approach” to awarding estate litigation costs was set out in the decision of McDougald Estate v. Gooderham, 2005 CanLII 21091 (ON CA), [2005] OJ No. 2432 (CA). Essentially, it incorporates the modern “loser pays” approach to awarding costs of litigation as follows: “The modern approach to fixing costs in estate litigation is to carefully scrutinize the litigation and, unless the court finds that one or more of the public policy considerations set out above applies, to follow the costs rules that apply in civil litigation”.

[83] Such approach displaces the “traditional” approach to costs whereby the costs of a proceeding were generally paid out of the estate subject to certain exceptions as follows: “The practice of the English courts, in estate litigation, is to order the costs of all parties to be paid out of the estate where the litigation arose as a result of the actions of the testator, or those with an interest in the residue of the estate, or where the litigation was reasonably necessary to ensure the proper administration of the estate”.

McDougald Estate v. Gooderham, supra

> **[84] Essentially, Michael Osidacz ran up his legal bills to a maximum until he was stopped by an order of this Court. Michael Osidacz exercised dubious judgment at best and generally tried to evade responsibility by shifting blame for most decisions either to the lawyers, or the legal advice received, or to Julie Craven.**
>
> **[85] The fact that Michael Osidacz received legal advice, per se, does not permit him to abdicate his responsibilities as trustee or immunize him from the ultimate decisions made. That is especially where, as here, the decisions he personally made, including raising unnecessary and unsubstantiated defences – such as limitation periods, denying obvious claims and asserting that Julie Craven's injuries were a result of events prior to March 18, 2006, without any evidentiary basis, had enormous consequences resulting in a situation where the Estate trustee essentially used estate funds to bankroll his legal fees and run up a gigantic bill without regard to any of the consequences. I find it would be inequitable to allow Michael Osidacz to have used the assets of the Estate as kind of an ATM machine, from which withdrawals automatically flowed, to fund litigation that was totally unreasonable.**
>
> **[86] Based on the foregoing, it is ordered that there be no indemnity of the legal costs incurred by Michael Osidacz and that he repay to the Estate the sum of $91,277.98, save and except for some limited costs which would be reasonably incurred in relation to the investigation and initial receipt of the claims which I fix at $20,000.00, leaving the amount to be repaid to be $71,277.98.**
>
> [Emphasis added.]

The disposition of the issues in this case seems eminently reasonable.

(c) *Akers v. Samba Financial Group,* [2017] UKSC 6 (U.K.S.C.)

This was an insolvency case involving shares in Saudi Arabian banks valued at approximately USD $318,000,000 which were settled in Cayman Islands bare trusts by their Saudi Arabian owner over a number of years. The beneficiary was a Cayman Islands company owned by the settlor. The company went into liquidation. The shares were transferred to a creditor of the company, Samba. The liquidators of the Cayman Islands company brought proceedings in England to question the validity of the transfer of the shares; the company resisted on the question of jurisdiction. For present purposes, the case is of interest in relation to the recognition of a foreign trust which a domestic court may enforce as a matter of equity and statute.

Lord Mance described the legal issue: "[i]t is now common ground, for the purposes of this appeal, that all six transactions by which Mr Al-Sanea purported to constitute himself a trustee for SICL can be treated as subject to Cayman Islands law. It is also common ground that the law of Saudi Arabia, where the shares are sited, does not recognise the institution of trust or a division between legal and equitable proprietary interests, although it does recognise a different institution, amaana, the precise implications of which have not been explored in evidence."[36] Lord Mance continued, "[i]n the courts below, and when the matter first came before the Supreme Court, the critical issue was identified as being whether SICL had equitable proprietary interests in the shares in respect of which Mr Al-Sanea had purportedly constituted himself trustee. It appears to have been assumed that, if SICL had such interests, then they were disposed of by Mr Al-Sanea's transfer of title in the shares to Samba. Samba's submission was that SICL could have no such equitable proprietary interests, since the law of Saudi Arabia, the *lex situs* of the shares, does not recognise purely equitable proprietary interests."[37]

In exploring the question of jurisidiction, the Supreme Court reviewed a treaty, the *Convention on the Law Applicable to Trusts and on their Recognition*, and its implementation in domestic law through a statute called the Recognition of Trusts Act 1987. The nub of the question emerged as follows:[38]

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[36] [2017] UKSC 6 at Para. 5 (U.K.S.C.).
[37] [2017] UKSC 6 at Para. 8 (U.K.S.C.).
[38] [2017] UKSC 6 at Paras. 17-22 (U.K.S.C.).

17. At common law, the nature of the interest intended to be created by a trust depends on the law governing the trust. This law therefore determines whether the intention is to give a beneficiary an equitable proprietary interest in an asset held on trust or a mere right against the trustee to perform whatever functions the trust imposes upon him with regard to the use and disposal of foreign shares and income derived from them: see Dicey, Morris & Collins, *The Conflict of Laws* (15th ed) (2012), vol 2, para 22-048, citing *Archer-Shee v Garland* [1931] AC 212.

18. Where the intention is to create an equitable proprietary interest, then the common law position is as stated in *Westdeutsche Landesbank Girozentrale v Islington London Borough Council* [1996] AC 669, 705F, per Lord Browne-Wilkinson:

"Once a trust is established, as from the date of its establishment the beneficiary has, in equity, a proprietary interest in the trust property, which proprietary interest will be enforceable in equity against any subsequent holder of the property (whether the original property or substituted property into which it can be traced) other than a purchaser for value of the legal interest without notice."

The initial inquiry is therefore whether an equity subsists, which it will prima facie do at common law, so long as the relevant property (original or substitute) does not pass into the hands of a transferee for value of the legal interest without notice of the equity. But a further issue may arise under the law of the situs of the relevant property.

19. The *situs* or location of shares and of any equitable interest in them is in the jurisdiction where the company is incorporated or the shares are registered (which is presently unimportant, since in this case they coincide in Saudi Arabia): *Dicey*, op cit paras 22-044 and 22-048, Underhill and Hayton, *Law of Trusts and Trustees* (19th ed) para 100.128, both citing *In re Berchtold* [1923] 1 Ch 192, *Philipson-Stow v Inland Revenue Comrs* [1961] AC 727, 762, per Lord Denning.

20. It is established by Court of Appeal authority (and was not challenged on this appeal) that, where under the *lex situs* of the relevant trust property the effect of a transfer of the property by the trustee to a third party is to override any equitable

interest which would otherwise subsist, that effect should be recognised as giving the transferee a defence to any claim by the beneficiary, whether proprietary or simply restitutionary: *Macmillan Inc v Bishopsgate Investment Trust plc (No 3)* [1996] 1 WLR 387. In that case, bona fide chargees for value of shares situated in New York and held on trust for Macmillan were thus able, by application of New York law, to take the shares free of Macmillan's prior equitable interest of which the chargees had had no notice. As will appear, I do not consider that any different position would result under the Convention.

21. That does not mean that a common law trust cannot or will not exist in respect of shares, simply because the lex situs may treat a disposition of the shares to a third party as overriding any interest of the beneficiary in the shares. A trust existed in respect of the shares in issue in *Macmillan v Bishopsgate* until they were disposed of under the *lex situs* by transfer to bona fide purchasers for value without notice. But a common law trust can also exist in respect of shares, such as the Saudi Arabian shares presently in issue, even though Saudi Arabian law does not recognise equitable proprietary interests at all and may not (though this has not been investigated) give any effect at all to a common law trust.

22. A common law court concerned with Cayman Islands trusts in respect of Saudi Arabian shares will give them their intended effect to the greatest extent possible, having regard to the overriding effect of any disposition under their *lex situs*. This is so both at common law and under the Convention. Thus, as between the immediate parties to the present trusts, Mr Al-Sanea and SICL, Mr Al-Sanea cannot deny the validity or effect of the trusts, or assert a right to deal with assets subject to a trust or their proceeds as his own, simply because Saudi Arabian law does not recognise the trusts as giving rise to the separate equitable proprietary interest that would exist if the shares were situated in, say, the United Kingdom or Cayman Islands. If Mr Al-Sanea were to be the subject of bankruptcy proceedings or a receivership in the United Kingdom or Cayman Islands, it is equally clear that his creditors could not claim that the Saudi Arabian shares formed part of his estate in bankruptcy.

> [Emphasis added.]

Thus, notwithstanding the domestic law of Saudi Arabia does not recognize trusts as a matter of law, a trust over the Saudi shares can be recognized and enforced elsewhere. Lord Mance went on to explore the point in considerable detail with reference to a number of relevant decisions. His Lordship then said:[39]

> There is nothing in the Convention to suggest that it was intended to be inapplicable to a trust simply because the trust was in respect of assets in a jurisdiction which does not recognise some form of separation of legal and equitable interests. Rather, the contrary - since one object of the Convention was to provide for the recognition of trusts in jurisdictions which did not themselves know the institution. There must be many common law trusts which have or acquire assets in civil law or other jurisdictions which do not recognise the concept of an equitable proprietary interest in the English common law sense. All that the provisions for recognition of a trust in article 11 of the Convention[40] contemplate, "as a minimum" is "that the trust property constitutes a separate fund". But that does not mean that there must exist a concept of equitable proprietary interest or any separation of legal and equitable proprietary

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[39] [2017] UKSC 6 at Para. 39 (U.K.S.C.).
[40] Article 11 reads:

"A trust created in accordance with the law specified by the preceding Chapter shall be recognised as a trust.

Such recognition shall imply, as a minimum, that the trust property constitutes a separate fund, that the trustee may sue and be sued in his capacity as trustee, and that he may appear or act in this capacity before a notary or any person acting in an official capacity.

In so far as the law applicable to the trust requires or provides, such recognition shall imply in particular -

(a) that personal creditors of the trustee shall have no recourse against the trust assets;

(b) that the trust assets shall not form part of the trustee's estate upon his insolvency or bankruptcy;

(c) that the trust assets shall not form part of the matrimonial property of the trustee or his spouse nor part of the trustee's estate upon his death;

(d) that the trust assets may be recovered when the trustee, in breach of trust, has mingled trust assets with his own property or has alienated trust assets. However, the rights and obligations of any third party holder of the assets shall remain subject to the law determined by the choice of law rules of the forum."

> interests under the lex situs of the relevant assets. The further provisions of article 11 remit to the law governing the trust the further consequences of recognition of a trust. But article 11(d) also recognises that third parties may have acquired rights in respect of trust assets under, in particular, the lex situs of the assets, which may prevent the recovery for the benefit of the trust of trust assets which the trustee has, in breach of trust, alienated. The provision in article 15 that, if "recognition of a trust is prevented" by the application of a provision of the law designated by the conflicts law of the forum which cannot be derogated from by voluntary act, "the court shall try to give effect to the objects of the trust by other means" is a further pointer towards the Convention's general aim of accommodating the institution of trust, so far as possible, with other systems.

While the question of jurisdiction does not arise in relation to most trusts, this judgment is a helpful resource on the question generally.

(d) *Tyrell v. Tyrell*, 2017 ONSC 4063 (Ont. S.C.J.)

This is another case with an international dimension. The testator was domiciled in Nevis. His Will was executed in Nevis and probate taken out over the Will in Nevis. The Estate Trustee and beneficiaries were resident in Ontario and there were assets of the Estate in Ontario as well. Does an Ontario court have jurisdiction to direct the Estate Trustee? Yes. Barnes J. held:[41]

> [12] I conclude that this Court has jurisdiction over matters affecting the administration of the Will. The issue of jurisdiction is resolved on the basis of the distinction between the “validity” of a trust and the “administration” of a trust.
>
> [13] The Respondents did not provide any cogent submissions or any authority for the submission that different common law choice of law (jurisdictional) rules apply to *inter vivos* trusts versus testamentary trusts. The same rules apply in resolving choice of law issues. Choice of law questions are resolved on the basis of the correct characterization of the issue under consideration. Trust issues may be

[41] 2017 ONSC 4063 at Paras. 12-16, 19-21 (Ont. S.C.J.).

characterized as one of formal or essential validity; capacity; revocation; construction; administration; procedure or succession etc.: See Ian M. Hull & Suzana Popovic-Montag, *Macdonell, Sheard and Hull on Probate Practice*, 5th ed (Toronto: Carswell, 2016), at 407. Canadian courts have drawn a distinction between the validity and administration of a trust: *Re Nanton Estate* (1948), 56 Man. R. 71 (Man. K.B.) and *Jewish National Fund*. [*Jewish National Fund v. Royal Trust Co.*, 1965 CanLII 49 (SCC), [1965] S.C.R. 784]

[14] Validity of the trust refers to all matters concerned with a determination of whether a trust is valid. There are two components: a) formal validity and b) essential validity. Formal validity is concerned with matters of form required to create a valid trust. It encompasses such matters as writing, witnesses, validity of signatures, etc. Essential validity refers to validity of the provisions of the trust: for example, capacity of the testator or the settlor and whether the provisions of the trust are permissible in law: see Donovan W.M. Waters, Mark Gillen & Lionel Smith, *Waters' Law of Trusts in Canada*, 3rd ed (Toronto: Carswell, 2005), at 1379.

[15] Administration of the trust refers to all matters relating to the administration or management of the trust. These include powers and obligations of the estate trustee, the distribution of assets, dealing with creditors, etc.: see *Waters' Law of Trusts in Canada*, at 1380; *Probate Practice*, at 410.

[16] The analytical framework for resolving choice of law issues can be summarized as follows: a) determine the correct characterization of the issue; b) determine the jurisdiction that is most "intimately or rationally connected" to the issue; c) determine applicable law of the jurisdiction most "intimately or rationally connected" to the issue; and d) apply the applicable law to resolve the issue or dispute: see *Waters'*, at 1373-1379; *Probate Practice*, at 407-410.

…

[19] A determination of which law applies to matters relating to the administration of the trust is resolved by determining the jurisdiction with the most "substantial connection" to the trust: see *Waters',* at 191-192. The "substantial connection" analysis is fact driven and factors such as the location of the assets, the testator

domicile, location of the beneficiaries and the location of the trustees are all relevant considerations.

[20] The residence or place of business of the estate trustee (administrator) is usually the most important factor in the "substantial connection" analysis because it is the trustee who carries out the business of administering the trust: see *Waters'*, at 191-192; *Branco*, at paras. 19-22 [*Branco v. Veira* (1995), 8 E.T.R. (2d) 49 (Ont. C.J. (Gen. Div.)].

[21] All the substantial assets of the estate are located in Nevis. A few bank accounts are located in Ontario. The testator was domiciled in Nevis. The beneficiaries are resident in Nevis, Ontario and New York. The estate trustee is resident in Ontario. Only the estate trustee is authorized to administer the Will. The estate trustee administers the Will from the province of Ontario. For the purpose of administering the Will, the most significant connecting factor is the residence of the estate trustee. Therefore, the Will is most substantially connected to the province of Ontario and the applicable law on matters relating to the administration of the Will is the law of Ontario. Thus, the Courts of Ontario have jurisdiction over matters relating to the administration of the Will. Therefore, the estate trustee, Janet Tyrell, shall comply with the order previously described

VII. REAL PROPERTY

(a) *Blackmore v. Bower*, 2016 ONSC 6644 (Ont. S.C.J.)

In this case common law spouses separated and then one died. The issue was whether title in a townhouse which had been held in joint tenancy was severed. The severance was said to have occurred by agreement evidenced by emails seemingly approving language in a draft agreement. Justice Pattillo agreed:[42]

[42] 2016 ONSC 6644 at Paras. 55-57, 64-65 (Ont. S.C.J.)

[55] In *Hansen Estate v. Hansen*, 2012 ONCA 112 (CanLII), the Court of Appeal stated at para. 34 that a joint tenancy may be severed in one of three ways:

1. A unilateral act affecting title, such as selling or encumbering the interest;

2. A mutual agreement between the co-owners to sever the joint tenancy; or

3. Any course of dealing sufficient to intimate that the interests of all were mutually treated as constituting a tenancy in common.

[56] The onus of proof rests on the party asserting the severance: McKee v. National Trust Co. Ltd. et al. (1975), 1975 CanLII 442 (ON CA), 7 O.R. (2d) 614 (C.A.).

[57] On the evidence which I accept, I am satisfied that Robert and Mark reached a mutual agreement to, among other things, sever their joint tenancy and create a tenancy in common giving each of them a 50% interest in the Townhouse. The agreement to sever their joint tenancy is clear from their course of dealings from March 2013 onwards and culminating in the July 11 Email.

…

[64] Before me Mark said the July 11 Email was simply asking his lawyer (although he addressed it to Markes) to get in touch with Robert's lawyer to put an agreement together for their review. It was also subject to him getting legal advice. He said the phone call with Robert was short and all that was discussed was getting in touch with the lawyer. He said that the three numbered paragraphs were concepts he really didn't understand. He simply went back to previous drafts and pulled out the concepts.

[65] The plain and unambiguous wording of the July 11 Email along with the prior course of dealings defeats Mark's attempts to otherwise explain it. His reliance on a further draft agreement is not genuine. The terms of the agreement as reflected in the July 11 Email were short and clear. He said: "Put it in writing and we will sign next week." There is no statement requiring further review of the agreement.

The point here is that the severance can be proven in many ways and an informal but settled agreement is sufficient notwithstanding that its formal capture in a written separation agreement had yet to be accomplished.

VIII. REMEDIES

(a) *Easy Loan Corporation v. Wiseman*, 2017 ABCA 58 (Alta. C.A.)

This is a tracing case and accepts, as the Ontario Court of Appeal did *in Re Ontario (Securities Commission) and Greymac Credit Corporation* (1986), 30 D.L.R. (4th) 1 (Ont. C.A.), appeal dismissed [1988] 2 S.C.R. 172, that the 'Lowest Intermediate Balance Rule' is a fair method to determine the entitlements of competing innocents seeking to trace their interests into a mixed fund. The rule states that a claimant to a mixed fund cannot assert a proprietary interest in that fund in excess of the smallest balance in the fund during the interval between the original contribution and the time when a claim with respect to that contribution is being made against the fund.

In this case, the Alberta Securities Commission issued an order freezing a certain companies bank account as it was alleged that the company was operating a Ponzi scheme. Investors applied for an order seeking declaration of a trust over the funds in their favour. The Court held:

> **III. Grounds of Appeal and Standard of Review**
>
> [17] It is important to emphasize that there is no appeal of the chambers judge's imposition of the constructive trust. No notice of appeal was filed by the receiver and counsel for the receiver confirmed at the hearing of the appeal that there was no appeal of that finding.
>
> …
>
> [20] The sole ground of appeal is in relation to the methodology used to trace the Frozen Funds. The appellant submits the chambers judge erred in law by holding that a pro rata sharing on the basis of tracing to the lowest intermediate balance in the account is the 'general rule' unless it is practically impossible, and

that the chambers judge failed to consider the intention of the beneficiaries to hold commingled funds as co-owners in the mortgage investment.

…

Tracing Rules and Principles

[28] Three methods are available to trace commingled trust assets on deposit in a bank account. They are: (i) the rule in *Clayton's Case*; (ii) the lowest intermediate balance rule, also referred to as "pro rata on the basis of tracing", the "North American method", "rolling charge method" or "LIBR" ("LIBR"); and (iii) the *pro rata* approach, also referred to as the "basic *pro rata* approach", "*pro rata ex post facto*" or "*pari passu ex post facto*" ("Proportionate Distribution").

[29] The following general equitable principles apply.

[30] First, "modern [tracing] rules ... have been ... altered, improved, and refined from time to time": *Re Hallett's Estate* at 710 per Jessel MR. And, "equity's ... flexible remedies such as constructive trusts, ..., tracing ... must continue to be moulded to meet the requirements of fairness and justice in specific situations": *Canson Enterprises Ltd. v Boughton & Co*., 1991 CanLII 52 (SCC), [1991] 3 SCR 534, 85 DLR (4th) 129 at 538. The significance of this principle will be apparent shortly, in the context of the applicability of the rule in *Clayton's Case*.

[31] Second, the overarching goal of equity is "to serve the ends of fairness and justice": *Canson* at 586 per LaForest J. When tracing into a commingled bank account that contains only trust funds, fairness of distribution is paramount. Balanced against fairness is a more pragmatic consideration: practicality and workability. "A rule that is in accord with abstract justice but which, for one or more reasons, is not capable of practical application, may not, when larger considerations of judicial administration are taken into account, be a suitable rule to adopt": *Ontario (Securities Commission) v Greymac Credit Corp (1986)*, 55 OR (2d) 673, 17 OAC 88 at para 48, affirmed 1988 CanLII 5760 (SCC), [1988] 2 SCR 172.

The Rule in Clayton's Case

[32] The *Rule in Clayton's Case*, also known as the "first in, first out" rule deems that funds deposited first into a commingled account are also the first funds withdrawn. The rule has been called "unfair, arbitrary, and based on a fiction": *Boughner* at para 81; see also *Greymac*.

…

[34] However, given the equitable tracing principles set out above and the parties' agreement that the rule in Clayton's Case did not apply in the present circumstances, we proceed on the basis that the rule in Clayton's Case has no application here. This leaves two other distribution methods.

Proportionate Distribution

[35] Proportionate Distribution divides the final balance in the commingled account in proportion to each claimant's original contribution to the fund. In other words, contributors share the shortfall in the account. An open question is whether set-off should apply against an investor's contribution as a result of funds the investor received from a return on capital, dividends, bonuses, etc. Given our conclusion that this is not the tracing method to use in these circumstances, there is no need to address set-off.

…

LIBR

[37] LIBR considers each beneficiary's contribution to the commingled account and the lowest balance in the account after each beneficiary's contribution. Simply put each beneficiary loses the ability to trace (and therefore claim) its contribution once the funds in the account drop below the amount of the beneficiary's contribution (deposit).

[38] A simple example: if X deposits $100 to a commingled account and the balance in the account later drops to $5, the most X can claim is $5, the lowest

balance in the account; the ability to trace to anything more than $5 is lost because anything more comes from a funding source other than X. “Intermediate” refers to the period between X’s contribution and when X makes the claim against the account. Once the lowest intermediate balance is determined for each beneficiary, each beneficiary is entitled to claim only the lowest balance’s proportional share of the final balance of the account.

[39] *Law Society of Upper Canada v Toronto-Dominion Bank* (1998), 1998 CanLII 4774 (ON CA), 42 OR (3d) 257, 116 OAC 24 (“LSUC”) at para 14 explains:

a claimant to a mixed fund cannot assert a proprietary interest in that fund in excess of the smallest balance in the fund during the interval between the original contribution and the time when a claim with respect to that contribution is being made against the fund.

[40] It is self-evident that calculating the lowest balance in the account for each beneficiary’s contribution is not workable or practical if the commingled account has many contributors, supporting records are unavailable or incomplete or the timeframe in question is lengthy. These problems do not arise in this case.

[41] Indeed, the proof is in the pudding. Counsel for one of the respondents calculated the lowest intermediate balance for each beneficiary and the proportion that each balance comprised of the Frozen Funds, all to the satisfaction of the chambers judge who personally signed the Order. No respondent disputes the amount.

In this case, the Court held that the LIBR was applicable and should be applied. It was neither unworkable or contrary to the intentions of the beneficiaries (investors). As such, the Court held this method would be a fair one to determine the interests of the bilked investors in the funds available.

IX. RECTIFICATION

(a) *Canada (Attorney General) v. Fairmont Hotels Inc.*, 2016 SCC 56 (S.C.C.)[43]

Canada (Attorney General) v. Fairmont Hotels Inc. is an important case. Here Fairmont owned a minority interest in Legacy Hotels REIT, a Canadian REIT. In 2002, Legacy wished to purchase American two American hotels and Fairmont agreed to finance the transactions through two subsidiaries, FHIW Hotel Investments (Canada) Inc. and FHIS Hotel Investments (Canada) Inc. One point in the loan was the treatment of foreign currency and the potential for Fairmont to pay foreign exchange tax given that the loans were to be in American dollars and market fluctuation could result in a taxable increase in value. Fairmont wanted to structure the loans to ensure tax neutrality. However, when Fairmont was acquired by another company the next year. This triggered foreign exchange tax liability for Fairmont and its two subsidiaries. A plan was considered to unwind the loan agreements and abandoned. Notwithstanding, by mistake, an officer of Fairmont believed that the plan was acted upon and redeemed some preference shares in the two subsidiaries resulting in a taxable gain. Could the decision to redeem the shares be rectified? No.

Justice Brown, for the majority, wrote a lengthy judgment on the law of rectification and held that it must be reigned in to some extent. Justice Brown wrote:[44]

> **[13] Because rectification allows courts to rewrite what the parties had originally intended to be the final expression of their agreement, it is "a potent remedy"** (*Snell's Equity* (33rd ed. 2015), by J. McGhee, at pp. 417-18). It must, as this Court has repeatedly stated (*Shafron v. KRG Insurance Brokers (Western) Inc.,* 2009 SCC 6 (CanLII), [2009] 1 S.C.R. 157, at para. 56, citing *Performance Industries Ltd. v. Sylvan Lake Golf & Tennis Club Ltd.*, 2002 SCC 19 (CanLII), [2002] 1 S.C.R. 678, at para. 31), **be used "with great caution", since a "relaxed approach to rectification as a substitute for due diligence at the time a document is signed would undermine the confidence of the commercial**

[43] The companion case of *Jean Coutu Group (PJC) Inc. v. Canada (Attorney General)*, 2016 SCC 55 (S.C.C.), considered the same issue under Article 1425 of the *Civil Code of Québec*, CQLR c CCQ-1991 ("The common intention of the parties rather than adherence to the literal meaning of the words shall be sought in interpreting a contract.").
[44] 2016 SCC 56 at Paras. 13-15, 32, 34-37 (S.C.C.).

world in written contracts": *Performance Industries*, at para. 31. It bears reiterating that **rectification is limited solely to cases where a written instrument has incorrectly recorded the parties' antecedent agreement** (Swan and Adamski, at §8.229). **It is not concerned with mistakes merely in the making of that antecedent agreement**: E. Peel, *The Law of Contract* (14th ed. 2015), at para. 8-059; *Mackenzie v. Coulson* (1869), L.R. 8 Eq. 368, at p. 375 ("Courts of Equity do not rectify contracts; they may and do rectify instruments"). **In short, rectification is unavailable where the basis for seeking it is that one or both of the parties wish to amend not the instrument recording their agreement, but the agreement itself. More to the point of this appeal, and as this Court said in *Performance Industries* (at para. 31), "[t]he court's task in a rectification case is . . . to restore the parties to their original bargain, not to rectify a belatedly recognized error of judgment by one party or the other".**

[14] Beyond these general guides, the nature of the mistake must be accounted for: Swan and Adamski, at §8.233. **Two types of error may support a grant of rectification. The first arises when both parties subscribe to an instrument under a common mistake that it accurately records the terms of their antecedent agreement**. In such a case, an order for rectification is predicated upon the applicant showing that the parties had reached a prior agreement whose terms are definite and ascertainable; that the agreement was still effective when the instrument was executed; that the instrument fails to record accurately that prior agreement; and that, if rectified as proposed, the instrument would carry out the agreement...

[15] In *Performance Industries* (at para. 31) and again in *Shafron* (at para. 53), this Court affirmed that **rectification is also available where the claimed mistake is unilateral — either because the instrument formalizes a unilateral act (such as the creation of a trust), or where (as in *Performance Industries* and *Shafron*) the instrument was intended to record an agreement between parties, but one party says that the instrument does not accurately do so, while the other party says it does.** In *Performance Industries* (at para. 31), "certain demanding preconditions" were added to rectify a putative unilateral mistake: specifically, that the party resisting rectification knew or ought to have

known about the mistake; and that permitting that party to take advantage of the mistake would amount to “fraud or the equivalent of fraud” (para. 38).

…

[32] **It therefore falls to a party seeking rectification to show not only the putative error in the instrument, but also the way in which the instrument should be rectified in order to correctly record what the parties intended to do. “The court’s task in a rectification case is corrective, not speculative”: *Performance Industries*, at para. 31. Where, therefore, an instrument recording an agreed-upon course of action is sought to be rectified, the party seeking rectification must identify terms which were omitted or recorded incorrectly and which, correctly recorded, are sufficiently precise to constitute the terms of an enforceable agreement. The inclusion of imprecise terms in an instrument is, on its own, not enough to obtain rectification; absent evidence of what the parties had specifically agreed to do, rectification is not available.** While imprecision may justify setting aside an instrument, it cannot invite courts to find an agreement where none is present. It was for this reason that the Court in *Shafron* declined to enforce the restrictive covenant covering the “Metropolitan City of Vancouver”. The term was imprecise, but there was “no indication that the parties agreed on something and then mistakenly included something else in the written contract”: *Shafron*, at para. 57.

…

[34**] The second point requiring clarification is the standard of proof. In Performance Industries, at para. 41, this Court held that a party seeking rectification will have to meet all elements of the test by “convincing proof”, which it described as “proof that may fall well short of the criminal standard, but which goes beyond the sort of proof that only reluctantly and with hesitation scrapes over the low end of the civil ‘more probable than not’ standard”…**

[35] In light, however, of this Court’s more recent statement in *F.H. v. McDougall*, 2008 SCC 53 (CanLII), [2008] 3 S.C.R. 41, at para. 40, that there is “only one civil standard of proof at common law and that is proof on a balance of probabilities”, the question obviously arises of whether the Court’s description in

Performance Industries of the standard to which the elements of the test for obtaining rectification must be proven is still applicable.

[36] **In my view, the applicable standard of proof to be applied to evidence adduced in support of a grant of rectification is that which *McDougall* identifies as the standard generally applicable to all civil cases: the balance of probabilities. But this merely addresses the standard, and not the quality of evidence by which that standard is to be discharged.** As the Court also said in *McDougall* (at para. 46), “evidence must always be sufficiently clear, convincing and cogent”. **A party seeking rectification faces a difficult task in meeting this standard, because the evidence must satisfy a court that the true substance of its unilateral intention or agreement with another party was not accurately recorded in the instrument to which it nonetheless subscribed. A court will typically require evidence exhibiting a high degree of clarity, persuasiveness and cogency before substituting the terms of a written instrument with those said to form the party’s true, if only orally expressed, intended course of action.** This idea was helpfully encapsulated, in the context of an application for rectification of a common mistake, by Brightman L.J. in *Thomas Bates and Son Ltd. v. Wyndham’s (Lingerie) Ltd.*, [1981] 1 W.L.R. 505 (C.A.), at p. 521:

The standard of proof required in an action of rectification to establish the common intention of the parties is, in my view, the civil standard of balance of probability. But as the alleged common intention ex hypothesi contradicts the written instrument, **convincing proof is required in order to counteract the cogent evidence of the parties’ intention displayed by the instrument itself. It is not, I think, the standard of proof which is high, so differing from the normal civil standard, but the evidential requirement needed to counteract the inherent probability that the written instrument truly represents the parties’ intention because it is a document signed by the parties**.

[37] In brief, while the standard of proof is the balance of probabilities, the essential concern of *Performance Industries* remains applicable, being (at para. 42) “to promote the utility of written agreements by closing the

> 'floodgate' against marginal cases that dilute what are rightly seen to be demanding preconditions to rectification".

The take-away from *Fairmont* is a return to a more traditional approach to rectification with a very limited scope for rectification where a particular act has been taken on the strength of professional advice; only errors in recording the action intended may be rectified rather than the substantive decision being, in essence, rescinded. "Rectification is not equity's version of a mulligan."[45]

(b) *McLauglin v. McLaughlin*, 2016 ONCA 899 (Ont. C.A.)

In this case a rectification order was successfully obtained in relation to the testator's primary Will. The secondary Will contained a number of errors including a revocation clause. The Application Judge on his own initiative held the secondary Will inadmissible to probate undercutting the rectification order made by another judge. The Court of Appeal held that the rectification order implicitly applied to the secondary Will and that it was admissible to probate.

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[45] 2016 SCC 56 at Para. 39 (S.C.C.)

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TAB 2

Estate Administration Tax Issues

Lori Duffy
WeirFoulds LLP

DAY TWO
October 17, 2017

cpd Continuing Professional Development

ESTATE ADMINISTRATION TAX ISSUES

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Background

Approximately 25 years ago Ontario probate fees, as they were then called, were almost tripled and "probate planning" became an important element of what estate planners did. As a result and not surprisingly, the revenues generated by the collection of probate fees did not result in the increased revenues expected by the provincial government.[1]

After the increase in probate fees in 1992, the Ontario government was faced with a number of law suits challenging the legality of this fee.

In 1994, Marie Sarah Eurig, as executor of her deceased husband's estate, applied for an order that she be granted letters probate without payment of the probate fee arguing that the probate fee was not lawful as it was not a fee but an indirect tax which was unconstitutional.

On October 22, 1998, the Supreme Court of Canada agreed with Mrs. Eurig, concluding that Ontario's probate fee was a tax, not a fee though they did not agree that it was an indirect tax.[2] On December 18, 1998, Royal Assent was given to the *Estate Admission Tax Act*, *1998*,[3] (the "**EATA**") which had the effect of retroactively establishing probate fees as taxes. Although it was now a tax, the payment was still collected by the offices of the Attorney General.

The EATA was amended on May 12, 2011, giving the Minister of Revenue (now the Minister of Finance), the ability to audit the collection of the Estate Administration Tax (the "**EAT**"). Of course, it is difficult to audit a tax if a form of tax return is not filed and accordingly, the Estate Information Return (the "**EIR**") was created by this legislation.

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[1] Barry A. Corbin has researched and written extensively on this issue. See "Estate Administration Tax – The Nightmare Begins", Ontario Bar Association "Deadbeat", May 2011, Vol. 29, No. 4.
[2] *Re Eurig Estate* [1998] 2 S.C.R. 565.
[3] *Estate Administration Tax Act, 1998*, S.O. 1998, c.34 Sched. as am.

The proposed legislation had many issues, partly due to the fact that it incorporated by reference the provisions of the *Retail Sales Tax*[4], to govern the procedures for the collection of the EAT. The legislation became effective on January 1, 2015, forty-three months after its introduction.[5]

The New "Regime"

As noted above, by incorporating the provisions of the *Retail Sales Tax Act* (the "RST") rather than drafting specific provisions for the collection of the EAT, some manipulation of the provisions was required to make it applicable to Estates and Estate Trustees. As a result, the EATA provides that a tax payable by a purchaser under the RST is the tax payable by an estate under the EATA and the amount remitted by a vendor under the RST is the amount payable by an estate representative under the EATA.

The definition of "estate representative" is found in section 1. (1) of the EATA and includes an executor, administrator, estate trustee with a will, estate trustee without a will, and a guardian of a person who is a beneficiary of the estate or as a guardian of the beneficiaries property.

The same section provides the definition of an "estate certificate" which includes a grant of probate and a certificate of appointment of estate trustee. It does not include a certificate of succeeding estate trustee or a certificate of estate trustee during litigation.

The legislation requires that an Estate Information Return (the "EIR") be received by the Ministry of Finance within 90 calendar days of the issuance of the Estate Certificate. It may be sent by mail, courier, fax or by email. If the estate representative subsequently discovers property owned by the deceased but not included in their application for appointment as estate

[4] *Retail Sales Tax Act,* R.S.O. 1990, c. R.31
[5] See also – WeirFoulds Estates & Trust Newsletter – Westlaw & Carswell, May 2011 ESLNWS 2011 and ESLNWS 2014 and ESLNWS 2015-01.

representative and not included in the EIR, they must file an amended EIR within 30 days after the revised statement is filed with the Courts pursuant to section 32 (2) of the *Estates Act.*[6]

The Ministry may assess or audit the return within a four year period from the date of the last filed EIR. There are limited exceptions to the requirement to file. No Estate Information Return is required to be filed if the estate certificate is one of the following:

1. Certificate of Appointment of Succeeding Estate Trustee with a Will;
2. Certificate of Appointment of Succeeding Estate Trustee with a Will limited to the assets referred to in the will;
3. Certificate of Appointment of Succeeding Estate Trustee without a Will; and,
4. Certificate of Appointment of Estate Trustee during Litigation.

Should an estate representative fail to file an EIR they may be subject to a fine of at least $1,000.00 and up to twice the amount of the EAT payable or imprisonment up to two years, or both the fine and imprisonment.

<u>Required Information in Completing the EIR</u>

The EIR requires that each asset owned by the deceased person be reported and given a value. The EATA defines the "value of the estate" as the value which is required to be disclosed under section 32 of the *Estates Act* of all the property that belonged to the deceased person at the time of their death less the actual value of any encumbrance on real property that is included in the property of the deceased person.

Section 32(1) of the *Estates Act* provides that the "person applying for a grant of probate or administration shall before it is granted make or cause to be made and delivered to the Registrar a true statement of the total value, verified by the oath or affirmation of the

[6] Estates Act, RSO 1990, cE21

applicant, of all the property that belonged to the deceased at the time of his or her death." Subsection 2 provides that when after the grant of probate or letters of administration, any property "belonging to the deceased at the time of his or her death and not included in such statement of total value is discovered by the Executor or administrator, they shall, within six months thereafter, deliver to the Registrar a true statement of the total value, duly verified by oath or affirmation, of such newly discovered property.[7] These two sections provide the guidelines for completing the EIR. However, the broadness of these sections requires estate representatives to consider whether an asset was actually owned by the deceased person, and if so, what is the appropriate method to determine its value. It can be challenging to determine whether an asset was owned by the deceased "at the time of their death". We have construed that as being the value of the asset at the end of the day of death however, that still can result in questions about whether an asset should be included. By way of example, the following are some assets that we have had considerable discussion on whether they are subject to EAT and therefore included in the EIR.

1. CPP Death Benefit.

As the death benefits are payable as a result of the death of the recipient, we have always taken the position that the death benefits are received after death and not included in the total value for EAT purposes. The Ministry of Finance website now agrees with this position.

2. Life Insurance payable to the Estate of the deceased

Given the position with respect to the CPP death benefit, one might have thought that proceeds payable to an Estate as a result of the death of the deceased person would not be

[7] Note that depending on when the subsequently discovered property is found, an EIR may not be required and the applicable EAT to be paid should be calculated by the rates applicable at the time the estate certificate was obtained. See subsection 2 (5) of the EATA.

subject to, and not included in the total value for EAT purposes. The Guide[8] published by the Ministry of Finance disagrees and states that insurance contracts with a residual amount payable to an estate (i.e., without a named beneficiary) is subject to EAT.

3. Jointly owned property

The Guide is clear that you are not required to include items that pass outside of the estate such as assets which are jointly owned with a right of survivorship with other parties. You are required however, to include any property in which the deceased had a beneficial interest, even if the deceased did not hold title. This leads to some very difficult determinations by the estate representative. Given the Supreme Court of Canada decision in *Pecore v Pecore*,[9] and the many cases that have followed and applied this decision, the issue of joint ownership is a difficult one and may present a challenge for the estate representative. The estate representative will need to determine what was the intention of the deceased person when the joint ownership was established. Did they intend to gift an interest of all or part of the property or is the "joint owner" essentially holding an interest in trust for the deceased person? Did they have intent at the time of the establishment of the joint ownership that the other person would have a beneficial interest in or a right of survivorship of the property? In meeting with our estate representative clients, they often look to us for guidance as to how to determine the intention of the deceased with respect to joint ownership. As will be discussed later in this paper, if the estate representative is satisfied that the deceased did intend to gift the right of survivorship when the joint ownership was established, they may still be required to provide to the Ministry details of all assets that were jointly held and the basis upon which the estate representative determined that it was joint ownership with right of survivorship.

4. Real Property

It is clear that real property owned in Ontario must be included on the Estate Information Return and valued. When the 2011 amendments to the EATA were first issued

[8] http://www.forms.ssb.gov.on.ca/mbs/ssb/forms/ssbforms.nsf/FormDetail?OpenForm&ENV=WWE&NO=9955E
[9] [2007] 1 SCR 795, 2007 SCC 17 (CanLII)

reference was made to the requirement to state the "appraised value" of real property. In subsequent meetings with Ministry of Finance representatives, they made it clear that a formal appraisal by a certified appraiser may not always be required and that letters of opinion in certain circumstances may be satisfactory. They have also indicated that reference to MPAC values may assist but may not represent the fair market value at the date of death. If the estate representative advises that the property was in fact jointly owned only to assist in the administration of the property and that a right of survivorship was not intended, then a determination would have to be made as to whether or not the whole of the property was owned by the deceased person or in fact was some percentage interest intended to be granted and if so how is this determined. If the deceased owned a percentage interest in real property such as a 40% interest as tenant in common with another co-owner, are we able to apply a discount for that minority interest? It would likely be difficult to sell such a minority interest to a third party, however, the Ministry has taken the view that it should be a straight percentage of the fair market value of the property with no discount.

The legislation has always provided that where real property is subject to a mortgage, the amount of mortgage debt outstanding as of the date of death can be deducted from the value of the property. What has not been clear is if the value of the real property is less than the amount of the mortgage debt outstanding, can the negative value be applied to other assets owned by the deceased at the time of death? Historically, this has not been considered to be the case but in completing the EIR, it appears to be possible[10] as the form does provide for a negative value to be given which is then applied to the total amount of EAT owing.

5. Pre-paid funeral expenses

We have recently encountered a number of Estates where the deceased person had pre-paid for their funeral and the value of that account was considerable at the date of death. Is this an asset that they owned at the date of their death? Could they have received payment

[10] The Guide provides under section D, Real Estate in Ontario, that the Net Value may be negative. We ran a sample EIR where the value of the mortgage debt was greater than the value of the property and the negative value was applied to the EAT owing.

for this asset or could they have sold this asset prior to their death? If under the terms of their contract they could have redeemed all or some portion of the amount pre-paid, it may be arguable that this should be included as an asset and EAT paid.

6. General Powers of Appointment held by the deceased at the time of death.

If a person held a general power of appointment, which would have allowed them to appoint themselves as a beneficiary, and they die without making the appointment, is this an asset owned by the deceased? Careful review of the power of appointment would have to be considered but it is arguable that the value of the assets subject to the appointment should be included in the deceased's estate as they had authority and control over them which they failed to appoint to a third party. This would require that other assets of the estate must be used to pay the EAT on an asset they have not and may never receive.

7. Interest in a discretionary trust

If a person dies and was a beneficiary of a trust, should their potential interest be valued and subject to EAT? If there are payments made to the deceased's estate from the trust, does this make it more likely that the deceased had a property interest in the trust which should therefore, be valued and subject to EAT? Similar issues have arisen in the family law context and the courts have been dealing with the treatment and valuation of a spouse's interest in a discretionary trust.[11] In one case, the court ordered that one spouse's "contingent capital interest in the assets of the trust is property and is to be valued" even though it was a discretionary trust. [12] Perhaps such potential interests should be included in a secondary will.

8. Gift payable after wind-up of a Spousal Trust to those living at the time of death of the Testator

We have had the situation where the will provided for the residue of the testator's Estate to be held in a Spousal Trust for the lifetime of her spouse and on his death, the

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[11] "Discretionary Trusts in the Family Law Context", Howard S. Black, STEP Toronto-Case Law & Potpourri of Trust Issues, January 18, 2017.
[12] Ibid, page 8.

amount then remaining will be divided among named beneficiaries who are living at the time of the testator's death. Accordingly, the residual beneficiaries of the Spousal Trust had their interest vested in them upon the testator's death as opposed to on the death of the surviving spouse. Should the residual beneficiary die prior to the death of the surviving spouse, they have a vested interest in the residue of the Spousal Trust which value cannot be determined. It is impossible to value such an interest and it may be appropriate to state on the EIR that the value on the date of death of the residual beneficiary is in fact zero.

Valuations

It has been suggested that the 2011 amendments to the EATA were made as the government was concerned that the values reported in Applications for estate certificates were often more like estimates than accurate valuations of fair market value, supported by proper appraisals or valuations. Suggestions that, for example, appraisers or other valuators were asked to give a valuation "for probate purposes" rather than the actual fair market value meant that assets were being undervalued and the Ministry was not collecting the correct amount of EAT. By requiring a stricter reporting system, it was intended that more EAT would be collected. As a result, it appears that our role as lawyers has increased beyond simply providing advice on these issues but also creating and maintaining detailed lists of appropriate appraisers and valuators for a multitude of assets to be provided to our estate representative clients.

As noted above, it has been suggested that letters of opinion from real estate agents may be sufficient, however, while the MPAC valuations may assist in determining the value of real property they may not be representative of the fair market value of that property at the date of death.

Ontario Regulation 310/14, section 3(2) paragraph 5 provides a complete list of the assets of the deceased person required to be provided in the EIR. The actual value of each asset must be provided or, if the actual value is unavailable, the estimated value of the asset at the time of the deceased person's death. Pursuant to subsection 3(4) of the EATA, if the amount

of EAT deposited is based on the estimated value of the assets of the estate, then the estate representative shall give an undertaking that the estate representative will, within six months of giving the undertaking, file a sworn statement of the actual total value of the assets of the estate and pay any additional EAT payable if the actual value is higher than the estimate. In addition, the estate representative shall, no later than thirty days after fulfilling the undertaking, file a revised EIR with particulars on how the undertaking was fulfilled and paying any additional EAT payable.

It is very important to determine what evidence or supporting documents must be obtained by the estate representative and maintained by the estate representative to support the value of each asset of the deceased person as filed in the EIR. To date, there has been little or no case law to guide us in what is the appropriate evidence to be provided. Conversations with Ministry representatives have given some direction but cannot always be relied upon. There have been several decisions that offer assistance in defining what is the "fair market value" of the assets. In *Re Mann Estate*[13] the court stated that

> "Fair market value is the highest price available estimated in terms of money which a willing seller may obtain for the property in an open and unrestricted market from a willing knowledgeable purchaser acting at arm's length."

The requirement of an estate representative to determine accurately the value of the Estate is not a new requirement, however, the detailed reporting of it at this early of a stage in the administration of the Estate is somewhat new. An Estate Trustee of course must always obtain the accurate value in order that they can properly account to the beneficiaries, to ensure that they are getting full value of the Estate when they sell the assets and to ensure the appropriate compensation is calculated and income tax paid.

Obtaining formal valuations may take time and may be costly to the Estate. Appraisers and valuators will also be required to wait until the Certificate of Appointment is issued and the Estate Trustee has access to estate funds to pay the costs of such appraisals. As

[13] Re Mann Estate [1972] "5w.w.r.23(b.c.s.c.), affirmed [1973] c.t.c.561(b.c.c.a.)" at page 27

noted above, with respect to real property, a determination must be made as to whether letters of opinion of real estate agents with experience in the area of the real property, will be sufficient or whether formal appraisals will be required. Where the asset is the principal residence of the deceased or other residential properties used by the deceased, two letters of opinion may be sufficient and you might consider averaging the two letters to obtain an appropriate value for the calculation of EAT. More complicated real property however, such as commercial buildings or rental properties would likely require that an accredited appraiser be retained to complete a formal appraisal of the real property. Although this may be an unwanted cost to the Estate, it might assist when the property is finally offered for sale or in any distribution of the property to the beneficiaries. Generally, one appraisal would be sufficient, however, if the value given by the appraiser seems out of line or varies from what the deceased had indicated the property might be worth, then a second appraisal may be required. In circumstances where the value of the property may be contentious, the estate representative may be required to have three certified appraisals completed. The Ontario Ministry of Finance website specifically refers to the Appraisal Institute of Canada to obtain qualified appraisers.

Motor vehicles owned by the deceased can also be difficult to value and depending on the nature of the motor vehicle, may be a contentious valuation for the beneficiaries. Again, the Ministry of Finance does provide some guidance and directs estate representatives to the Canadian Red Book for market values of motor vehicles and they also direct owners of boats to the Boat Value Book for Vessels.

Valuing businesses will likely require the assistance of a Chartered Business Valuator. The designation of "CBV" is given by the Canadian Institute of Chartered Business Valuators. Such a valuator may appraise shares, assets or an interest in a business. The nature of the business being valued will, of course, vary the type of valuation that will be required. Whether or not the business is to be valued as a going concern or whether the business is intended to be liquidated and sold, would likely affect the value. In many small businesses, the deceased may have played a large role in the ongoing operation, or may have had a significant connection with

customers or clients, such that the value of the business may drop considerably as a result of the death of the owner. All of this must be factored into such a valuation. [14]

The Audit

Section 4.2 of the EATA provides that the Minister may assess an estate in respect of its tax payable. Subsection 4.7 (1) and (2) of the EATA incorporate by reference the audit and inspection powers authorized by subsections 31(1), (2), (2.1), and 2 of the RSTA for any purpose relating to the administration and enforcement of the EATA. Section 31 (1) of the RSTA provides as follows:

> "Any person thereunto authorized by the Minister for any purpose related to the administration or enforcement of this Act may at all reasonable times enter into any premises or place where any business is carried on or any property is kept or anything is done in connection with any business or any books or records are or should be kept pursuant to this Act, and,
>
> (a) audit or examine the books and records and any account, voucher, letter, telegram or other document that relates or may relate to the information that is or should be in the books or records or the amount of tax collectable or payable under this Act;
>
> (b) examine the property described by an inventory or any property, process or matter, an examination of which may, in the person's opinion, assist in determining the accuracy of an inventory or in ascertaining the information that is or should be in the books or records or the amount of any tax collectable or payable under this Act; and
>
> (c) require a vendor, purchaser or registrant liable to collect or pay or considered possibly liable to collect or pay tax under this Act or, if the vendor, purchaser or registrant is a partnership or corporation, require a partner or the president, manager, secretary or any director, agent or representative thereof and any other person on the premises of the vendor, purchaser or registrant to give him or her all reasonable assistance with the audit or examination and to answer all questions relating to the audit or

[14] For a detailed review of this issue please see "Valuations and Appraisals", Mary-Alice Thompson, The Law Society of Upper Canada, Practice Gems: Probate Essentials 2015, September 10, 2015.

examination, either orally or, if he or she so requires, in writing, on oath or by statutory declaration, and for that purpose require such person to attend at the premises or place with him or her."

In addition, Ontario Regulation 310/14, section 3(2) 14 provides that the estate representative may be required to provide "Any other information about the deceased person that is necessary for the determination of the amount of tax owing or paid under section 2 of the Act". This is a very broad catch all provision.

We have had one of our clients audited under the provisions of the EATA. Attached to this paper is a copy of the letter that our client received. You will note that although it is clear in the EATA and in the Regulation, that the EAT only applies to the assets governed by the will submitted for the estate certificate the audit process requires copies of all wills. They have also requested a listing of all properties that pass outside of the Estate as a result of joint ownership or as a result of having named or designated a beneficiary. Our client was required to establish that such assets were properly excluded from the payment from EAT. This audit notice was received eleven months after the filing of the EIR.

One issue that arose in our response to the audit request was whether or not any of the items they have requested would be subject to the principle of solicitor-client privilege. We looked to cases decided in conjunction with the *Income Tax Act*[15] which, unlike the RSTA or the EATA has a specific section dealing with solicitor-client privilege.[16] The case law is clear solicitor-client privilege should only be interfered with, and to the extent absolutely necessary to achieve the end sought by the legislation. Furthermore, to abrogate solicitor-client privilege, statutory language must be clear, unequivocal and unambiguous and general language granting the power to compel production of records has been held insufficiently specific to authorize a demand for production of records over which solicitor-client privilege is asserted.

[15] Income Tax Act, RSC 1985, c. 1 (5th Supp).
[16] Ibid. section 232.

In our review of the documents required to be produced, our clients instructed us to simply comply and produce the documents requested and they had no issue in our providing the valuations that they had acquired.

After receipt of the audit notice, we were contacted by the Ministry of Finance and were advised that they had established a formal electronic secure dropbox to exchange information. They also clarified that they required back-up information for each asset included in our application, by way of example, all bank statements. We requested that an electronic dropbox not be used and they agreed that we could allow our clients' materials to be delivered to them in person, in paper format.[17]

After the delivery of our materials, a follow up telephone call was made to us by the Ministry and they requested additional items of clarification.

We provided written response to this telephone request and several months later, we were advised that a letter would be sent to us. As a result of the inquiries made, we noted that one asset had in fact been improperly included in our EIR and we filed an amended EIR and advised the Ministry that we would be requesting a refund. A refund was received as indicated in the attached letter from the Ministry. The audit was completed slightly more than one year after the audit notice was received by us. This did result in considerable additional costs to the estate and did delay the administration of the estate by one year.

The Comfort Letter

When the 2011 amendments to the EATA were introduced, considerable discussion was had about the four year assessment period and the fact that there was no clearance certificate available that would end an estate representative's liability before that time.

[17] See also "What to Expect During an Ontario Ministry of Finance Audit https://www.fin.gov.on.ca/en/audit/mofaudit.html

The legislation was passed without any amendment to allow for such a certificate. However, the Ministry did suggest that a form of "comfort letter" may be made available.

Ministry representatives have confirmed that a "comfort letter" may be issued by them in the form attached to this paper, however, it will only be issued after they have completed an audit of the EIR and the estate representative has provided them with the Clearance Certificate issued by the Canada Revenue Agency.

Conclusion

The requirement to file the EIR has certainly required estate representatives to be more cautious in the values they place on estate assets and has increased the retaining of valuators and appraisers to provide backup support for the values provided in the EIR. It has also meant that we as lawyers, are often required to provide more assistance in completing the application for an estate certificate. Our retainer letters should deal with this and, if we are preparing and filing the EIR on behalf of the estate representative, we should ensure that we have clear, written authorization to do so.

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Ministère des Finances
Division de l'observation fiscale et des avantages fiscaux
Direction des conseils et de l'observation fiscale

33, rue King Ouest
CP 625
Oshawa ON L1H 8H9
Tél. : 905-433-6501
Télécopieur: 905-433-5666

Issue Date 13-Nov-2015
Court File No. [redacted]

Dear [redacted]:

We are conducting an audit of the above account under the *Estate Administration Tax Act, 1998,* for the estate of [redacted]. Please forward the following documents to the undersigned to arrive at the above address on or before December 14, 2015.

The records required for review at the commencement of the audit are, but not limited to, the following:

- Copy of Will(s)
- Proof of Death Certification
- Bank Statement(s) – Foreign and Domestic for November 2014
- Brokerage/Investment Statements as at November 19, 2014
- Appraisal(s)
- Copy of Deed
- Title of ownership
- Property Assessment Notice
- Statement of Adjustments which makes up the purchase price, final amount required from the purchase and the amount due to the vendor.
- Copy of the final cheque received from the lawyer's office when the property is sold
- Copies of Vehicle / Vessel Ownership and supporting documentation for the Fair Market Value
- Details and value of items included in other property
- Details and value of assets reported on the Certificate of Appointment of Estate Trustee Application
- Personal Tax Return(s) filed with Canada Revenue Agency – Last filed return and final return
- Business Valuation Reports for [redacted] Inc., [redacted] Inc., [redacted] Inc.
- [redacted] Inc., [redacted] Inc. and [redacted] Inc. Corporate Tax Return filed with Canada Revenue Agency for the fiscal year ending 2014
- [redacted] Inc., [redacted] Inc. and [redacted] Inc. Copies of the Federal schedule T2S(50) attached to the Corporate Tax Return filed with Canada Revenue Agency for the fiscal year ending 2014

SAMPLE ONLY

- List of the shareholders and their percentage of ownership in the company for [redacted] Inc., [redacted] Inc. and [redacted] Inc.
- Copy of Partnership Agreement(s)
- Loan Agreement(s)
- Registration of Safety Deposit Box including itemized list if applicable
- Notice of Estate Sale if applicable

Please include a listing of assets that passed outside of the estate as a result of joint ownership with a right of survivorship or assets with a named beneficiary and the supporting documentation to support the exclusion.

If you have any questions, please call the toll free number below and discuss them with either myself, at extension [redacted] or my manager, [redacted], at extension [redacted].

Sincerely,

[redacted]

Enclosure(s)

SAMPLE ONLY

Ministry of Finance
Tax Compliance and Benefits Division

Compliance Branch

33 King Street West
PO Box 627
Oshawa ON L1H 8H5
Telephone: 905- 433-6719
Facsimile: 905 433-5666

Ministère des Finances
Division de l'observation fiscale et des avantages fiscaux

Direction de l'observation fiscale

33, rue King Ouest
CP 627
Oshawa ON L1H 8H5
Téléphone : 905 433-6719
Télécopieur : 905 433-5666

SAMPLE ONLY

Issue Date: Nov -23-2016
Court File No:
ID:

c/o Lori M. Duffy
4100- 66 Wellington Street West,
PO Box 35,
Toronto Dominion Centre
Toronto-On
M5K 1B7

Dear Lori M. Duffy:

The recent Estate Administration Tax Audit conducted on the Estate resulted in a refund of which is enclosed.

If an estate representative discovers additional assets owned by the deceased, including after an audit has been completed, a statement disclosing the subsequently discovered property must be filed with the court within six months of the discovery (subsection 32(2) of the *Estates Act*) along with any additional Estate Administration Tax owing. An amended Information Return setting out the subsequently discovered property and its fair market value must be received by the Ministry of Finance within 30 calendar days after the statement is delivered to the court.

If you have already requested and received a refund from the court house that issued the estate certificate, you must notify the Ministry of Finance of the refund overpayment.

If you have any questions, please call the toll free number below and contact the auditor, at extension or myself at extension

Sincerely,

Enclosure(s)

Ministry of Finance
Tax Compliance and Benefits Division
Compliance Branch
33 King Street West
PO Box 625
Oshawa ON L1H 8H9

Ministère des Finances
Division de l'observation fiscale et des avantages fiscaux
Direction de l'observation fiscale
33, rue King Ouest
CP 625
Oshawa ON L1H 8H9

[Estate Trustee Name]
[Address]
[City] [Province_State] [Postal Code_Zip]
[Country]

Issue Date DD-MM-YYYY
Court File No. XXXXXXXXXXXX

Dear [Estate Trustee Name]:

Based on the information submitted, the Ministry of Finance has completed its Estate Administration Tax review and found the estate of [Deceased Person Name] to be in compliance with the Estate Administration Tax Act.

If an estate representative discovers additional assets owned by the deceased, including after a review has been completed, a statement disclosing the subsequently discovered property must be filed with the court within six months of the discovery (subsection 32(2) of the *Estates Act)* along with any additional Estate Administration Tax owing. An amended Information Return setting out the subsequently discovered property and its fair market value must be received by the Ministry of Finance within 30 calendar days after the statement is delivered to the court.

Estate representatives who fail to file the Information Return as required, or who make false or misleading statements on the return, are guilty of an offence and, on conviction, are liable to a fine of at least $1,000 and up to twice the tax payable by the estate, or imprisonment of not more than two years, or both.

Should you require any further information, please do not hesitate to contact me at the toll free number listed below ██████.

Sincerely,

SAMPLE ONLY

Enquiries 1 866 ONT-TAXS 1 866-668-8297 | Fax 905 433-5666 | Teletypewriter (TTY) 1 800 263-7776 | Internet **ontario.ca/finance**

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LET RIGHT PREVAIL

TAB 3

Posthumous Conception: Recent Changes to the *Succession Law Reform Act* And their Impact on Estate Law

Krystyne Rusek
Pallett Valo LLP

DAY TWO
October 17, 2017

cpd Continuing Professional Development

Posthumous Conception: **Recent Changes to the *Succession Law Reform Act* and their Impact on Estate Law**

Krystyne Rusek[1]
Pallett Valo LLP

As of January 1st, 2017, new rules regarding parentage were put into effect by the Ontario government, pursuant to the *All Families Are Equal Act (Parentage and Related Registrations Statute Law Amendment), 2016* (the "*AFAEA*")[2]. These changes have far-reaching consequences in the legal realm, primarily in the areas of family law and estate law.

One change of particular interest to estate practitioners is the creation of succession rights for posthumously conceived children, pursuant to the amendments of the *Succession Law Reform Act* (the "*SLRA*")[3]. These changes not only affect the estate of the deceased parent of the posthumously conceived child, but also the estates of the grandparents and other relatives of the child.

A. Background

Prior to January 1st, 2017, the definition of "child" in the *SLRA* included a child conceived before and born alive after the parent's death.[4] Similarly, the definition of "issue" included a descendant conceived before and born alive after the parent's death.[5] These definitions contemplated posthumous birth, but did not contemplate posthumous conception.

With the advent of new reproductive technologies, sperm, eggs and embryos can all be frozen, stored and then thawed for future use. Many individuals are availing themselves of these new technologies in order to preserve their ability to have children later in life or after medical interventions that cause sterilization, such as chemotherapy. While not yet common, posthumous conception is a scenario that will become more prevalent in the coming years. For that reason, estate practitioners must be aware of the legal effects of the new legislation and be able to anticipate unintended consequences for their clients.

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[1] I wish to thank my colleagues, Alan Kay of McMaster, McIntyre & Smyth LLP, and Craig Ross, of Pallett Valo LLP, for their valuable input and detailed review of this article. I would also like to thank WELPartners for providing me with an introduction to this very interesting topic.
[2] S.O. 2016, c. 23 (the "*AFAEA*").
[3] R.S.O. 1990, c. 26, as amended (the "*SLRA*").
[4] *SLRA*, s. 1.1(1).
[5] *Ibid*.

B. Amendments to the *SLRA*[6]

Prior to January 1st, 2017, the parent of a child, for the purposes of succession, was the father or mother of a child. The terms "father and "mother" have been deleted in the *SLRA* by the *AFAEA* and parentage is now determined in accordance with Part 1 of the *Children's Law Reform Act*[7] (the "*CLRA*").[8]

The *AFAEA* also expanded the definitions of "child" and "issue" in subsection 1(1) of the *SLRA* to include children and descendants conceived[9] and born after the death of a parent, provided all of the following conditions, set out in a new subsection 1.1(1), are met:

1. The person who, at the time of the death of the deceased person, was his or her spouse, must give written notice to the Estate Registrar for Ontario that the person may use reproductive material or an embryo to attempt to conceive, through assisted reproduction and with or without a surrogate, a child in relation to which the deceased person intended to be a parent.[10]
2. The notice under paragraph 1 must be in the form provided by the Ministry of the Attorney General and given no later than six months after the deceased person's death.
3. The posthumously-conceived child must be born no later than the third anniversary of the deceased person's death, or such later time as may be specified by the Superior Court of Justice under subsection (3).
4. A court has made a declaration under section 12 of the *Children's Law Reform Act* establishing the deceased person's parentage of the posthumously-conceived child.[11]

The new section goes on to provide for the definition of certain terms contained within the section, as well as further details regarding procedure:

> Interpretation
>
> (2) For the purposes of paragraph 1 of subsection (1), "assisted reproduction", "embryo", "reproductive material", "spouse" and "surrogate" have the same meaning as in section 1 of the *Children's Law Reform Act*.

---

[6] A summary chart of these amendments is attached as Schedule "A".
[7] R.S.O. 1990, c. C.12, as amended (the "*CLRA*").
[8] The rules of parentage are complex in nature and will not be discussed in this paper outside of the rules that apply to posthumous conception.
[9] Under s. 1(3) of the *CLRA*, conception through assisted reproduction is deemed to be the date on which the reproductive material or embryo is implanted in the birth parent.
[10] Under s. 1(3) of the *CLRA*, conception through assisted reproduction is deemed to be the date on which the reproductive material or embryo is implanted in the birth parent.
[11] *SLRA*, s. 1.1(1).

Extension of time

(3) On motion or application, as the case may be, by a surviving spouse who gives notice under paragraph 1 of subsection (1), the Superior Court of Justice may make an order extending the period referred to in paragraph 3 of that subsection, if the Court considers it appropriate in the circumstances.[12]

1. Notice to the Registrar

As stated above, in order to have the expanded definition of "child" and "issue" apply, notice must be provided to the Estate Registrar within 6 months of the date of death of the deceased, of an intention to use the reproductive material of a deceased person.

The form of Notice is provided by the Ministry of the Attorney General and is available under the *Succession Law Reform Act* Forms tab of the Ontario Court Services webpage. A copy of the Notice is attached as Schedule "B".

a. Spouse

It is of interest to note that in order to satisfy clause 1 of subsection 1.1(1), only the spouse of the deceased, at the time of his or her death, can use the reproductive matter to conceive a child who will have rights under the *SLRA*. The definition of spouse for this section is deemed to be that of section 1 of the *CLRA*:

> "spouse" means the person to whom a person is married or with whom the person is living in a conjugal relationship outside marriage;

There is no statutory definition of "conjugal relationship". Ontario courts have tended to follow a non-exhaustive list of factors set out in the case of *Molodowich v. Penttinen*[13] in determining whether parties are in a "conjugal relationship".

b. Receipt and Retention of Notices

Notice of an intention to use reproductive material of a deceased person is only required to be provided to the Estate Registrar for Ontario.[14] It therefore can be concluded that the Estate Registrar will be responsible for retaining all notices and, presumably, notifying applicants for probate about:

- notices that have been filed prior to the date an application for probate is filed;

[12] *SLRA*, s. 1.1(2) and (3).
[13] (1980), 1980 CanLII 1537 (ON SC), 17 R.F.L. (2d) 376 (Ont. Dist. Ct.).
[14] Contrast this to the B.C. *Wills, Estates and Succession Act* [SBC 2009] c. 13, which requires that notice be provided to the deceased's representative, beneficiaries and intestate successors.

- notices that are filed while the probate application is being processed; and
- notices that are filed after a Certificate of Appointment has been issued.

As well, given the estate representative's duty to ascertain heirs, there may be a positive obligation to search the records of the Estate Registrar for any filed notices.[15]

At a minimum, notices will need to be retained for 3 years and 90 days, as evidence that the notice was filed properly, in cases where a child is posthumously conceived and born. Given the court's power to extend the deadline in clause 3 of subsection 1.1(1), it is possible that notices will need to be retained for longer than that period, however until there has been judicial interpretation of clause 3, notices may need to be kept indefinitely.

c. Non-Compliance

From the wording of clause 2, it appears that failure to adhere to the form required, or failure to meet the strict deadline will result in a rejection of the notice. However, will this non-compliance with the notice requirements preclude any succession rights to the posthumously conceived child? Can the acts or omissions of one of the child's parents forever extinguish the rights of a child to inherit or receive support from the other parent, or will there be some form of recourse available?[16]

2. Birth of Child Within 3 Years of Death

Clause 3 of subsection 1.1(1) requires that the posthumously-conceived child be born no later than the third anniversary of the deceased person's death, subject to the granting of an extension under subsection 1.1(3) by the court. An extension may be granted in "appropriate circumstances".

The question of what are "appropriate circumstances" and what is a reasonable extension will be dependent on the particular facts of each case. This creates some uncertainty in the administration of estates. Estate representatives will presumably know within 6 months of death that a surviving spouse intends to use the deceased's reproductive material to conceive posthumously. They will also have a general timeline of 3 years post-death in which they can expect a child to be born. However, the court's ability to extend this deadline in "appropriate circumstances" leaves much uncertainty with respect to the administration of an estate.

Given that the request for an extension must be brought by motion or application, it can be assumed that the estate representative will have notice of the requested relief. However, can the

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[15] Note, the notice will be linked only to the estate of the deceased parent even though the notice may also affect the estates of the deceased parent's relatives.
[16] Contrast this to the principal that the limitation of a minor's claim will not commenced until the minor has reached the age of majority.

estate trustee oppose the request for an extension? Will other interest parties, such as beneficiaries or creditors be granted standing to challenge the extension request?

3. Declaration of Parentage

Lastly, in order for a posthumously conceived child to qualify for succession rights or support rights, a declaration of parentage must be obtained. This declaration is obtained on application to the Superior Court of Justice under section 12 of the *CLRA*, which states:

> Posthumous conception
>
> 12 (1) A person who, at the time of a deceased person's death, was his or her spouse, may apply to the court for a declaration that the deceased person is a parent of a child conceived after his or her death through assisted reproduction.
>
> Time limit
>
> (2) An application under subsection (1) may not be made,
>
> (a) until the child is born; and
> (b) unless the court orders otherwise, later than 90 days after the child's birth.
>
> Declaration
>
> (3) The court may grant the declaration if the following conditions are met:
>
> 1. The deceased person consented in writing to be, together with the applicant, the parents of a child conceived posthumously through assisted reproduction, and did not withdraw the consent before his or her death.
>
> 2. If the child was born to a surrogate, the applicant is a parent of the child under section 10, and there is no other parent of the child.

Pursuant to subsection 15(2) of the *CLRA*, the declaration is deemed to be effective from the date of birth of the child.

a. Spouse

The ability to apply for the declaration is again restricted to the spouse of the deceased, as of the time of his or her death. An intended co-parent, who is not a spouse of the deceased, appears to be precluded from obtaining this declaration. As with the notice provision, the definition of spouse for this section includes both married spouses and persons living in a conjugal relationship outside of marriage.

b. Consent in writing to parentage

An applicant will be required to prove, on a balance of probabilities, that the deceased provided written consent to parentage of a posthumously conceived child, and that said consent was not withdrawn.

There is no prescribed form of consent under clause 1 of subsection 12(3). The adequacy of the consent will be a matter for the court to determine, applying the general rules of evidence. The consent may require judicial interpretation or may be challenged on various grounds.

Whether consent was withdrawn will likewise be an evidentiary issue. As stated, the withdrawal of consent need not be in writing. If withdrawal of consent is verbal, there will be an obvious need for corroboration.

c. Procedural matters

There are no specifics in regard to the procedure for the application for a declaration of parentage. One would presume that the estate of the deceased person would need to be a party to the application, but would beneficiaries under a Will and intestate successors have standing, as interested parties, to oppose the application?

As mentioned above, the *SLRA* allows for a posthumously conceived child to be born up to 3 years after death of the intended parent's death, with the possibility of an extension of this deadline. The application for a declaration of parentage must be brought after the child's birth, but no later than 90 days after birth, unless the court orders otherwise. If an application for a declaration of parentage is opposed, it could be many years before a posthumously conceived child is declared the child of the deceased. An estate trustee will need to balance the rights of existing beneficiaries to the timely administration of an estate against the rights of the not-yet conceived beneficiary to share in the estate.

d. Non-Compliance

The same issues that have been raised with respect to notice under subsection 1.1(1) will also apply with respect to the procedural requirements of an application for a declaration of parentage: will procedural non-compliance forever extinguish the rights of a posthumously conceived child to inherit or receive support from the deceased parent's estate?

C. Testate Estates and Will Interpretation[17]

As discussed, the definitions of "child" and "issue" in the *SLRA* have been expanded to include children and descendants conceived after the death of the person, provided the conditions of subsection 1.1(1) are met.

Under subsection 2(1) of the *CLRA*, these definitions will apply to "instruments", unless a contrary intention is expressed in the instrument. If a Will is considered an instrument, the terms "child", "children" and "issue" will be interpreted in accordance with the updated *CLRA* and *SLRA*. However, under subsection 2(3) of the *CLRA*, it appears that the application of subsection (1) to instruments not made under an Act, such as Wills, is not retroactive.[18] If this interpretation is correct, Wills that were made prior to January 1st, 2017, will be interpreted in accordance with the definitions and rules of parentage of the previous versions of the *CLRA* and *SLRA*, and the expanded definitions will not apply. For the purposes of discussing the effects of the *AFAEA*, this commentary will be directed to testamentary instruments made after January 1st, 2017.

Pursuant to the rule of convenience, where there are existing members of a class, that class will close on the testator's death, even where it is theoretically possible for more members of the class to be born later.[19] The class will not close if there are no members of the class as of the date of death.[20] It is not clear whether the amendments to the definition of "child" and "issue" under the *SLRA* override this rule of construction. Does the class of beneficiaries remain open until the deadlines set out in the *CLRA* and *SLRA* expire, or must the deceased's Will specifically state that the class will remain open?

If the amendments do not alter the application of the rule of convenience, posthumous children and issue will only inherit under a Will if there are members of that class alive as of the date of death, or if the Will specifically provides for inheritance by posthumously conceived children.

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[17] Distribution of testate estates will be subject to dependant support claims made on behalf of the posthumously conceived child, as discussed later in the paper. If a suspensory order is obtained in conjunction with the commencement of the claim, the distribution of the estate could be suspended until the claim is resolved.

[18] This interpretation is subject to challenge for a number of reasons. First, unless a contrary intention is indicated, a Will speaks from the date of the testator's death and is generally interpreted in accordance with the laws in effect at that time. A testator is presumed to know the law, and if capable, is able to amend his or her Will to reflect actual intentions. Second, the amendments to the *SLRA* do not include any provisions addressing application of the amended definitions in the *CLRA* to Wills made before January 1st, 2017. Contrast this to the change effected in 1978 with respect to children born out of wedlock. The 1978 change was reflected in s. 2(1) of the *CLRA*, with s. 2(2) clarifying that the change applied to instruments made on or after March 31st, 1978. The change was also reflected in s. 1(3) of the *SLRA*, with s. 1(4) clarifying that it applied to Wills made on or after March 31st, 1978. Section 1.1(1) of the *SLRA* does not have a clause comparable to subsection 1(4). The question arises as to whether the omission of an application clause in the *SLRA* was intentional or inadvertent, or whether it is even needed, given s. 2(3) of the *CLRA*.

[19] Knaplund, Kristine S., *Postmortem Conception and a Father's Last Will*, 46 Arizona Law Review 91, 91 (2004) at page 109.

[20] *Ibid.*

If the amendments serve to keep the class open as of date of death, various possibilities exists and the terms of the Will will be paramount. If the Will restricts the definitions of "child" and "issue" to children and issue conceived prior to death, a posthumously conceived child will have no inheritance rights under the Will, and will be limited to a dependant support claim. If the Will uses, but does not define the terms "child" and "issue", the definitions of those terms will be in accordance with the *CLRA*. As a result, posthumously conceived children and issue may fall into a class of beneficiaries entitled to inherit under the Will.[21]

Recommendations for Planning Solicitors:

Planning solicitors are advised to discuss with their clients whether posthumously conceived children and issue are intended to inherit under the Will. Wills will need to contain clear definitions of "child", and "issue" and will need to specify a time at which the members of a class are to be determined.

It is also recommended that clients be questioned about any existing stored reproductive material or any intention to store reproductive material, whether by them or by their children and grandchildren. If the client confirms the possibility of posthumous conception, a planning solicitor may wish to review the documents relating to the use of the reproductive materials[22], and discuss the written consent to parentage required under the *CLRA*.

As discussed, the *SLRA* contains time limits in regard to the birth of a posthumously conceived child. However, these time limits can be altered by the terms of a Will. Shorter timelines for conception and/or birth may be set out in the Will, so as to minimize delay to the administration of the estate. Longer timelines may be preferred in cases where a successful pregnancy and birth are desired. Where the timelines in the Will are different from those in the *SLRA* and *CLRA*, the Will should include a requirement that the estate trustee notify the deceased's spouse of these timelines.

One option for estate planning solicitors to consider is the creation of a trust for posthumously conceived children. This would therefore create a separate class of beneficiaries. The terms of the trust could fix a date for the determination of members of the class and would provide a gift-over to alternative beneficiaries. This will allow an estate to be administered in a more-timely manner, with more certainty and protection for the estate trustee.[23]

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[21] The expanded definition of "child" would obviously not apply where children are identified by name in the Will.
[22] Use of genetic material is regulated by the *Assisted Human Reproduction Act*, S.C. 2004, c. 2, which requires that written consent be provided by the donor of the material, whether before or after the donor's death (s. 8).
[23] In this regard, solicitors may need to assess if there is a potential problem created by the rule against perpetuities, given that no changes were made to the *Perpetuities Act*. Will a posthumously conceived child (as defined in the

D. Intestate Estates[24]

Where an individual does not have a valid Will, the definitions of "child" and "issue" under the *CLRA* will apply to the distribution of the estate.[25]

Because of the amendment to the definition of "child" and "issue" in the *SLRA*, the posthumously conceived child and issue of the deceased parent will be entitled to share in the distribution of the parent's estate, provided the conditions under subsection 1.1(1) are satisfied.

As stated above, an estate administrator, who files an application for probate, will presumably have been notified by the Estate Registrar that the deceased's spouse has filed notice under subsection 1.1(1). Under section 26 of the *Estates Administration Act*[26], an intestate estate cannot be distributed within the first year of death. It will be up to the estate administrator to decide after the expiry of the 1-year period whether to distribute the estate, or wait for a child to be conceived.[27]

The intestacy provisions of s. 47 of the *SLRA* have also been amended to include new subsections (10) and (11), which state:

> (10) For the purposes of this section, descendants and relatives of the deceased conceived and born after the death of the deceased shall inherit as if they had been born in the lifetime of the deceased and had survived him or her, if the conditions in subsection 1.1(1) are met.
>
> (11) The right of a descendant or relative to whom subsection (10) applies begins on the day he or she is born.

Subsection (10) operates to extend inheritance rights of posthumously conceived children to the estates of their relatives and antecedents, e.g. grandparents, uncles, etc.

CLRA rather than under the Will) be considered a life in being? If not, then the perpetuity period may be limited to a maximum of 21 years (there being no life in being). Or, where there is a gift-over to a grandchild in trust, and the trust is to go until age 21, it is possible that the life in being is the testator's child. In this case, the grandchild might not be born until 3 years (or longer with court order) after the child's death. The grandchild would be 18 years of age, or possibly younger, at the end of the perpetuity period. The question of whether a posthumously conceived child will be considered a life in being has not been addressed by the changes under the *AFAEA*. As a result, solicitors will need to provide comprehensive advice to their clients about the impact of the rule against perpetuities and will need to ensure that the terms of the client's Will do not result in the voiding of a gift.

[24] Distribution of intestate estates will be subject to dependant support claims made on behalf of the posthumously conceived child, as discussed later in the paper. If a suspensory order is obtained in conjunction with the commencement of the claim, the distribution of the estate could be suspended until the claim is resolved.

[25] Pursuant to ss. 2(1) and 2(2) of the *CLRA*, the amendments apply as of January 1st, 2017.

[26] R.S.O. 1990, c. E. 22, as amended.

[27] As stated in footnote 24, this will be subject to a suspensory order obtained in conjunction with a dependant support claim.

Subsection (11) acts to crystallize the claims of posthumously conceived children as of the date the child is born. Until the child is born, no claim exists.[28]

An estate administrator has the right to distribute an intestate estate after the first anniversary of the date of death, however, a posthumously conceived child may not be born for some time after that. If the child's entitlement does not crystallize until date of birth, does it follow that an estate administrator is permitted distribute the entire estate before the birth of the child, thus preventing that child from receiving his or her proportionate share of the estate?[29]

The 1985 report of the Ontario Law Reform Commission on "Human Artificial Reproduction and Related Matters" provides some guidance in regard to the interpretation of these provisions. The report recommended that estates that have already been distributed should not be disturbed, nor should there be any postponement of distribution in cases where [reproductive material] is held in cryopreservation.[30] It appears that the wording of subsection (11) is intended to reflect this recommendation. Furthermore, the amendments to the intestacy provisions by the *AFAEA* did not provide for the suspension of the distribution of estate upon receipt of the notice under subsection 1.1(1).[31]

As a result, the logical interpretation is that upon the birth of a posthumously conceived child, the child will be entitled to share proportionately in the undistributed estate, but will have no claim against the portion that has been distributed.[32]

E. Dependant Support

The definition of "child" for the purpose of Part V of the *SLRA* includes posthumously conceived children.[33]

Section 57 of the *SLRA* has been amended by the addition of subsection (2), which states:

> (2) For the purposes of clause (c) of the definition of "dependant" in subsection (1), where the conditions in subsection 1.1(1) are met in relation to a child conceived and

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[28] This subsection appears to apply to intestate inheritance from both a deceased parent and a deceased antecedent or relative. Contrast this with s. 8.1 of the B.C. *Wills, Estates and Succession Act*, in which the crystallization of a claim, to the date the child is born, is only applicable to claims of a "descendant… to inherit from the relatives of a deceased person". The question therefore arises as to the intended application of s. 47(11), i.e. was it intended to only apply to entitlement in the estates of grandparents and other relatives?

[29] Again, this would not be permitted if a suspensory order is in effect.

[30] Ontario Law Reform Commission on "*Human Artificial Reproduction and Related Matters*" (1985), at pages 180-181.

[31] The 2008 report of the Manitoba Law Reform Commission on *Posthumously Conceived Children: Intestate Succession and Dependants Relief* strongly recommends that any legislation should include "a 'hard cutoff' date before which the estate may not be distributed" (at page 180).

[32] This interpretation appears to run contrary to the intended purpose of the amendments, which is to recognize a posthumously conceived child's entitlement on intestacy.

[33] Pursuant to ss. 2(1) and (2) of the *CLRA*, the amendment applies as of January 1st, 2017.

born alive after the death of the deceased, the deceased is deemed to have been, immediately before his or her death, under a legal obligation to provide support to the child.

Section 59 has been amended to allow an application, by a surviving spouse, on behalf of a posthumously conceived child, to make application for dependant support, where notice has been given under subsection 1.1(1), and where the child has not yet been conceived.[34] This application must be commenced within 6 months of the deceased parent's death.[35] Upon application, the court may order that the administration of the deceased's estate be suspended, in part or in whole, for such time and to such extent as the court deems appropriate.[36]

In cases of posthumous conception, if a certificate of appointment is obtained forthwith after death, it is possible that a testate estate could be fully distributed before an order under section 59 is granted. On an intestacy, this would not be as likely, given that an administrator is restricted by section 26 of the *Estates Administration Act* from distributing the assets before the 1-year anniversary of death. Time will therefore be of the essence in commencing dependant support claims on behalf of posthumously conceived children.

E. Vesting Under Section 9 of *Estates Administration Act*

As discussed in footnote 23, the legislature did not make any consequential amendments to the *Perpetuities Act*[37] to deal with posthumous birth, nor did it make any amendments to sections 9-13 of the *Estates Administration Act*. Section 9 applies to intestacies and to certain Wills. It provides that real property not disposed of, conveyed to, divided or distributed among the persons beneficially entitled thereto will vest in those beneficiaries 3 years following the death of the deceased, unless the estate representative registers a caution. Registration of a caution will extend the vesting period by an additional 3 years and can be renewed or withdrawn.

Generally, this should not pose an issue since the 3-year vesting period will coincide with the requirement for the posthumously conceived child to be born within 3 years. However, if the 3-year birth requirement is extended by the court, an estate representative must then consider whether:

- a caution should be registered so as to preserve a posthumously conceived child's vesting rights;
- a caution should not be registered so as to preclude a posthumously conceived child's vesting rights; or

[34] *SLRA*, s. 59(2).
[35] *Ibid.*
[36] *SLRA*, s. 59(1).
[37] R.S.O. 1990, c. P.9.

- to distribute the property, as discussed, above respecting intestate distributions.

E. Conclusion

In response to advances in reproductive technology, the legislature has taken steps to ensure that posthumously conceived children are afforded some rights with respect to the estates of their deceased parents and relatives. The changes to the *CLRA* and *SLRA* appear to strike a reasonable balance between the rights of these children and the other considerations such as the rights of other beneficiaries and dependants, and the timely and orderly administration of estates.

As the frequency of posthumous conception increases in the future, many questions will arise with respect to the interpretation of these statutory amendments. Unfortunately, until judicial interpretation has occurred on the amended legislation, a great deal of uncertainty will exist with respect to the rights of posthumously conceived children and the obligations of estate trustees. Estate planning lawyers will have an important role in advising their clients on the effects of the new legislation and drafting testamentary documents to reflect their clients' intentions.[38]

---

[38] The changes to the SLRA and in particular, succession rights of posthumously conceived children and issue have been discussed by a number of organizations and members of the estates bar. In the process of writing this paper, I have reviewed numerous articles and have incorporated some thoughts and ideas contained in those articles into this paper. I refer you to the following informative articles and blogs: Ontario Law Reform Commission, *Report on Human Artificial Reproduction and Related Matters*, 1985; Alberta Law Reform Institute, *Assisted Reproduction After Death: Parentage & Implications*, March 2015; Manitoba Law Reform Commission, *Posthumously Conceived Children: Intestate Succession and Dependants Relief*, November 2008; Clare E. Burns and Anastasija Sumakova, *Mission Impossible: Estate Planning and Assisted Human Reproduction*, 2010 Canadian Bar Association National Conference; Susan Gary, *Posthumously Conceived Heirs*, GPSolo Magazine, September 2005; Darren Lund, *All About Estates*, various blogs between March 31st, 2017 and August 4th, 2017, (allaboutestates.ca); Kristine S. Knaplund, *Postmortem Conception and a Father's Last Will*, 46 Arizona Law Review 91, 91 (2004); Suzanna Popovic-Montag, *Fertility Law Considerations for Estate Lawyers*, The Probater, Volume 23, Number 1, March 2017 and *Fertility Beyond the Grave*, Blog August 2, 2017 ; Kimberley A. Whaley and Helen Likwornik, *Life After Death: Modern Genetics and the Estate Claim*; WELPartners Blog, March 1, 2009, published in the Estates, Trusts & Pensions Journal [Vol.28]; Mary Kate Zago, *Second Class Children: The Intestate Inheritance Rights Denied to Posthumously Conceived Children and How Legislative Reform and Estate Planning Techniques Can Create Equality* (2014). Law School Student Scholarship. 609.

Schedule "A"

<table>
<tr><th colspan="2">Amendments to the Succession Law Reform Act, RSO 1990, Chapter S. 26
Pursuant to the All Families Are Equal Act (Parentage and Related Registrations Statute Law Amendment), 2016, SO 2016, c.23 – Bill 28</th></tr>
<tr><td><u>Old Version</u>
(In force Dec. 10, 2016 to Dec. 31, 2016)</td><td><u>New Version</u>
(In force January 1st, 2017)</td></tr>
<tr><td colspan="2">Definition/Interpretation</td></tr>
<tr><td>Section 1(1)

"child" includes a child conceived before and born alive after the parent's death;</td><td>Section 1(1)
"child" includes,
(a) a child conceived before and born alive after the parent's death, and
(b) a child conceived and born alive after the parent's death, if the conditions in subsection 1.1 (1) are met;</td></tr>
<tr><td>Section 1(1)

"issue" includes a descendant conceived before and born alive after the person's death;</td><td>Section 1(1)
"issue" includes,
(a) a descendant conceived before and born alive after the person's death, and
(b) a descendant conceived and born alive after the person's death, if the conditions in subsection 1.1 (1) are met;</td></tr>
<tr><td>Section 1(1)
"parent" means the father or mother of a child;</td><td>Definition of "parent" in subsection 1(1) of the Act is repealed.</td></tr>
<tr><td>Section 1(1)
"spouse" means either of two persons who,
(a) are married to each other, or
(b) have together entered into a marriage that is voidable or void, in good faith on the part of the person asserting a right under this Act;</td><td>Section 1(1)
"spouse", except in Part V, has the same meaning as in section 1 of the Family Law Act;

s. 1 FLA:

"spouse" means either of two persons who,
(a) are married to each other, or
(b) have together entered into a marriage that is voidable or void, in good faith on the part of a person relying on this clause to assert any right.</td></tr>
<tr><td>Section 1(2)
Polygamous marriages
(2) In the definition of "spouse", a reference to marriage includes a marriage that is actually or potentially polygamous, if it was celebrated in a jurisdiction whose system of law recognizes it as valid.</td><td>Subsection 1(2) of the Act is repealed.</td></tr>
</table>

Section 1.1 did not exist.	The following section was added following the section before the heading to Part I.
	Posthumous conception, conditions 1.1 (1) The following conditions respecting a child conceived and born alive after a person's death apply for the purposes of this Act: 1. The person who, at the time of the death of the deceased person, was his or her spouse, must give written notice to the Estate Registrar for Ontario that the person may use reproductive material or an embryo to attempt to conceive, through assisted reproduction and with or without a surrogate, a child in relation to which the deceased person intended to be a parent. 2. The notice under paragraph 1 must be in the form provided by the Ministry of the Attorney General and given no later than six months after the deceased person's death. 3. The posthumously-conceived child must be born no later than the third anniversary of the deceased person's death, or such later time as may be specified by the Superior Court of Justice under subsection (3). 4. A court has made a declaration under section 12 of the *Children's Law Reform Act* establishing the deceased person's parentage of the posthumously-conceived child. **Interpretation** (2) For the purposes of paragraph 1 of subsection (1), "assisted reproduction", "embryo", "reproductive material", "spouse" and "surrogate" have the same meaning as in section 1 of the *Children's Law Reform Act*. **Extension of time** (3) On motion or application, as the case may be, by a surviving spouse who gives notice under paragraph 1 of subsection (1), the Superior Court of Justice may make an order extending the period referred to in paragraph 3 of that subsection, if the Court considers it appropriate in the circumstances.

<table>
<tr><th colspan="2">Intestate Succession</th></tr>
<tr><td>Section 47(10) and (11) did not exist. Section 47 of the Act ended at the following subsection:

Descendants conceived but unborn
(9) For the purposes of this section, descendants and relatives of the deceased conceived before and born alive after the death of the deceased shall inherit as if they had been born in the lifetime of the deceased and had survived him or her.</td><td>Section 47 of the Act is Amended by adding the following subsections:

Descendants posthumously conceived
(10) For the purposes of this section, descendants and relatives of the deceased conceived and born alive after the death of the deceased shall inherit as if they had been born in the lifetime of the deceased and had survived him or her, if the conditions in subsection 1.1 (1) are met.

Right to inherit
(11) The right of a descendant or relative to whom subsection (10) applies to inherit begins on the day he or she is born.</td></tr>
<tr><th colspan="2">Support of Defendants</th></tr>
<tr><td>Section 57

“spouse” means a spouse as defined in subsection 1 (1) and in addition includes either of two persons who,
(a) were married to each other by a marriage that was terminated or declared a nullity, or
(b) are not married to each other and have cohabited,
(i) continuously for a period of not less than three years, or
(ii) in a relationship of some permanence, if they are the natural or adoptive parents of a child. (“conjoint”)</td><td>The definition of “spouse” in section 57 of the Act is repealed and the following substituted:

“spouse” has the same meaning as in section 29 of the Family Law Act.

s. 29 FLA:
“spouse” means a spouse as defined in subsection 1 (1), and in addition includes either of two persons who are not married to each other and have cohabited,
(a) continuously for a period of not less than three years, or
(b) in a relationship of some permanence, if they are the parents of a child as set out in section 4 of the Children’s Law Reform Act.</td></tr>
<tr><td>Section 57(2) did not exist.</td><td>Section 57 of the Act is Amended by adding the following subsection

Dependant posthumously-conceived child
(2) For the purposes of clause (c) of the definition of “dependant” in subsection (1), where the conditions in subsection 1.1 (1) are met in relation to a child conceived and born alive after the death of the deceased, the deceased is deemed to have been, immediately before his or her death, under a legal obligation to provide support to the child.</td></tr>
</table>

Section 59(2) did not exist.	Section 59 of the Act is amended by adding the following subsection: **Posthumous child not yet conceived** (2) An application may be made under subsection (1) by a surviving spouse who gives notice under paragraph 1 of subsection 1.1 (1) on behalf of a child of the deceased that is referred to in the notice and is not yet conceived, if the application is made no later than six months after the death of the deceased.

Schedule "B"

Ontario Ministry of the Attorney General

Notice to Estate Registrar of Ontario (Posthumous Conception)

Submit to: Estate Registrar of Ontario
c/o Toronto Estates Office
Superior Court of Justice
330 University Ave
Toronto ON M5G 1R7

I, ______________________________ , the surviving spouse of
(Name of Surviving Spouse)

______________________________ hereby give notice to the
(Name of Deceased Spouse)

Estate Registrar for Ontario as required under section 1.1 of the *Succession Law Reform Act* that I may use reproductive material or an embryo to attempt to conceive, through assisted reproduction and with or without a surrogate, a child in relation to which

______________________________ intended to be a parent.
(Name of Deceased Spouse)

Surviving Spouse

First Given Name	Second Given Name
Third Given Name	Surname
Full Current Mailing Address (street or postal address) (city or town)	(county or district)

Deceased Spouse

First Given Name	Second Given Name
Third Given Name	Surname
Date of Birth (yyyy/mm/dd)	Date of Death (yyyy/mm/dd)
Last mailing address (if different than address of spouse provided above) (street or postal address) (city or town)	(county or district)

This Notice must be submitted to the Estate Registrar of Ontario no later than six months following the date of death.

____
(Signature of Surviving Spouse)

____
Date (yyyy/mm/dd)

SAMPLE ONLY

The Law Society of Upper Canada | Barreau du Haut-Canada

TAB 4

20TH ANNUAL
Estates and Trusts Summit

Update on Charity Law

Terrance Carter
Carters Professional Corporation

DAY TWO
October 17, 2017

cpd Continuing Professional Development

THE LAW SOCIETY OF UPPER CANADA
20th ANNUAL ESTATES AND TRUSTS SUMMIT

Toronto – October 17, 2017

UPDATE ON CHARITY LAW

(Current as of October 4, 2017)

Terrance S. Carter
Carters Professional Corporation
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UPDATE ON CHARITY LAW
October 17, 2017
(Current as of October 4, 2017)

Terrance S. Carter
Carters Professional Corporation

Table of Contents

A. Introduction 3
B. Federal Budget 2017 Highlights 3
   1. Ecological Gifts 4
   2. Repeal of Additional Corporate Donation Deductions on Medicine for International Aid 6
   3. Farewell First-Time Donor's Super Credit, We Hardly Knew You 7
   4. Amendments to Anti-terrorism Legislation 7
C. Recent CRA Publications 8
   1. New CRA Guidance on Charities That Assist the Aged 8
   2. CRA's New Cause-related Marketing Webpage 12
   3. New Privacy Disclosure in T2050 Application to Register a Charity Under the ITA 13
   4. Sweeping Changes Recommended in Report on Political Activities 14
   5. Changes to Charitable Registration Application Process 18
   6. Voluntary Disclosure and Canadian Registered Charities in Context 19
   7. CRA to Update Business Numbers to Provide e-Services Starting in November 2018 21
   8. CRA Releases New Guidance on Head Bodies and Internal Divisions 22
   9. Changes to CRA's CG-014 CED Guidance 23
D. Recent Tax Decisions, Rulings, and Interpretations Involving Charities 23
   1. Income Tax Treatment for Monies Paid to Support Refugees 23
   2. Administrative Penalty Assessed for False Statements on Donation Receipts 25
   3. CRA Issues a Technical Interpretation of Charities Returning Gifts 26
E. Corporate Law Update 28
   1. Corporations Canada Dissolves Part II CCA Corporations 28
   2. Corporations Canada Increases Online Services 28
   3. Ontario Corporations Now Required to Keep Records of Land Ownership 29
   4. Bill 154 - Amendments to the ONCA 30
   5. Bill 154 - Amendments to the OCA 31
F. Federal Legislation Update 35
   1. Budget Implementation Act, 2016, No. 2 Passes 35
   2. CASL Private Right of Action Implementation Suspended 36

3. End of CASL Transition Period 37

G. Provincial Legislation Update 38

1. Amendment to the Ontario Employer Health Tax will Impact Registered Charities 38
2. Proposed Ontario Regulations Authorizing Charitable Corporations to Pay Directors in Limited Situations 39
3. Bill 154 - Amendments to the CAA 40
4. Charities Operating in Quebec are Still Required to Submit an Annual Information Return in Quebec 46

H. Other Case law of Interest 46

1. Unfunded Cheque Results in Unenforceable Gift 46
2. "Armchair Rule" Used by Court to Determine if Gift was an Endowment or Expendable 47
3. SCC Grants Leave to Appeal from Case Involving Unfair Church Discipline 49
4. Orders Amending By-laws Outside the Jurisdiction of Arbitrators 50
5. Tribunal Upholds Religious School Right to Reject Applicants Based on Creed 51

I. Conclusion 54

J. Case Law Appendix 55

A. INTRODUCTION

Over the last 12 months there have been a number of legislative and common law developments at the federal and provincial level that impact how charities, as well as not-for-profit corporations, operate in Canada. The purpose of this paper is to provide a brief overview of some of the more important developments in the last year, including changes introduced through the 2017 Federal Budget,[1] new publications from the Charities Directorate of the Canada Revenue Agency ("CRA"), corporate updates under the *Canada Not-for-Profit Corporations Act* ("CNCA"),[2] the Ontario *Corporations Act* ("OCA"),[3] the Ontario *Not-for-profit Corporations Act* ("ONCA"),[4] and the *Charities Accounting Act* ("CAA"),[5] as well as other federal and provincial initiatives and recent court decisions affecting charities. Within each section of this paper, items are presented chronologically.

B. FEDERAL BUDGET 2017 HIGHLIGHTS

On March 22, 2017, federal Finance Minister, Bill Morneau, tabled the second budget of the Liberal Federal Government ("Budget 2017").[6] While Budget 2017 again emphasized the Liberal election platform focusing on economic growth, job creation and supporting a strong middle class, Budget 2017, like Budget 2016, did not include any new tax incentives for the charitable and not-for-profit ("NFP") sector, as has been enjoyed in previous federal budgets. Legislation to implement certain proposals from Budget 2017 was introduced on April 11, 2017

---

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[1] Department of Finance Canada, *Budget 2017: Building a Strong Middle Class*, (Ottawa: 22 March 2017), online: http://www.budget.gc.ca/2017/docs/plan/toc-tdm-en.html.

[2] Canada Not-for-profit Corporations Act, SC 2009, c 23.

[3] *Corporations Act,* RSO 1990, c C.38.

[4] Not-for-Profit Corporations Act, 2010, SO 2010 c 15.

[5] Charities Accounting Act, RSO 1990, c C.10.

[6] *Supra*, note 1.

by means of Bill C-44, *Budget Implementation Act, 2017, No. 1* ("Bill C-44"),[7] which received Royal Assent on June 22, 2017. On September 8, 2017 the Minister of Finance released *Legislative Proposals Relating to the Income Tax Act and Explanatory Notes* which included proposals which would implement changes to the Ecological Gifts program mentioned in Budget 2017.[8]

Although Budget 2017 did not dramatically alter the legal and regulatory landscape for charities, there are, nonetheless, a number of important developments of note.

1. Ecological Gifts

The ITA provides for an ecological gifts program where certain donations of ecologically sensitive land or easements, covenants and servitudes on such land ("Ecogifts") give donors enhanced tax incentives. Budget 2017 proposes a number of measures in order to better protect Ecogifts. The implementing legislation for this proposal has yet to be tabled.

Currently, the ITA permits individual donors of Ecogifts to claim a charitable donation tax credit and corporate donors to claim a charitable donation tax deduction. In this regard, the amount of the donation (up to 100% of net income) may be claimed in a year and unused amounts may be carried forward for up to ten years. In addition, any capital gains associated with the donation of Ecogifts (other than a donation to a private foundation) are exempt from tax. In order to qualify for the Ecogifts program, the Minister of Environment and Climate Change Canada ("ECCC") must: (a) certify that the land is ecologically sensitive and that its conservation and protection is important to the preservation of Canada's environmental heritage; (b) approve the organization that will receive the gift if it is a registered charity (but approval is not necessary if the organization is the government of Canada, a province, a municipality in Canada, or a municipal or public body performing a function of government in Canada); and (c) certify the fair market value of the donation. In addition, any easements, covenants or servitudes involved must run in perpetuity. As well, in order to ensure donated land is not subsequently used for other

[7] Bill C-44, *Budget Implementation Act, 2017, No. 1*, 1st Sess, 42nd Parl, 2015-16-17 (assented to 22 June 2017), SC 2017, c 20.
[8] Ministry of Finance, "Legislative Proposals Relating to the Income Tax Act and Explanatory Notes", (Ministry of Finance: Ottawa, 08 September 2017), online: https://www.fin.gc.ca/drleg-apl/2017/ita-lir-0817-eng.asp.

purposes, the ITA imposes a 50% tax of the fair market value of the land upon a recipient who changes the use of the property or disposes of it without the consent of the Minister of ECCC.

Budget 2017 proposes the following changes to apply to transactions or events that occur on or after March 22, 2017:

- Where Ecogifts are transferred between organizations for consideration, the protection offered by the 50% tax may be inappropriately lost. To ensure that transfers of Ecogifts from one organization to another do not result in the loss of this protection, Budget 2017 proposes that the transferee of the property in such a situation be subject to the 50% tax if the transferee changes the use of the property, or disposes of the property, without the consent of the Minister of ECCC.
- Budget 2017 proposes to clarify that the Minister of ECCC has the ability to determine whether proposed changes to the use of lands would degrade conservation protections.
- Currently, an Ecogift that is proposed to be made to a registered charity must be approved by the Minister of ECCC on a gift-by-gift basis. However, approval is not necessary if the recipient organization is the government of Canada, a province, a municipality in Canada, or a municipal or public body performing a function of government in Canada. Budget 2017 proposes to extend the Ministerial approval requirements, on a gift-by-gift basis, to recipients that are municipalities as well as municipal and public bodies performing a function of government. However, Ecogifts proposed to be made to government of Canada or a province would still not require Ministerial approval.
- Budget 2017 proposes that private foundations will no longer be eligible to receive Ecogifts in order to prevent potential conflict of interest. An example of a scenario that may give rise to a conflict is where a director of a private foundation donates an easement in respect of a property to the private foundation so that the individuals responsible for enforcing the private foundation's rights under the easement would be the same persons as those against whom the rights must be enforced.

- In Quebec, where civil law applies, only real servitudes may be donated under the Ecogift program but not personal servitudes because they cannot run in perpetuity. As such, since the conditions associated with real servitudes can be difficult to meet, such donations are infrequently made. To encourage more Ecogifts in Quebec, Budget 2017 proposes that certain donations of personal servitudes may qualify as Ecogifts if they meet a number of conditions, including a requirement that the personal servitude run for at least 100 years.

In this regard, Budget 2017 proposes to amend various sections of the ITA, including subsection 43(2), paragraph 110.1(1)(d), the definition of "total ecological gifts" in subsection 118.1(1), and 207.31.

2. Repeal of Additional Corporate Donation Deductions on Medicine for International Aid

Budget 2017, through Bill C-44, repealed the additional corporate donation deductions on medicine for international aid by repealing paragraph 110.1(1)(a.1) and subsections 110.1(8) and (9) of the *Income Tax Act* ("ITA"),[9] as well as amending subsection 149.1(15) of the ITA. The repeal applies to gifts made after March 22, 2017. The special deduction for corporations was first introduced in the 2007 Budget to allow corporations that make donations of medicines from their inventory to claim a special additional deduction equal to the lesser of 50 percent of the amount, if any, by which the fair market value of the donated medicine exceeds its cost and the cost of the donated medicine. The goal of this deduction was to encourage corporations to provide medicines for the purpose of international aid.

Budget 2017 stated that this measure was to be repealed, "given the high compliance costs for charities and very low take-up." However, no changes are being made with regard to the normal ability for a corporation to deduct the fair market value of donated medicine.

While it is not clear what is meant by the "high compliance costs" for charities, in order for corporations to claim an eligible medical gift, a charity had to have applied to the Minister of International Development in order to be assessed concerning whether it met specific requirements under regulation 3505, including, among other requirements, that it have

[9] *Income Tax Act*, RSC, 1985, c 1 (5th Supp).

"sufficient expertise in delivering medicines for use in charitable activities carried on outside Canada".

3. Farewell First-Time Donor's Super Credit, We Hardly Knew You

Budget 2017 also confirmed that the First-Time Donor's Super Credit ("FDSC") "…will be allowed to expire in 2017 as planned, due to its low take-up, small average amount donated, and the overall generosity of existing tax assistance for charitable donations". This is not surprising given that the FDSC, first introduced in Budget 2013, was announced as a temporary tax-credit for the 2013 to 2017 taxation years, and *Economic Action Plan 2013 Act, No. 1,* which implemented the FDSC, included their repeal for the 2018 and subsequent taxation years. As a result, those hoping that the FDSC might be extended beyond 2017 will no doubt be disappointed that the eventual repeal of subsections 118.1(3.1), (3.2) and the definition of "first-time donor" in the ITA will proceed in 2018.

4. Amendments to Anti-terrorism Legislation

Budget 2017, through Bill C-44, makes a number of technical and substantive amendments to the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act*,[10] along with coordinating amendments to related legislation. Bill C-44 is largely silent concerning the effective date of the amendments to anti-terrorism legislation, but does state that the trust companies provision comes into force on a day to be fixed by the Governor in Council. Amendments made by Bill C-44 will expand the list of disclosure recipients, allowing for Financial Transactions and Reports Analysis Centre of Canada ("FINTRAC") to disclose designated information that is has reasonable grounds to suspect would be relevant to threats to the security of Canada to the Department of National Defence and the Canadian Armed Forces. Bill C-44's amendments will also expand the list of persons and entities to which record keeping, identification verification and reporting of suspicious transactions and registrations apply to include "trust companies incorporated or formed by or under a provincial Act that are not regulated by a provincial Act". Under certain circumstances, amendments made by Bill C-44 will

[10] Proceeds of Crime (Money Laundering) and Terrorist Financing Act, SC 2000, c 17.

also permit FINTRAC to disclose designated information to institutions or agencies of foreign states (including any political subdivisions or territories thereof) or to international organizations with similar powers and duties as FINTRAC's.

While developing a regime for greater transparency of beneficial ownership concerning corporate entities is an important initiative, Budget 2017's proposals purporting to "strengthen" the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act*, and the corresponding legislative amendments in Bill C-44, appear to be expanding Canada's already robust information collecting and sharing regime, which was most recently bolstered by Bill C-51 that the Liberal Party had campaigned to amend.

C. RECENT CRA PUBLICATIONS

1. New CRA Guidance on Charities That Assist the Aged[11]

On December 8, 2016, the CRA released a guidance entitled: *Relieving Conditions Attributable to Being Aged and Charitable Registration* (CG-026)[12] dealing with charities that assist the aged ("Guidance"). It replaces the CRA's Policy Statement CPS-002, *Relief of the Aged* that was released on July 6, 1990 ("Previous Policy").

The Guidance provides a much needed and helpful update on the Previous Policy, clarifying what the CRA considers charitable for Canadian charities serving the aged. For example, almost half of the Previous Policy (paragraphs 9 to 15) was in relation to the provision of housing for the aged, which has since been superseded by the CRA's guidance entitled: *Housing and Charitable Registration* (CG-022) dealing with charities that provide housing to their beneficiaries.[13]

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[11] This section of the paper is excerpted from *Charity & NFP Law Bulletin* No 396, "New CRA Guidance on Charities That Assist the Aged", prepared by Theresa Man, online: http://www.carters.ca/pub/bulletin/charity/2017/chylb396.pdf.

[12] Canada Revenue Agency, "Relieving Conditions Attributable to Being Aged and Charitable Registration", Guidance CG-026 (Ottawa: CRA 8 December 2016), online: https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/policies-guidance/relieving-conditions-attributable-being-aged-charitable-registration.html.

[13] Canada Revenue Agency, *Housing and Charitable Registration*, Guidance CG-022 (Ottawa: CRA 7 February 2014), online: https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/policies-guidance/housing-charitable-registration.html.

a) Age is Not Relevant

The Guidance clarifies that simply having attained a certain age is not a condition that is eligible for charitable relief. Instead, the eligible beneficiary group to be served must be those affected by one or more conditions attributable to being aged. This CRA position is consistent with the common law. Although the Previous Policy also stated that the CRA is of this view, the explanation in the Guidance is much clearer.

b) Conditions attributable to being aged

Since the age of the persons served is not relevant, it is necessary for charities to identify the conditions attributable to being aged for which relief is provided in order to be charitable. In this regard, the CRA provided a list of conditions attributable to being aged that are "generally" recognized by the CRA, including (i) frailty; (ii) social isolation; (iii) decline in motor skills, flexibility, strength, speed of execution, or hand-eye co-ordination; (iv) physical or mental health conditions attributable to being aged; (v) difficulty functioning in, or adapting to, current technology; and (vi) vulnerability to elder abuse.

While the Guidance indicates that the above list is not exhaustive, if an organization is established to relieve a condition not listed above, the organization would have to demonstrate that such a condition is eligible for relief by providing "objective, reliable, and relevant evidence." Such evidence could include the following:

- materials from impartial sources, such as articles in established academic and professional journals or publications confirming the benefit of the proposed activities to the identified beneficiaries
- submissions from persons independent of the organization that are qualified by relevant professional bodies or work experience to speak authoritatively on the subject or issue[14]

[14] *Supra* note 12 at para 29.

The Guidance further states that the sufficiency of the evidence will be assessed by the CRA based on the facts of each case, upon considering the "nature of the condition and all relevant information." As well, the CRA may conduct its own research before making a decision. It is possible that the CRA's list of acceptable needs associated with aging is not completely realistic or sufficiently broad. For example, the list does not include activities that address financial needs of seniors (such as credit and financial counselling) in light of the fact that debt of seniors has been on the rise in recent years. It is also of concern that the requirements on charities to provide extensive "objective, reliable, and relevant evidence" may prevent the sector from having sufficient flexibility in order to operate activities to relieve the ever-changing needs associated with the aged in Canada.

c) Required Charitable Purposes

To be eligible for charitable registration, the CRA requires that charities that relieve conditions attributable to being aged identify in their charitable purpose the following elements: a "purpose descriptor" (such as "to relieve conditions attributable to being aged"); the scope of the activities that will be conducted to relieve the identified conditions; the eligible beneficiary group; and the conditions attributable to being aged that will be relieved.

The Guidance lists examples of how acceptable purposes would need to be drafted, which is helpful since there were no examples in the Previous Policy. However, the sample purposes are drafted in a very specific and focused manner. Many organizations that provide services to seniors are multi-faceted rather than addressing only one or two of their needs.

d) Acceptable activities

The Guidance stated that the activities conducted to relieve conditions attributable to being aged must be "effectively relieving the condition, either directly or indirectly." In this regard, "relieving the condition" means "eliminating the presence of, or reducing the negative effects of, the condition." In other words, there must be a connection between the conditions that need to be relieved and how activities are conducted to relieve the identified conditions.

Therefore, the activities will vary depending on what conditions are intended to be relieved. As with the purposes, the Guidance lists the examples of acceptable activities.

The Guidance also states that any private benefit conferred as part of the delivery of the activity must be "incidental to achieving the charitable purpose (meaning the private benefit is necessary, reasonable, and proportionate to the resulting public benefit)." This is consistent with the requirement to meet the CRA's policy on the public benefit.[15]

e) Special Topics

The Guidance makes specific reference to a number of special issues that come up for charities serving the aged in the community. For example, it makes reference to the CRA's guidance on housing (referred to above). It further clarifies that residents at these facilities are not required to be assessed using an income threshold or other financial criteria, and that the housing does not have to be provided at less than fair market value. It is also helpful that the Guidance specifically clarifies that "[a]n organization can conduct its activities according to specific cultural traditions, in the language of its choice, or according to particular religious beliefs, as long as its benefits are made available to anyone in the eligible beneficiary group described in its purpose." This is good news because it recognizes the needs of the multicultural population of Canada and thereby the need for activities that are sensitive to cultural background, language, and religious belief.

Of note, the Guidance acknowledges that some activities that relieve conditions attributable to being aged could also further other charitable purposes. It gives the example that providing mobility aids to the aged who have a physical condition could also promote health and therefore must also meet the requirements in the CRA's Guidance CG-021, *Promotion of Health and Charitable Registration*. As well, an organization that provides health care products and services must meet the applicable requirements relating to effectiveness, quality and safety set out in that guidance. This requirement is problematic. The CRA's requirement means that if an

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[15] Canada Revenue Agency, Policy Statement CPS-024, *Guidelines for Registering a Charity: Meeting the Public Benefit Test*, (Ottawa: CRA, 10 March 2006, online: https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/policies-guidance/policy-statement-024-guidelines-registering-a-charity-meeting-public-benefit-test.html.

activity could fall within two heads or subcategories of charity, then the charity would need to meet both sets of CRA criteria. In essence, the CRA is requiring that the charity has two thresholds to meet. If it is charitable for a charity to provide health care related services (such as mobility aids, healthy living counselling, etc.) to the aged to relieve a condition associated with aging, that, in and of itself, is already charitable. It is unnecessary to also require the charity to meet the separate requirements in the health care guidance.

2. CRA's New Cause-related Marketing Webpage

On February 11, 2017, the CRA introduced a new webpage to explain Cause-related Marketing, which was further updated on February 21, 2017.[16] In general terms, cause-related marketing is defined by the CRA as fundraising activity where a registered charity (or other qualified donee) works with a for-profit entity to promote the sale of the for-profit's items or services on the basis that part of the revenues will be donated to the registered charity.

The benefit that the for-profit entity receives under the arrangement is considered an advantage. In order for a registered charity to issue an official donation receipt for a donation, the charity must first be able to calculate the value of any advantage the donor (*e.g.* the for-profit entity) received. The value of the advantage to a donor is normally subtracted from the amount of the donation in order to calculate the eligible amount of the gift for purposes of the official donation receipt.[17]

However, some advantages are considered by the CRA as too minimal to affect the value of a gift. If the value of all advantages related to a gift is not more than $75 or 10% of the amount gifted to the charity (whichever is less), the charity does not need to subtract those amounts from the gift amount when issuing a receipt. It should be noted that where an advantage is more than 80% of the amount gifted to the charity, the CRA takes the position there was no intention to make a gift and therefore, the charity cannot issue a receipt.

[16] Canada Revenue Agency, "Cause-related Marketing", (Ottawa: CRA, 11 February 2017), online: https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/operating-a-registered-charity/issuing-receipts/cause-related-marketing.html?rss.
[17] *Supra* note 9, section 248(30).

Since it can be very difficult to calculate the value of an advantage in cause-related marketing arrangements, the CRA webpage suggests that where a charity is not able to issue an official donation receipt, the for-profit entity may seek professional advice to determine whether the expenses from the cause-related marketing arrangement can be claimed as an advertising expense.

3. New Privacy Disclosure in T2050 Application to Register a Charity Under the ITA

On February 21, 2017, the CRA updated the T2050 "Application to Register a Charity Under the *Income Tax Act*", the application form that must be completed and submitted to the CRA when applying for charitable registration.[18]

The update to Form T2050 includes a new privacy disclosure on the last page indicating that personal information is being collected under the authority of the ITA in order to validate the identity and contact information of directors, officers and authorized representatives of the applicant organization. The information is also used as a basis for the indirect collection of additional personal information from other internal and external sources, which includes social insurance numbers, personal tax information, and relevant financial and biographical information, which may be used by the CRA "to assess the overall risk of registration with respect to the obligations of registration as outlined in the ITA and the common law."

The disclosure states that where the application for charitable status is approved, the CRA is permitted to make the form (including any attachments) and copies of the registration letter (including any conditions and warnings contained therein) available to the public, with the exception of the confidential information in Part 5 and Part 6 of the Form T2050. If registration is denied, the information will not be provided to the public. Personal information may also be shared with other government departments and agencies under information-sharing agreements, which may include RCMP, CSIS, as well as foreign governments and agencies in accordance with section 241 of the ITA.

[18] Form available on the CRA's website: https://www.canada.ca/en/revenue-agency/services/forms-publications/forms/t2050-application-register-a-charity-under-income-tax-act.html.

The CRA privacy disclosure encourages applicant organizations to voluntarily inform directors and officers that their personal information has been collected and disclosed to the CRA for the application process. The CRA privacy disclosure also requires that those signing the T2050 on behalf of the applicant confirm they have read the said privacy disclosure.

4. Sweeping Changes Recommended in Report on Political Activities

On May 4, 2017, the CRA published on its website the *Report of the Consultation Panel on the Political Activities of Charities* (the "Report"),[19] prepared after the CRA's consultation with the charitable sector between September 2016 and December 2016 (the "Consultation"). In conjunction with the release of the Report, the Minister of National Revenue announced, on the same day, the Liberal government's suspension of all remaining CRA audits of charities for political activities that had been initiated through the 2012 Federal Budget. The suspension is to remain in place pending the implementation of the Report's recommendation.

The Report states that the "legislative framework for regulating charities is out-dated and overly restrictive" and calls for changes to the current administrative and legislative framework governing "political activities" by charities. In doing so, the Report provides four recommendations, including the immediate suspension of the political activity audits that was acted upon by the Minister of National Revenue. The CRA had committed to providing a formal response to the Consultation Panel's recommendations by the end of June 2017, though no formal response has been published as of October 2017.

a) The Report and Recommendations

The Report explains that there has been much confusion concerning the limits of what charities can say, how much they can say, and to whom they can speak when it comes to advocating for public policy change. The confusion stems from the often conflated terms

[19] Canada Revenue Agency, *Report of the Consultation Panel on the Political Activities of Charities*, Government of Canada, online: https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/resources-charities-donors/resources-charities-about-political-activities/report-consultation-panel-on-political-activities-charities.html [the "Report"]. The Report was prepared by a panel appointed by the Minister of National Revenue, consisting of Marlene Deboisbriand (Chair), Shari Austin, Susan Manwaring, Kevin McCort and Peter Robinson.

"activities" and "purposes" in the ITA.[20] While the Report indicates that "political purposes" are prohibited, subsections 149.1 (6.1) and (6.2) of the ITA permit charities to carry out a limited amount of what the Report refers to as "non-partisan political activities" to achieve their charitable purposes. However, many of these key terms remain undefined, and the line between a charity having a political purpose and conducting political activities to achieve its charitable purposes remains unclear.

In particular, the Consultation found a consistent, sector-wide call for legislative change, with many charities stating that administrative changes would be insufficient to address fundamental issues with the current legislative framework over political activities. In response to the Consultation, the Report provided four recommendations to change both the administration of the ITA and the ITA itself with regard to political activities by charities, as well as a broader recommendation to modernize the legislative framework for charities. A brief summary of these recommendations follows.

b) Full Public Policy Dialogue and Development

To eliminate confusion over acceptable activities and how to calculate political activities, the Report recommends that the CRA immediately revise its Policy Guidance CPS-022, Political Activities (the "Political Activities Guidance")[21] to define "political activities" to mean "public policy dialogue and development" and to expressly permit charities to fully engage in them where doing so would further the charity's charitable purposes, and they are non-partisan and subordinate to the charitable purposes. In this regard, the Report recommends that the Political Activities Guidance view "public policy dialogue and development" as entailing "providing information, research, opinions, advocacy, mobilizing others, representation, providing forums and convening discussions." Examples of such activities provided in the Report include: providing information on their charitable objects to sway public opinion, engaging in advocacy and mobilizing the public to support keeping or changing law or policy, and expressing non-partisan

[20] *Supra* note 9.
[21] Canada Revenue Agency, *Policy Guidance CPS-022, Political Activities*, (Ottawa: CRA, 2 September 2003), online: https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/policies-guidance/policy-statement-022-political-activities.html.

views on social media. This recommended change in terminology from "political activities" to "public policy dialogue and development" is insightful and welcome because it removes the misunderstanding that any contact with a politician is "political" and actually reflects the contribution that charities can make not only to programs but also to social and economic policy development because of their experience and expertise.

The Report also recommends that the CRA remove its policy requirement that charities' materials reflect all sides of an argument, and instead add a requirement that they be fact-based. It further recommends that charities should not be required to quantify or report on the quantification of political activities on the T3010, Registered Charity Information Return, but instead be required to provide only a narrative description of the nature of public policy dialogue and development work that they undertake.

c) Changes to CRA Compliance and Appeals, Audits, Communication and Collaboration

To enhance clarity and consistency, the Report recommends implementing changes to CRA administration of the ITA in the areas of compliance and appeals, audits, communication and collaborative approaches. The recommendations generally focuses on greater transparency and communication between the CRA and the charitable sector, consistency in information provided, as well as enhanced avenues through which charities can receive guidance on issues, such as an expanded Charities Liaison Officer role and access to the Taxpayers' Ombudsman.

Concerning compliance and audits, the Report's recommendations include ensuring consistency in the CRA's application of the compliance continuum and consulting with the sector when identifying thematic audit topics. Concerning appeals, the Report recommends that appeals should be heard by the Tax Court of Canada rather than by way of judicial review at the Federal Court in order to level the playing field and enhance fairness in a system that is currently perceived to be biased in favour of the CRA. Concerning communication and collaboration, the Report recommends reinstating in-person programs, such as Charities Information Sessions and the Charities Partnership and Outreach Program, as well as the establishment of a high-level standing working group to identify and address issues of concern to charities.

d) Removal of Legislative Reference to Non-partisan Political Activities

The third recommendation in the Report is to "[a]mend the ITA by deleting any reference to non-partisan political activities to explicitly allow charities to fully engage without limitation in non-partisan public policy dialogue and development, provided that it is subordinate to and furthers their charitable purposes". The Report's recommendation to delete any reference to "non-partisan political activities" is somewhat unclear, as there is no mention of such term in the ITA. Nonetheless, the recommendation goes on to provide some clarity by proposing to "retire the term "political activities", which the Report says tends to be understood as partisan. It reasoned that doing so would provide clarity and certainty for the charitable sector and the CRA, and would explicitly allow charities to be fully engaged in "non-partisan public policy dialogue and development." Similarly, the Report recommends retaining the prohibition on "partisan political activities" and political purposes for charities.

e) A Modern Legislative Framework that Focuses on Charitable Purposes

As a more long-term solution, the Report recommends the modernization of the ITA dealing with charities. Specifically, the Report recommends a focus on charitable purposes rather than activities, an inclusive list of charitable purposes reflecting contemporary issues, and the ability to appeal the Tax Court of Canada's refusal to register, or to revoke, charitable status.

Building on its mandate, the Report suggests additional legislative changes, including removing the need for charities to maintain "direction and control" of non-qualified donees in certain circumstances. Doing so, the Report states, would enable charities to work with partners "as equals in furtherance of their charitable purposes". The Report further recommends greater accommodation of social enterprise and social finance models that would benefit the charitable sector.

f) The Way Forward

The current suspension of the political activity audits comes as a result of the Liberal government's commitment that it would "[a]llow charities to do their work on behalf of Canadians free from political harassment, and modernize the rules governing the charitable and

not-for-profit sectors … [by] clarifying the rules governing "political activity," with an understanding that charities make an important contribution to public debate and public policy."[22]

However, notwithstanding the Minister of National Revenue's announcement of the suspension of ongoing audits of charities for political activities, it remains to be seen how the Federal Government and the CRA will respond to the remainder of the Report's recommendations. In particular, many of the recommendations touched on issues related to the regulation of charities that are not limited to political activities, and would require extensive changes to the ITA concerning the administration of charities, *e.g.*, providing for an inclusive list of charitable purposes or permitting appeals to the Tax Court of Canada as opposed to the Federal Court of Appeal.

Nonetheless, the Report and the announcement by the Minister constituted extremely good news for the charitable sector and a hope for the future given that the political audits mandated by the previous government in 2012 have been seen as having created an unjustified and unnecessary "chill" effect on charities in Canada with regard to public policy and advocacy.

The CRA is to be commended for the process that it used in this consultation, being a combination of on-line and in-person consultations in seven major cities and appointing a panel of five sector representatives to review the consultation submissions and provide recommendations to the CRA which have now been made public in their report.

5. Changes to Charitable Registration Application Process

In late June 2017, the CRA sent an email to key stakeholders announcing a number of upcoming changes to the charitable registration process. This was subsequently posted on the CRA's website.[23] The announcement stated that the Charities Directorate would no longer review applications submitted with draft governing documents. Such applications would be considered incomplete and returned to the applicant. The CRA also recommended that trust documents

[22] Office of the Prime Minister of Canada, *Minister of National Revenue Mandate Letter*, online: Government of Canada http://pm.gc.ca/eng/minister-national-revenue-mandate-letter.
[23] Canada Revenue Agency, *What's New – June 2017*, (Ottawa: CRA, 29 June 2017), online: https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/whats-new.html.

include a clause allowing trustees to amend or alter the purpose(s) of the trust in order to meet the legislative and common law requirements for charitable registration. As well, if an applicant believes that the purposes in its governing documents do not accurately reflect its programs, proposed purposes can be included in the application, along with its current certified governing documents. These changes came into effect July 1, 2017.

6. Voluntary Disclosure and Canadian Registered Charities in Context

On June 9, 2017, the Ministry of National Revenue announced changes to the Canada Revenue Agency (the "CRA") Voluntary Disclosures Program ("VDP") by publishing two documents outlining the proposed changes as of January 1, 2018, the Draft Information Circular - IC00-1R6 - Voluntary Disclosures Program[24] and the Draft GST/HST Memorandum 16.5 – Voluntary Disclosures Program (collectively, the "Proposals").[25] The general purpose of the VDP is to provide taxpayers with an opportunity to voluntarily come forward and correct previous omissions in their dealings with the CRA in order to avoid penalties and prosecutions. The Proposals outline extensive proposed changes to the VDP aimed at preventing abuse of the system by sophisticated taxpayers, including those with offshore accounts in order to avoid detection by the CRA. The Proposals were open for public consultation for a period of 60 days from June 9, 2017. While the VDP has application to non-profit organizations under paragraph 149(1)(l) of the ITA ("NPOs"), it only applies to registered charities in the very limited context of employee source deductions and HST. As such, the specifics of the Proposals will be of limited interest to registered charities, although they have been attracting a lot from the media.

In lieu of the VDP applying to registered charities, other than in the above mentioned limited context, it is important to be aware that the CRA does provide a voluntary disclosure process for charities that have been involved in matters of non-compliance and would like to bring themselves back into compliance.

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[24] Canada Revenue Agency, *Draft Information Circular – IC00-1R6 Voluntary Disclosures Program*, (Ottawa: CRA, June 2017), online: https://www.canada.ca/en/revenue-agency/campaigns/ic00-1r6-voluntary-disclosures-program.html.

[25] Canada Revenue Agency, *Draft GST/HST Memorandum 16.5 – Voluntary Disclosures Program*, (Ottawa: CRA, June 2017), online: https://www.canada.ca/en/revenue-agency/campaigns/16-5-gst-memorandum-vdp-draft.html.

This voluntary disclosure process is set out on the CRA webpage entitled, "Bringing Charities Back into Compliance" (the "CRA Guide").[26] The CRA Guide encourages registered charities that have been involved in unintentional or accidental matters of non-compliance to contact the Charities Directorate at the CRA in writing, either on a general or no-name basis, or by telephone, in order to provide a "complete and accurate description" of the non-compliance. After contacting the CRA, charities may be required by the CRA to correct the effects of past non-compliance within a reasonable timeframe, enter into a compliance agreement outlining the steps to rectify the non-compliance, or present a plan to demonstrate what action has been taken or what measures will be put into place to prevent future non-compliance. There is nothing, though, in the CRA Guide that promises a particular outcome as there is in certain circumstances with the VDP.

Not every matter of non-compliance warrants proceeding with a voluntary disclosure to the Charities Directorate. However, serious matters of non-compliance or repeat non-compliance that could lead to a sanction (financial penalty or suspension of receipting privileges) or revocation of charitable status, with the associated stigma of directors and officers possibly being found to be "ineligible individuals" under the ITA, may benefit from a pre-emptive disclosure to the Charities Directorate. Since the disclosure must be voluntary, it must be started before the CRA has commenced its audit. The end goal is to have the charity with one or more serious compliance issues end up with a negotiated compliance agreement with the Charities Directorate, as opposed to leaving the charity exposed to the risk of sanctions or revocation if a CRA audit was to occur without a disclosure.

However, in making a voluntary disclosure, the CRA may examine other non-compliance issues not disclosed by the charity. It is, therefore, important to conduct a due diligence review identifying all issues of non-compliance before commencing a voluntary disclosure with the Charities Directorate in order for those non-compliance issues to be afforded the benefits of the voluntary disclosure process.

[26] Canada Revenue Agency, *Bringing Charities into Compliance*, (Ottawa: CRA, March 2016), online: https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/compliance-audits/bringing-charities-back-into-compliance.html.

Given the limited scope of the CRA Guide to assist charities wanting to come back into compliance compared to the VDP available for for-profits and NPOs (even with the changes outlined in the Proposals), it would be a help to the charitable sector if the Charities Directorate was to develop a more robust voluntary disclosure program for registered charities similar in scope to the VDP. In this regard, in a letter addressed to the Charities Directorate dated August 8, 2017,[27] the Charities and Not-for-Profit Law Section of the Canadian Bar Association recommended the development of a guidance dealing with voluntary disclosures by registered charities and that such guidance be addressed by the Charities Directorate of the CRA, as opposed to the Tax Services Offices under the VDP.

Until such guidance is available, charities that discover they are non-compliant should work with legal counsel under the protection of solicitor-client privilege with respect to the current CRA Guide to determine if and how best to make a disclosure to the CRA, and what steps may be necessary to bring the charity back into compliance.

7. CRA to Update Business Numbers to Provide e-Services Starting in November 2018

On September 22, 2017, following an e-mail sent to certain stakeholders on July 21, 2017, the Charities Directorate of the Canada Revenue Agency ("CRA") announced that, once the Charities IT Modernization Project (CHAMP)[28] is implemented, registered charities will be able to use their business numbers,[29] through the CRA's "My Business Account" portal,[30] to file their information returns online, as well as to update and manage their account information, check file status and received and manage their communications with the CRA. The announcement further states that, over the next few months and until October 2018, charities' internal divisions

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[27] Letter from the Charities and Not-for-Profit Law Section of the Canadian Bar Association (8 August 2017), online: http://www.cba.org/CMSPages/GetFile.aspx?guid=cd9d9e47-fc78-4d20-892b-bd7d90784dcc.

[28] Canada Revenue Agency, *Report on the Charities Program 2015-2016*, (Ottawa: CRA, 2016), online: https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/about-charities-directorate/report-on-charities-program/report-on-charities-program-2015-2016.html#N10AC5.

[29] Canada Revenue Agency, *RC2 The Business Number and Your Canada Revenue Agency Program Accounts*, (Ottawa: CRA, 2016), online: https://www.canada.ca/en/revenue-agency/services/forms-publications/publications/rc2-business-number-your-canada-revenue-agency-program-accounts.html.

[30] Canada Revenue Agency, *About my Business Account*, (Ottawa: CRA, 2016), online: https://www.canada.ca/en/revenue-agency/services/e-services/e-services-businesses/business-account/about-business-account.html.

sharing the business numbers of their head bodies will be assigned unique business numbers so they can access these online services. This process does not require any action from impacted charities, as their internal divisions will continue to operate under the governing documents currently on file with the CRA. More information is expected to be available on the Charities Directorate website soon.

8. CRA Releases New Guidance on Head Bodies and Internal Divisions

On September 22, 2017, the CRA published a new guidance, CG-028, "Head bodies and their internal divisions" (the "Head Bodies Guidance"),[31] which outlines the CRA's requirements for the charitable registration of head bodies and their internal divisions. For the purpose of the Head Bodies Guidance, a head body is a registered charity that has authority over its internal divisions, is resident in Canada, and was either created or established in Canada. The Head Bodies Guidance states that a head body's governing documents must permit it to exert authority over its internal divisions by taking actions, such as appointing and controlling their boards, approving their budgets and creating them or closing them down. Although "internal division" is not defined under the ITA, the Head Bodies Guidance considers internal divisions to be branches, parishes, sections or other divisions of a registered charity that operate as extensions of and under the authority of the head body, further its charitable purposes, are not separately incorporated but rather operate under the head body's governing documents and receive donations on their own behalf. Internal divisions have their own charitable numbers and are registered separately with the CRA from the head body but are subordinate to it. To register an internal division, the internal division must submit to the CRA a letter of good standing from the head body outlining the internal division's relationship with the head body, together with the governing document that created or established the head body. The Head Bodies Guidance also provides information concerning requirements of head bodies and internal divisions after registration, as well as a helpful chart outlining the differences between registered charities, head bodies and internal

[31] Canada Revenue Agency, *CG-028, Head Bodies and Their Internal Divisions*, (Ottawa: CRA, 2 September 2017), online: https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/policies-guidance/head-bodies-and-their-internal-divisions.html.

divisions, and sample scenarios to understand whether or not an organization is an internal division.

9. Changes to CRA's CG-014 CED Guidance

On September 22, 2017, the Charities Directorate of the CRA announced recent changes to the CG-014 "Community Economic Development Activities and Charitable Registration" ("CED Guidance") to include exceptions to charitable activities aimed at improving socio-economic conditions in areas affected by a disaster. According to the new Appendix A, a disaster is "a hazard that overwhelms a community's ability to cope and may cause serious harm to people's safety, health, welfare, property, or the environment" and it can be a natural phenomenon or the result of human action. Accordingly, the area is presumed to be in need for two years after the date of the disaster, but the charity may continue to work in the area provided it shows continuing need. The new CED Guidance describes the ability of charities to support local small businesses and it provides a list of requirements for charities to show that the benefit the businesses receive is only incidental to the work of the charity.

D. RECENT TAX DECISIONS, RULINGS, AND INTERPRETATIONS INVOLVING CHARITIES

1. Income Tax Treatment for Monies Paid to Support Refugees

On March 3, 2017, the CRA released technical interpretation 2016-0651661E5 – Payments to Syrian refugees by a church. This technical interpretation was in response to a letter received by the CRA from a church inquiring about the income tax treatment of payments made by the church to support a Syrian refugee family (the "family"). Specifically, the church asked whether the money received by the family was to be included as income in the family's tax returns, and whether there are any special rules for refugees for income tax purposes.

In terms of background, the inquiring church was a private sponsor that has established a fund to support a particular Syrian refugee family, and had provided support to the family since they arrived in Canada. The monies provided by the church were to assist the family with their living expenses. The family also received money through the Resettlement Assistance Program provided by the government.

In response to the questions asked, the CRA noted that paragraph 56(1)(u) of the ITA requires social assistance payments received in the year and made on the basis of a means, needs, or income test are to be included in a taxpayer's income, unless they are included in the taxpayer's spouse's or common-law partner's income. The CRA further noted that income included under paragraph 56(1)(u) will be offset by a matching deduction under paragraph 110(1)(f) of the ITA. As such, there will be no income tax implications, other than potentially affecting certain income-tested benefits. Accordingly, the CRA indicated that "if the payments made by the church are assistance made on the basis of "means, needs or income test," then they are likely social assistance payments for purposes of paragraph 56(1)(u)" of the ITA.

"Social assistance" is not defined under the ITA, but, with reference to paragraph 56(1)(u), the CRA indicated that it is generally understood to mean "aid provided by a government or government agency, although it can be provided by other organizations (such as a church), on the basis of need." With respect to the means, needs, or income test, the CRA advised that it considers them to be financial tests and describes them as follows: "1. [a]n "income" test, which is a test based solely on the income of the applicant, 2. [a] "means" test, which is similar to an income test, but also takes into account the assets of the applicant, [and] 3. [a] "needs" test, which takes into account the income, assets and financial needs of the applicant."

In its response, the CRA also noted that subsection 233(1) of the *Income Tax Regulations*[32] requires organizations providing social assistance to report such assistance on Form T5007-Statement of Benefits, unless expressly exempted.

This technical interpretation is helpful to organizations providing assistance to refugees in Canada, as well as all organizations, including NFPs and charities that provide assistance based on a means, needs or income test.

[32] CRC, c 945.

Further information on the provision of social assistance, the resulting reporting requirements and form T5007 can be found on the CRA website[33], as well as in the CRA's pamphlet T4055 Newcomers to Canada.[34]

2. Administrative Penalty Assessed for False Statements on Donation Receipts

On April 25, 2017, the Tax Court of Canada (the "Court") released its decision in *Ploughman v The Queen* (the "Ploughman Decision"), an appeal by Glenn Ploughman ("Ploughman"), from the CRA's assessment under section 163.2 of the ITA, often referred to as the third-party penalty provision.

The Court found that Ploughman participated in the making of, or assented to or acquiesced in the making of, false statements by 135 participants in a charitable donation program. The background facts of this case are complex and it is beyond the scope of this paper to describe in detail. However, in general terms, the Court found Ploughman was a creator or promoter of a charitable donation program ("Donation Program") that was based on the creation of a timeshare property and the donation of vacation ownership weeks to registered charities by participants in the Donation Program. However, timeshare units were never created and therefore vacation ownership weeks were never actually donated by any participants. Each of the 135 official receipts issued to participants in the Donation Program, which stated that each donor had made an in-kind donation of a specified number of "Biennial Weeks Vacation Ownership at Arawak Inn & Beach Resort", contained a false statement.

Based on the evidence, the Court found that when Ploughman sent a letter to the participants in the Donation Program recommending that they submit their charitable receipts to the CRA, he knew or would reasonably be expected to have known, but for circumstances amounting to culpable conduct, that each of the official receipts contained a false statement. Further the Court found that Ploughman's indifference concerning the non-existence of the

[33] Canada Revenue Agency, "T4115 T5007 Guide - Return of Benefits", (Ottawa: CRA, 20 December 2016), online: https://www.canada.ca/en/revenue-agency/services/forms-publications/publications/t4115-t5007-guide-return-benefits.html.
[34] Canada Revenue Agency, "T4055 Newcomers to Canada - 2016", (Ottawa: CRA, 21 December 2016), online: https://www.canada.ca/en/revenue-agency/services/forms-publications/publications/t4055-newcomers-canada-2016.html.

timeshare units, the failure to implement other transactional steps on which the Donation Program was based, and his indifference as to whether his recommendation in that letter was well founded, showed an indifference concerning whether the ITA was complied with and thus constituted culpable conduct.

Subsection 163.2(6) of the ITA provides a safe harbour for an advisor who relies, in good faith, on information provided by or on behalf of a person who makes a false statement. However, the Court found that Ploughman's reliance on the legal opinion letter of Ms. Guindon (the lawyer who had provided the legal opinion concerning the Donation Program as described below) did not satisfy the statutory criteria of subsection 163.2(6) of the ITA. The Court noted that subsection 163.2(6) of the ITA applies only where the advisor is acting on behalf of the person who makes the false statement, but the Donation Program involved a number of participants who were clients of other canvassers, such that Ploughman may not have been acting on behalf of those participants. In addition, the Court found Ploughman was not acting in good faith.

The Donation Program was previously at the centre of a 2015 case, *Guindon v Canada*. In that case, Guindon, a lawyer without expertise in tax law, provided a legal opinion on the tax consequences of a leveraged donation program and signed 135 charitable receipts totalling $3,972,775 in her capacity as the president of a registered charity. Guindon was found liable under s. 163.2(4) of the ITA for knowingly assisting another taxpayer with making false statements or omissions in a tax return.

3. CRA Issues a Technical Interpretation of Charities Returning Gifts

On May 17, 2017, the CRA released technical interpretation 2016-0630351, dated March 31, 2017, and provided its response to the questions "1) Can a registered charity return a gift of a life insurance policy to a donor?" and "2) If so, what are the tax consequences to the registered charity and to the donor?" In 1981, the donor gifted a life insurance policy to a foundation which supports a college. The gift was intended to form a scholarship for a specific program. That program, though it existed at the time of the gift, no longer exists. The donor therefore believed that a condition of the gift was not fulfilled, and requested that the gift be returned. The

foundation would be willing to do so if the CRA could assure the donor there would be no "negative impact on its registered status".

The technical interpretation first refers the donor to Guidance CG-016 Qualified donees – Consequences of returning donated property, and notes that in most cases a charity cannot return a gift.[35] It then says that there are some cases in which a charity may be obligated to return gifts due to trust law, but that those are ultimately a decision for the court, rather than the CRA, to make, as those scenarios do not fall under the ITA. As to the tax consequences, the letter points to the rules under the ITA which apply in situations where there was no gift at law or there was a gift at law that needed to be returned, and the charity had given the donor a charitable donation receipt. In such a case, the donor cannot retain the tax benefit of such a receipt.

For the potential impact on a qualified donee, the letter refers to Guidance CG-016 and to the "Returning a gift to a donor" webpage.[36] It recommends that "before returning gifted property, qualified donees should determine if other provincial or federal legislation might affect their ability to legally return donated property." It further warns that "a registered charity that returns gifted property could be regarded as making a gift to a non-qualified donee or providing an undue benefit, which are contraventions of the Act and could result in sanctions that include revocation of registered status." The letter ends by saying that the determination of whether the gift can be legally returned is beyond the scope of the technical interpretation. The view is an important reminder that when donors and charities are discussing the potential return of charitable property, the common law and provincial jurisdiction should also be considered in addition to any potential income tax consequences.

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[35] Canada Revenue Agency, CG-016, *Qualified donees – Consequences of returning donated property*, (Ottawa: CRA, 18 October 2012), online: https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/policies-guidance/guidance-016-qualified-donees-consequences-returning-donated-property.html.

[36] Canada Revenue Agency, *Returning a gift to a donor*, (Ottawa: CRA, 08 April 2016), online: https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/operating-a-registered-charity/receiving-gifts/returning-a-gift-a-donor.html.

E. CORPORATE LAW UPDATE

1. Corporations Canada Dissolves Part II CCA Corporations

On February 13, 2017, Corporations Canada released a notice advising that all federal corporations created under Part II of the *Canada Corporations Act* ("CCA")[37] needed to have completed their transition to the CNCA and have received their certificate of continuance by July 31, 2017. Notwithstanding the original deadline of October 17, 2014 for CCA Part II corporations to continue under CNCA, there were still a number of federal not-for-profit corporations that had not done so and that received notices of pending dissolution from Corporations Canada.

Following this deadline, Corporations Canada dissolved most Part II CCA corporations that had not continued by the deadline. However, Corporations Canada is also continuing to work with a small number of corporations that have filed transition applications but have not completed their continuance due to various deficiencies. Apart from this small exception, all federal not-for-profit corporations now operate under the CNCA or have been dissolved. After all Part II CCA corporations have been continued or dissolved, the process to repeal Part II of the CCA and its regulations can begin. However, Part II CCA corporations dissolved because they failed to transition to the CNCA can apply to be revived and transitioned into the CNCA in one step by submitting Form 4032: *Articles of Revival (transition)* after having obtained approval from the members. For more information see Corporations Canada's Revival (transition) guide.[38]

2. Corporations Canada Increases Online Services

In accordance with a May 17, 2017 announcement, Corporations Canada has begun providing a new service to allow not-for-profit corporations incorporated under the CNCA to submit requests online to amend their articles of incorporation. The service is provided through its Online Filing Centre[39] for a fee of $200. The service standard for the amendment is "Same

[37] Canada Corporations Act, RSC 1970, c C-32.
[38] Corporations Canada, *Revival (transition) guide*, (Ottawa: Corporations Canada, 05 January 2016), online: https://www.ic.gc.ca/eic/site/cd-dgc.nsf/eng/cs06603.html.
[39] Corporations Canada Online Filing Centre, online: https://www.ic.gc.ca/app/scr/cc/CorporationsCanada/hm.html?locale=en_CA.

day/Next Day Service". The Online Filing Centre already allows federal not-for-profit corporations to incorporate, file annual returns, and file by-laws online, among other services.

3. Ontario Corporations Now Required to Keep Records of Land Ownership

On December 10, 2016, certain provisions of Bill 144, the *Budget Measures Act, 2015* ("Bill 144"),[40] which enacted the *Forfeited Corporate Property Act, 2015* ("FCPA")[41] and the *Escheats Act, 2015* ("EA"),[42] came into force creating new recordkeeping obligations for Ontario corporations designed to assist in dealing with situations where corporations dissolve without having properly disposed of all of their assets.

Bill 144 also introduced the new recordkeeping obligations for both new and existing Ontario corporations by way of amendments to the Ontario *Business Corporations Act* ("OBCA")[43] the OCA, and the ONCA (when it comes into force). These amendments provide that Ontario corporations are now required to maintain a register of ownership interests in land in Ontario at their registered office. This includes:

- The identity of each property in Ontario in which the corporation possesses an "ownership interest";
- The date on which the corporation acquired the property and, if applicable, the date on which it disposed of it; and
- A copy of any deed, transfers or similar documents that contain the municipal address, the registry or land titles division and the property identifier number, the legal description, and the assessment roll number of each property listed on the register, if any.

"Ownership interest" is an undefined term thereby implying that these measures could extend to both legal and beneficial ownership in real property. These may also include where the corporation has an interest in property by way of lease or other arrangement. These requirements are unique to Ontario, as currently other jurisdictions in Canada in which charities

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[40] *Budget Measures Act*, 2015, SO 2015, c 38 - Bill 144.
[41] Forfeited Corporate Property Act, 2015, SO 2015, c 38, Schedule 7.
[42] *Escheats Act, 2015*, SO 2015, c 38, Schedule 4.
[43] RSO 1990, c B.16.

and NFPs might incorporate are not required to maintain such registers. While for some corporations the creation and maintenance of such registers will likely be straightforward, it is anticipated that corporations with a history in the province will need time and effort in order to review all prior documentation dealing with their ownership interests in land.

Corporations incorporated after December 10, 2016 must comply with the new recordkeeping requirements immediately. For corporations that were incorporated prior to December 10, 2016, they will have two years, *i.e.*, until December 10, 2018, to comply with the new requirements.

4. Bill 154 - Amendments to the ONCA

Bill 154, *Cutting Unnecessary Red Tape Act, 2017* ("Bill 154"),[44] was introduced in the Legislative Assembly of Ontario on September 14, 2017. In addition to other proposed amendments affecting charities and not-for-profits discussed below, Bill 154 introduces amendments to the ONCA substantially similar to those contained in Bill 85, *Companies Statute Law Amendment Act, 2014* ("Bill 85"),[45] which had died on the order paper upon the dissolution of the Provincial Parliament on May 2, 2014.

In this regard, Bill 85 had proposed a new section 207 of the ONCA that would have required that Part III OCA corporations amend their articles of incorporation by the end of the three-year transition period, even though the ONCA also contained a deemed amendment provision (subsection 207(6)). The new section 207 of the ONCA, as proposed in Bill 154, provides an extended period of validity for certain by-laws and special resolutions not added to the articles even beyond the three-year anniversary of the section coming to force. The by-laws and special resolutions that may be valid are listed in the proposed subsection 207(3) as:

- A provision respecting the number of directors of the corporation;
- A provision providing for two or more classes or groups of members;
- A provision respecting voting rights of members;

[44] Bill 154, *Cutting Unnecessary Red Tape Act, 2017*, 2nd Sess, 41st Parl, Ontario, 2016-17 (second reading 3 October 2017).
[45] Bill 85, *Companies Statute Law Amendment Act, 2014*, 2nd Sess, 40th Parl, Ontario, 2013-14.

- A provision respecting delegates made pursuant to section 130 of the OCA;
- A provision respecting the distribution of the remaining property of a corporation that is not a public benefit corporation on winding up or dissolution.

Subsection 167(5.1) of the ONCA, as proposed in Bill 154, also prescribes a transition provision whereby, on the day the section comes into force, the articles of a charitable corporation are deemed to be amended in accordance with sub-subclause 167(1)(d)(i)(A) of the ONCA with regard to the distribution of property upon dissolution.

New proposed subsection 4(1.1) in Bill 154, provides that the ONCA does not apply to corporations sole, except as prescribed. As well, new proposed section 207.1 authorizes the Lieutenant Governor in Council to prescribe provisions of the ONCA and the regulations that are to apply to corporations sole and to prescribe modifications, if any.

5. Bill 154 - Amendments to the OCA[46]

Notwithstanding the introduction of Bill 154 proposing amendments to the ONCA, it will still be a number of years before proclamation of the ONCA. As such, of immediate interest to Ontario not-for-profit corporations is that Bill 154 also contains proposed amendments to the OCA to allow Part III OCA not-for-profit corporations to enjoy some of the modernized rules contained in the ONCA and other changes that would provide more flexibility to their operations. The following are the key changes in this regard.

- Special legislation and charity law will prevail over the OCA in the event of a conflict.[47] (The OCA is currently silent on this issue.)
- Corporations may hold members' meetings by telephonic or electronic means, unless the by-laws of a corporation provide otherwise.[48] (Currently, the OCA does not permit members' meetings to be held by telephonic or electronic means.)

[46] This section of the paper is excerpted from *Charity & NFP Law Bulletin* No. 406, "Bill 154 – Proposed Amendments to OCA", prepared by Theresa Man, online: http://www.carters.ca/pub/bulletin/charity/2017/chylb406.pdf.
[47] *Supra* note 3, new section 117.1 will be inserted.
[48] *Ibid*, new section 125.1 will be inserted.

- Corporations will have the full capacity, rights, powers and privileges of a natural person; it will not be necessary for a by-law to be passed in order to confer any particular power on a corporation or its directors; and a corporation's acts will be valid even if the corporation acted contrary to its instrument of incorporation, its by-laws or the OCA.[49] (The OCA currently provides that corporations have the capacity of a natural person (*i.e.* the corporation can engage in the same lawful activity as an individual person such as entering into contacts), and may exercise its powers outside of Ontario to the extent permitted by the jurisdiction in which it exercises those powers. The OCA also grants specific powers to not-for-profit corporations.[50])
- A corporation may sell, lease or exchange all or substantially all of its undertaking or all or substantially all of a part of its undertaking if authorized to do so by a special resolution.[51] (This provision provides better clarity on when a corporation may sell all or substantially all of its undertaking.[52])
- Corporations may adopt contracts entered into prior to incorporation and thereby be bound by such contracts and the person who purported to act on behalf of the corporation ceases to be bound by or entitled to the benefits under the contract.[53] (The OCA is currently silent on this issue.)
- Directors and officers will be subject to a statutory objective standard of care, *i.e.* by acting honestly and in good faith with a view to the best interests of the corporation and exercising the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.[54] (The OCA is currently silent on this issue and therefore directors and officers are subject to the subjective standard of care under common law.)

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[49] *Ibid*, new section 126.1 will be inserted, and the following provision will no longer apply: clauses 23(1)(a) to (p) and (s) to (v), subsection 23 (2), and sections 59, 274, and 275.
[50] *Ibid*, sections 274, 275, 23(1) and 133.
[51] *Ibid*, new section 126.2 will be inserted and clause 23(1)(m) will longer apply.
[52] *Ibid*, clause 23(1)(m).
[53] *Ibid*, new section 126.3 will be inserted.
[54] *Ibid*, new section 127.1 will be inserted.

- Directors may be removed by a simple majority vote. However *ex officio* directors may not be removed from office.[55] (The OCA currently requires two-thirds vote to remove a director.[56]) A director elected by a group of members that has an exclusive right to elect the director may be removed only by a resolution passed by a majority of the votes cast by the members of that group at a general meeting.[57] (The OCA is currently silent on this issue). However, the new rules would not affect the operation of any provision respecting the removal of directors contained in the letters patent, supplementary letters patent or by-laws in place prior to the proclamation of these amendments to the OCA.[58]
- Members may, by an extraordinary resolution (*i.e.* 80% of the votes cast at a members' meeting), decide not to appoint an auditor and not to have an audit in respect of a financial year if the corporation had annual revenue in that financial year not exceeding $100,000 or a different amount prescribed by the regulations.[59] (Currently, an audit exemption requires the consent in writing by all members.[60] Replacing the word "income" with "revenue" provides greater clarity on its meaning. Permitting the $100,000 threshold be changed by regulations provides more flexibility.)
- The by-laws of a corporation may permit non-members (with their consent in writing) to be elected to the board of directors.[61] (Currently, directors are required to be members of the corporation.[62] However, the following corporations currently may elect non-members to their board if so permitted by their by-laws: hospitals within the meaning of the *Public Hospitals Act*, corporations that operate recognized stock

[55] *Ibid*, new subsection 127.2(1) and (3) will be inserted, and s. 67 will no longer apply.
[56] *Ibid*, sections 133 and 67.
[57] *Ibid*, new subsection 127.2(2) will be inserted.
[58] *Ibid*, new subsection 127.2(4) will be inserted.
[59] *Ibid*, new section 130.1 will be inserted, and section 96.1 will no longer apply.
[60] *Ibid*, sections 133 and 96.1.
[61] *Ibid*, subsection 286(3) will be amended.
[62] *Ibid*, subsections 286(1) and (2).

exchanges, and corporations under Part V of the OCA (other than a pension fund or employees' mutual benefit society).[63]

- If a corporation has no directors or members, the court may make an order appointing the required number of directors.[64] (This is not currently permitted under the OCA.)
- Notice of members' meetings may be given by electronic means if conditions specified in the *Electronic Commerce Act, 2000* are met.[65] (The OCA currently does not permit notice of members' meeting be given electronically.)
- A corporation may not export out of the OCA (*i.e.* continue from the OCA to another jurisdiction) unless the laws of that other jurisdiction provide that the corporation continues to be liable for its obligations, that any existing cause of action, claim or liability to prosecution is unaffected, that actions and proceedings by or against the corporation may continue to be prosecuted, and that rulings, orders or judgments in favour of or against the corporation may be enforced.[66] (The OCA is currently silent on these requirements.)

Bill 154 also amends various sections of the OCA in order to accommodate the filing, keeping and searching of documents in electronic format. As well, Bill 154 expands the Minister's regulation-making powers in respect of the content, form, format and filing of various documents. The Minister, or a person designated by the Minister, will have the power to enter into agreements authorizing a person or entity to provide business filing services.

Companies that have objects in whole or in part of a social nature that are incorporated under the OCA will have five years after the proclamation of subsection 4(1) of Schedule 7 of Bill 154 to continue by special resolution under the ONCA, the OBCA or the *Co-operative Corporations Act*,[67] otherwise they will be dissolved. If a social company has more than one class of shareholders, the continuance must be approved by each class of shareholders by a separate

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[63] *Ibid*, subsection 286(3).
[64] *Ibid*, new subsection 288(4) will be inserted.
[65] *Ibid*, sections 93, 161 and 296 will be amended such that notice must be given "in writing". Section 6 of the *Electronic Commerce Act, 2000* (SO 2000, c 17) provides, with limited exceptions in section 31, that documents in writing can be in electronic form where they are (a) accessible by the other person so as to be usable for subsequent reference; and (b) capable of being retained by the other person."
[66] *Ibid,* new subsection 313(1.0.1) will be inserted.
[67] RSO 1990, c C.35.

vote. Twenty-five years after this new provision comes into force, the OCA will no longer apply to social companies that are incorporated by or under a general statue but will continue to apply to social companies incorporated by or under a special statute.[68]

There are also other proposed amendments to the ONCA that are complementary to or consistent with the ONCA. These include: only insurance companies under Part V of the OCA may be incorporated under Part II or III of the OCA,[69] companies will no longer be permitted to apply for supplementary letters patent to convert into corporations with or without share capital;[70] only insurers may apply for supplementary letters patent to convert a company into a public company, a private company or a corporation without share capital;[71] and the Minister may cancel under subsection 317(1) of the OCA for sufficient cause certain orders and other documents.[72]

Lastly, a word of caution to those who are interested in reading the proposed OCA amendments contained in Schedule 7 of Bill 154 in relation to when which provision would take effect. Schedule 7 contains 85 sections. Different sections come into force on different dates, with section 85 listing which sections would come into force on the 25th anniversary of the said proclamation, on the day when Bill 154 receives Royal Assent, on the 60th day after Bill 154 receives Royal Assent, on the day when the ONCA comes into force, or on the 3rd anniversary after Bill 154 receives Royal Assent; with the balance of sections coming into force on a day named by proclamation of the Lieutenant Governor.[73]

F. FEDERAL LEGISLATION UPDATE

1. Budget Implementation Act, 2016, No. 2 Passes

On December 15, 2016, Bill C-29, A second Act to implement certain provisions of the budget tabled in Parliament on March 22, 2016 and other measures (the "Budget

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[68] *Supra* note 3, section 2 will be amended and new section 2.1 will be inserted and re-enacted
[69] *Ibid*, sections 17 and 118.
[70] *Ibid*, clause 34(1)(q).
[71] *Ibid*, subsection 34(10).
[72] *Ibid*, subsection 317(1).
[73] *Supra* note 44, section 85 of Schedule 7.

Implementation Act, 2016, No. 2"),[74] which was released October 19, 2016 and implements portions of the 2016 Federal Budget, received Royal Assent. Of primary interest to charities is clause 42 of the Budget Implementation Act, 2016, No. 2, which implements amendments to the definition of total charitable gifts, total cultural gifts, and total ecological gifts in subparagraph 118.1(1) of the ITA, specifically with regard to gifts made by an individual's graduated rate estate. Clause 42 of the Budget Implementation Act, 2016, No. 2 also implements the changes to ITA subparagraphs 118.1(5.1) and 118.1(19)(c), which deal with gifts by an individual's graduated rate estate and excepted gifts in respect of the gift of non-qualifying securities. These changes apply to the 2016 and subsequent taxation years.

Also potentially of interest to charities and NFPs is clause 71 of the *Budget Implementation Act*, *2016, No. 2*, which adds Part XIX Common Reporting Standards to the ITA, and came into force on July 1, 2017. Part XIX "implements the reporting and due diligence standards of the Common Reporting Standard … developed by the Organisation for Economic Co-operation and Development that underpins the automatic exchange of financial account information." It will require financial institutions to report certain information to the CRA on reportable accounts.

2. CASL Private Right of Action Implementation Suspended

On June 2, 2017, the Governor General in Council issued an Order in Council (the "new Order in Council")[75] amending Order in Council P.C. 2013-1323,[76] the Order fixing the coming into force dates for sections of CASL. The new Order in Council repealed a paragraph in Order in Council P.C. 2013-1323 that set the date for the coming into force of a private right of action under CASL.

[74] Bill C-29, A second Act to implement certain provisions of the budget tabled in Parliament on March 22, 2016 and other measures, 1st Sess, 42nd Parl, 2015-16-17 (assented to 15 December 2016).

[75]*Order in Council Repealing the Coming into Force of the Private Right of Action dispositions of Canada's Anti-Spam Law*, SI/2017-31, (2017) C Gaz II 1506 (PC 2017-0580), online: <http://www.gazette.gc.ca/rp-pr/p2/2017/2017-06-14/html/si-tr31-eng.php?pedisable=true>.

[76] *Order Fixing Certain Dates as the Days on which Certain Provisions of the Act Come into Force*, P.C. 2013-1323, 2013 C Gaz II 3087 (made under: Canada's Anti-Spam Law), online: <http://fightspam.gc.ca/eic/site/030.nsf/eng/00272.html>.

Innovation, Science and Economic Development Canada issued a press release to accompany the repeal, explaining that the government is suspending the implementation of the private right of action "in response to broad-based concerns raised by businesses, charities and the not-for-profit sector."[77] The press release notes that what is needed is "a balanced approach that protects the interests of consumers while eliminating any unintended consequences for organizations that have legitimate reasons for communicating electronically with Canadians." As such, a parliamentary committee will be asked to review the legislation. The *Canada Gazette* further noted that the delay was for the purpose of promoting "legal certainty for numerous stakeholders claiming to experience difficulties in interpreting several provisions of the Act while being exposed to litigation risk."[78]

3. End of CASL Transition Period

On July 1, 2017, an important provision of Canada's anti-spam legislation ("CASL"),[79] the transition period in section 66 of CASL, ended. When CASL came into force on July 1, 2014, section 66 of CASL provided a three-year transition period for implied consent for organizations to have been able to send commercial electronic messages arising out of existing business or non-business relationships. Implied consent under CASL, *e.g*. donations to registered charities or membership in non-profit organizations, is generally tied to a statutory time limit of two years or less. However, during the transition period, implied consent arising from existing business or non-business relationships created prior to July 1, 2014 was effective until the end of the three-year period. The intention of the transition period was to permit organizations to which CASL applies to obtain express consent from these individuals. As of July 1, 2017, this transition period ended.

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[77] Innovation, Science and Economic Development Canada, "Government of Canada suspends lawsuit provision in anti-spam legislation", (Ottawa: ISEDC, 7 June 2017), online: <https://www.canada.ca/en/innovation-science-economic-development/news/2017/06/government_of_canadasuspendslawsuitprovisioninanti-spamlegislati.html>.

[78] *Supra* note 75.

[79] An Act to promote the efficiency and adaptability of the Canadian economy by regulating certain activities that discourage reliance on electronic means of carrying out commercial activities, and to amend the Canadian Radio-television and Telecommunications Commission Act, the Competition Act, the Personal Information Protection and Electronic Documents Act and the Telecommunications Act, SC 2010, c 23.

Implied consent obtained after July 1, 2014 is still valid, though such implied consent is subject to the normal time limitations under CASL and was not impacted by the transition period.

G. PROVINCIAL LEGISLATION UPDATE

1. Amendment to the Ontario Employer Health Tax will Impact Registered Charities

As a matter of background concerning amendments that recently came into force, as of January 1, 2014, the amount of annual remuneration that may be exempt from Ontario's Employer Health Tax ("EHT") is $450,000, up from the previous $400,000. EHT is a payroll tax that all employers in Ontario are required to pay on the total remuneration paid to employees in a given year. The basic rule is that eligible employers are exempt from EHT on the first $450,000 of their total annual remuneration paid out. The amount of tax that employers are required to pay varies depending on the amount of remuneration paid. Currently the tax rates vary between 0.98% - 1.95%. Employers cannot claim the EHT exemption, though, if their annual payroll (including payroll of associated employers) is above $5 million. Eligible employers who are registered charities, however, can claim the EHT exemption even if their annual payroll is above $5 million.

As of January 1, 2017, amendments to the *Employer Health Tax Act Regulations* came into force whereby registered charities with two or more qualifying "charity campuses" are now permitted to claim an EHT exemption for each qualifying "charity campus".[80] What qualifies as a "charity campus" is summarized on the Ministry of Finance's website and is stated as including, "all of a registered charity's locations that are in one building, or on one parcel of land (property), or on contiguous properties (properties that touch along a boundary or at a point). If a registered charity has branches, sections, parishes, congregations or other divisions (internal divisions), a "charity campus includes all of the locations of the registered charity and all of the locations of any of its internal divisions that are in one building, or on one property or on contiguous properties."

[80] Ontario Ministry of Finance, online: http://www.fin.gov.on.ca/en/tax/eht/registeredcharities.html

An “associated employer” is any employer “who is connected by ownership by a combination of ownership and relationships between individuals” (*e.g.* relatives, blood, marriage, adoption). Because there is only one available EHT exemption for an employer in any given year, associated employers, whether they are associated for the entire year, or only for a specific period of time throughout the year, must consider their combined total remuneration paid to determine whether they qualify for the EHT exemption. Employers that are associated with a registered charity, however, are not required to include the registered charity’s total annual remuneration to determine whether they qualify for the EHT exemption, and are not required to share its EHT exemption with the registered charity.

2. Proposed Ontario Regulations Authorizing Charitable Corporations to Pay Directors in Limited Situations

On July 10, 2017, the Office of the Public Guardian and Trustee of Ontario (“PGT”) posted Proposal Number 17-MAG008 (the “Draft Amendments”),[81] which contained draft amendments to Ontario Regulation 4/01[82] under the CAA. The Draft Amendments were open to public comment until August 29, 2017. The Draft Amendments proposed to amend Ontario Regulation 4/01 to provide relief from the common law rule prohibiting the remuneration of directors of charitable corporations and persons related to them by outlining certain circumstances where charitable corporations would be authorized to pay directors and related persons for goods, services, or facilities. The current Ontario Regulation 4/01 does not address director remuneration. The Draft Amendments would not apply to directors of unincorporated associations or trustees of charitable trusts.

Currently, in order for directors of charitable corporations to receive remuneration in a capacity other than as a director, charitable corporations and their directors must obtain a consent order from the PGT under section 13 of the CAA. This process can be time intensive and generally requires the assistance of legal counsel. The Draft Amendments would simplify this process by dispensing with the need for a consent order in prescribed circumstances for

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[81] Office of the Public Guardian and Trustee of Ontario, *Proposal Number 17-MAG008* (Toronto: Regulatory Registry, 10 July 2017), online: http://www.ontariocanada.com/registry/view.do?postingId=24430&language=en.
[82] Approved Acts of Executors and Trustees, O Reg 4/01.

charitable corporations. Under the Draft Amendments, directors would continue to be prohibited from receiving direct or indirect payment for services they provided in their capacity as directors or employees of the charitable corporation, for fundraising services, for selling goods or services for fundraising, or in connection to the purchase or sale of real property.

Before payments could be made to a corporate director or a related person, the charitable corporation would first need to meet a number of conditions set out in the Draft Amendments. For example, the amount paid must be reasonable considering the goods or services received; the amount must be paid with a view to the best interests of the charity; and the amount paid must not cause the charity to become insolvent. Before the payments may be authorized, all of the charity's directors, as well as any persons connected to the directors that provide goods, services, or facilities, must agree in writing to a maximum amount that can be paid and directors, other than the one to be paid or connected to the person to be paid, must agree in writing that the payment meets the requirements laid out in the Draft Amendments. Further, the board must have (a) at least five voting directors for every director who is either receiving payment or connected to a person receiving payment, and (b) a minimum of four voting directors excluding such director. The director that is to be paid, and any related person, cannot attend the meeting during which the decision about payment is made.

The Draft Amendments, if enacted into law will ease the process for incorporated charities that want to rely upon their board members who can provide services in another capacity without the need for a consent order. As such, incorporated charities should continue to follow developments with respect to the Draft Amendments should they wish to be able to remunerate their directors in another capacity.

3. Bill 154 - Amendments to the CAA

In addition to the proposed amendments to the ONCA and to the OCA mentioned above under Corporate Law Update, Bill 154 also proposes changes to CAA permitting "social investments". The CAA applies to all charities in Ontario and provides in section 10.1 that sections 27 to 31 of the *Trustee Act,*[83] dealing with investment powers by trustees, apply to trustees and

[83] RSO 1990, c T.23.

charitable corporations holding property for charitable purposes.[84] Schedule 2 of Bill 154 proposes to amend the CAA by adding sections 10.2 to 10.4 to permit "social investments" by trustees and charitable corporations holding property for charitable purposes and to exclude the application of the *Trustee Act* (with minor exceptions) with regard to "social investments."

The Ministry of Economic Development and Growth, in conjunction with the Ministry of the Attorney General, has been working over the last few years to explore possible legislative changes to facilitate increased social investing by charities in Ontario. The end result of these efforts is the proposed amendments to the CAA in Schedule 2 of Bill 154, which appear to have been based to a great extent on the legislative wording contained in Part 14A of the *Charities (Protection and Social Investment) Act 2016* of England and Wales.[85]

a) Provision of social investments under Bill 154

Subsection 10.2(1) of the CAA, as proposed by Bill 154, provides that a "social investment" is made when a trustee applies or uses trust property in order to: a) "directly further the purposes of the trust," *and* b) achieve a "financial return" for the trust. Subsection 10.2(3) defines "financial return" as an "outcome in respect of the trust property [that] is better for the trust in financial terms than expending all the property." Subsection 10.2(4) states that the fact that a social investment may have other results, in addition to furthering of the purposes of the trust and the achievement of a financial return, does not "prevent it from being regarded as the making of a social investment." In addition, subsection 10.2(5) states that a social investment, for the purposes of sections 10.3 and 10.4 (dealing with the power, limitation and duties involved with a social investment), "is not, for that reason alone, an investment for any other purpose."

Proposed subsection 10.3(1) establishes the specific power of trustees to use or apply trust property to make a social investment. However, in accordance with subsection 10.3(2), a social investment may not be made "in relation to trust property that is subject to a limitation on capital being expended for the purposes of the trust, unless the trustee expects that making the social investment will not contravene the limitation or the terms of the trust allow for such an

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[84] *Supra* note 5*,* s. 10.1.
[85] Charities (Protection and Social Investment) Act 2016 (UK), c 4.

investment." In addition, subsection 10.3(4) provides that the power to make a social investment may be restricted or excluded by the terms of the trust.

Section 10.3 also limits the application of the *Trustee Act* for charities making social investments. Specifically, subsection 10.3(3), provides that sections 27 to 29 of the *Trustee Act* do not apply to the making of social investments, with the exception of subsections 27(3) and (4) dealing with mutual funds and common trust funds, subject to "necessary modifications."

Proposed section 10.4 prescribes the duties of trustees with regard to making social investments. These duties are (i) the trustee has to "satisfy him, her or itself that it is in the interests of the trust to make the social investment, having regard to the benefit expected to be achieved for the trust" before making a social investment (paragraph 10.4(1)(b)); (ii) the trustee has to periodically "review the social investment of the trust property" (subsection 10.4(2)); and (iii) in both cases, before making a social investment and as part of their on-going review, a trustee "shall" determine whether, in the circumstances, advice should be obtained respecting the proposed social investment, and if so, obtain and consider the advice (paragraph 10.4(1)(a) and subsection 10.4(3)). According to subsection 10.4(4), reliance on advice obtained in accordance with this proposed section is not a breach of trust, something which will no doubt encourage trustees and directors of charities to seek out advice. However, there is nothing in Bill 154 which defines what type of "advice" should be obtained. Finally, subsection 10.4(5) states that the above duties of trustees cannot be restricted or excluded by the terms of the trust, which in accordance with subsection 10.2 (6) would include the constating documents of a charitable corporation.

b) Commentary

While the proposed amendments to the CAA authorising charities to make social investments is a positive development by the provincial government in support of the charitable sector in Ontario, and in particular foundations, the wording of the proposed amendments raises a number of questions and issues that will need to be addressed if Bill 154 is enacted as currently drafted. Some of those issues are highlighted below.

1) As a result of Bill 154, charities will generally need to categorize investment decision making into one of three categories:

   i) An investment as a prudent investor under the *Trustee Act* that is focused on a financial return;

   ii) A social investment under the proposed amendments to the CAA in Bill 154 that is focused on a hybrid approach of directly furthering the purposes of the charity *and* achieving a financial return; or

   iii) A program related investment ("PRI") under the Canada Revenue Agency ("CRA") *Guidance on Community Economic Development Programs* (CED Guidance),[86] that permits the use of an investment vehicle to "directly further one or more of a charity's charitable purposes,"[87] and in doing so "*may* generate a financial return, [although] they are not made for that reason."[88] If an investment meets the CRA definition of a PRI, the value of the PRI would not be included in the asset base for the calculation of the 3.5% disbursement quota, i.e., "property not used directly in charitable programs or administration" under the ITA.[89] However, the disbursement would not be considered to be a charitable expenditure for purposes of meeting the 3.5% disbursement quota obligation of the charity, other than with regard to possibly including lost opportunity costs of the PRI.[90] Most importantly, if an investment by a charity constituted a PRI in the opinion of the CRA, then the charity would be required to evidence a significant degree of "direction and control,"[91] as described in the CED Guidance in order to avoid jeopardizing its charitable status.

   It remains a question of fact to be determined in the circumstances of each case whether a trustee would have made an investment under one of the above categories, or possibly

[86] Canada Revenue Agency, "CG-014, Community Economic Development Activities and Charitable Registration", online: https://www.canada.ca/en/revenue-agency/services/charities-giving/charities/policies-guidance/community-economic-development-activities-charitable-registration-014.html.
[87] *Ibid* at para 69.
[88] *Ibid* at para 40.
[89] *Supra* note 9, subsection 149.1(1).
[90] *Supra* note 86 at para 68.
[91] *Ibid* at para 47.

two categories, *e.g.* as a social investment *and* a PRI. However, the absence of a clear definition in the proposed amendments in Bill 154 concerning what a social investment is and what it is not could result in confusion for charities in deciding on what type of investment to embark. For example, the determination of when a social investment might cross the line and become a PRI under the CRA CED Guidance and become subject to audit by the CRA should be the subject matter of discussion and co-ordination between the Province of Ontario and the CRA with the issuance of some type of complementary guidance to assist charities. Otherwise, it is possible that the CRA could conclude that what a charity intended to be a social investment was in fact a PRI subject to the CED Guidance, but without there being adequate direction and control or an exit plan from such investment[92] as required by the CED Guidance.

2) Charities that hold "endowments" where there is a limitation on the expenditure of capital will need to determine whether making a social investment will contravene "the limitation or [whether] the terms of trust allow for such an investment" as required by proposed subsection 10.3(2) of the CAA. This will mean that the charity will need to undertake a careful inventory of their investments to determine if there is any documentation for *inter vivos* or testamentary gifts that may contain any limitation on the expenditure of capital (including a determination of whether the definition of capital includes realised capital gains or not) and, if there was a limitation, then either avoiding using such funds in making a social investment or, if they are going to make a social investment, then documenting why the trustees have concluded that they "expect" that the contemplated social investment will not contravene the limitation on expenditure of capital as a permitted exception under proposed subsection 10.3(2) of the CAA.

3) As explained above, proposed subsection 10.2(6) of the CAA states that the constating documents of a charitable corporation form part of the trust for purposes of a social investment, and proposed subsection 10.3(4) states that the terms of a trust may restrict or exclude the power to invest in social investments. Therefore, where a power clause in the constating documents (such as letters patent, articles of incorporation or articles of

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[92] *Ibid* at para 51.

continuance) expressly states that the property of the charity is to be invested in accordance with a specific investment power (such as a prudent investment power), the question arises whether such express investment power precludes the ability of the charity to invest in a social investment. Similarly, if a charitable corporation is incorporated in a province outside Ontario and the charity carries on operations in another province as well as in Ontario, then the question is whether the charity is permitted to make social investments in Ontario where the constating documents of the charitable corporation call for charitable funds to be invested in accordance with the trustee act of the province in which the charity was incorporated.

4) Since Bill 154 proposes that sections 27 to 29 of the *Trustee Act* will not apply to social investments (except for subsections 27(3) and (4), dealing with mutual funds and common trust funds "with necessary modifications"), then the statutory protection from liability available to trustees with regard to prudent standard investments under subsection 27(8) of the *Trustee Act* will not be available when making social investments. Although proposed subsection 10.4(4) of the CAA states that reliance upon "advice" does not constitute breach of trust, the language in the proposed subsection does not provide the same extent of protection as clearly stating that a trustee is "not liable for loss" as currently provided for in section 28 of the *Trustee Act*. This loss of statutory protection should be a matter of some concern for trustees and directors of charities contemplating making social investments.

5) As indicated above, the proposed subsection 10.4(1) will impose a new mandatory obligation on trustees and directors of charitable corporations that they "*shall* determine whether, in the circumstances, advice should be obtained […] and if so, obtain and consider the advice" *before* making a social investment. However, if the process to make a social investment is so nuanced that the board of a charity must consider whether they need to obtain advice (which will likely involve seeking legal advice), it raises the question about whether the proposals are in fact as practical as they should be, particularly since there is no guidance in Bill 154 concerning from whom a charity should seek advice. Remedial legislation to assist charities should be sufficiently clear on its face that lay

people on the board of trustees or directors of a charity should be able to decide if they wish to pursue a particular course of action without being required to consider retaining individuals to advise them.

While it is commendable that the Province of Ontario is undertaking a statutory initiative to assist charities in Ontario to access charitable capital for social investments, there are numerous questions and issues associated with the proposed legislation that will need to be thought through and addressed in order to avoid uncertainty and possible confusion for charities. As a result, charities, and particularly foundations, will want to closely monitor the progress of Bill 154 to see if there is clarification provided in the form of guidance, regulations, or possibly even amendments if determined to be necessary.

4. Charities Operating in Quebec are Still Required to Submit an Annual Information Return in Quebec

Although charities registered with the CRA that collect donations from Quebec residents are no longer required to register separately in Quebec, charities that operate in Quebec are still required to file the annual information return TP-985.22-V. The information return TP-985.22-V is mandatory for any charity that is "carrying on activities in Quebec" and it must be filed within 6 months after the charity's year-end.

H. OTHER CASE LAW OF INTEREST

1. Unfunded Cheque Results in Unenforceable Gift

In the decision of *Teixeira v Estate of Maria Markgraf*, released January 20, 2017, the Ontario Superior Court of Justice ("Court") considered the validity of a gift of money that the donor did not actually have. The issue of the validity of a gift was raised when the payor, Maria Markgraf ("Markgraf"), made an *inter vivos* gift to the payee, Arlindo Teixeira, her long-time neighbour ("Teixeira"), in the form of a $100,000 cheque, despite having only $81,732 in her account.

The facts of the case were not in dispute: in appreciation for the kindness shown to her by Teixeira, Markgraf wrote a cheque for $100,000 payable to Teixeira and instructed a family

member to deliver it. Even though Markgraf had other investments with her bank amounting to a total of greater than $100,000, the account on which the cheque was drawn had only $81,732, which caused the cheque to be returned to Teixeira. By then, Markgraf had passed away, so Teixeira brought an application against the estate to enforce the gift.

In considering the issue at hand, the Court looked at the necessary elements for a valid gift: i) donative intent; ii) acceptance; and iii) sufficient delivery. It found that Markgraf had “voluntarily intended” to make the $100,000 gift and, even though she may have been mistaken as to the funds available in her account, this was sufficient to meet the donative intent element of a valid gift. The second element of acceptance was also satisfied, as Teixeira had accepted the cheque and attempted to deposit it at his bank. With regard to the third element for a valid gift, the Court acknowledges that, while not a necessary part of a contract, delivery is a basic requisite of gifts. Moreover, the Court states that “there must be an efficient delivery of the gifted property or some accepted substitute. As a rule the gift must be literally given away.” As the Court found that this third element had not been satisfied in this case, it thereby rendered the gift invalid.

The Court stated that the delivery by cheque “is neither money nor representation of money, it is only a direction to the drawer’s bank” and, thus, the gift is not complete until the cheque has cleared. In this case, because Markgraf’s account did not have sufficient funds, the Court found that the delivery of the cheque was not complete. As a result, the gift was consequently not perfected and was unenforceable. Furthermore, the decision confirmed the equitable principle of estoppel was not applicable to the facts of this case.

While this case did not involve a charity, it does serve as a reminder to charities, as well as donors, that all three elements of a gift must be present in order for the gift to be valid. Even where clear donative intent and acceptance of the gift are present, a gift may fail where it cannot be properly delivered to the intended recipient.

2. “Armchair Rule” Used by Court to Determine if Gift was an Endowment or Expendable

In *The Paul Sugar Palliative Support Foundation v. Creighton Estate*, released February 27, 2017, the Supreme Court of BC was called on to interpret an unclear testamentary gift to determine whether the gift was intended to be a capital endowment to be held and invested

with only the income to be expendable, or whether the full amount of the capital of the gift was intended to be expendable. While this case was only an oral decision with limited precedential value because of a lack of facts and no reference to case law, it will be of interest to legal counsel who may be called upon to determine whether a testamentary gift constitutes an endowment or is expendable.

The last will of the testator provided for a gift to the Vancouver Foundation ("VF") "to be added to the capital of the Paul Sugar Palliative Support Foundation" (the "PSPSF"). The PSPSF is currently a registered charity and, according to the PSPSF website, the Vancouver Foundation manages PSPSF's funds. Complicating matters was the fact that the testator, while he was alive, had established the PSPSF as a "permanent fund" through an *inter vivos* deed of gift to the VF (the "Deed of Gift"), but which fund had not been actualised before the testator died because the minimum monetary threshold had not been reached. The terms of the PSPSF stated that the VF was to "hold the capital of the fund permanently, and…invest and administer it in accordance with the provisions of the *Vancouver Foundation Act*".

To aid in its interpretation of the will, the court relied upon the "armchair rule", which it explained was the rule where "the court has to endeavour to place itself in the position of the testator at the time when the last will was made, and give due weight to the circumstances" when called upon to interpret an unclear provision in the will in question. While the court gave no reference to case law as authority for this rule, the "armchair rule" was originally set out in *Boyes v Cook*, where the High Court of Justice of England and Wales originally stated that "[the court] may place [itself], so to speak, in the testator's arm-chair, and consider the circumstances by which he was surrounded when he made his will to assist [it] in arriving at his intention", and was more clearly articulated in *Re Burke*, a 1959 Ontario Court of Appeal decision. Utilizing this rule and based on the testator's previous gifts to the V, as well as the understanding of the lawyer who drafted the will (who was also the executor of the will), the court found that the testator had apparently intended that the gift be given to the PSPSF without limitations, and that the term "capital" was not intended to limit how the gift was to be used. The court held that, despite the gift's initial appearance to be an endowment based upon the wording of the last will of the testator as well as the wording of the Deed of Gift that had been referenced in the will, the

testator had not intended that the capital of the testamentary gift be held and invested as an endowment. The balance of the decision dealt with the question of costs of the court application.

This decision underscores the importance of ensuring that testamentary charitable gifts are carefully drafted to ensure that they accurately reflect what the testator actually intends. Otherwise, the estate or the charity may be forced to make an expensive and potentially contentious court application for a judicial interpretation, which might include applying the "armchair rule" in order to determine what the testator had really intended, sometimes with surprising results, as with this decision.

3. SCC Grants Leave to Appeal from Case Involving Unfair Church Discipline

On April 13, 2017, the SCC granted leave to appeal in the decision of *Wall v Judicial Committee for the Highwood Congregation of Jehovah's Witnesses* ("*Wall*"). Leave to appeal was sought by the Judicial Committee of the Highwood Congregation of Jehovah's Witnesses and the Highwood Congregation of Jehovah's Witnesses (the "Congregation"). The SCC has assigned the hearing date of November 2, 2017. In the *Wall* case (which was released on September 8, 2016), a majority on the Alberta Court of Appeal affirmed that courts have the legal jurisdiction to review decisions made by a religious organization where discipline or expulsion of a member was carried out in a manner that does not reflect principles of natural justice.

In finding that Mr. Wall's expulsion from the membership in the Congregation was done using procedures that did not reflect principles of natural justice, the Alberta Court of Appeal noted that Mr. Wall was not provided with the details of the allegations made against him or an explanation of the discipline process that he would face prior to expulsion; he was not advised whether there would be a record of the proceedings, nor did he receive a written reasons of either the Judicial Committee or the Appeal Committee.

The SCC's ruling on this case will have a significant impact on how charities and not-for-profits are able to discipline their members *vis-à-vis* principles of natural justice.

4. Orders Amending By-laws Outside the Jurisdiction of Arbitrators

On May 30, 2017, the Ontario Superior Court of Justice delivered its decision in *Cricket Canada v Bilal Syed*, whereby it partially allowed an application by Cricket Canada, a national sports organization incorporated under the CNCA, to set aside in part an arbitral award (the "Award") that had ordered Cricket Canada to include specific provisions in its by-laws in order to implement the arbitrator's decision.

The Award concerned a claim by a candidate for Cricket Canada's board of directors who, after an unsuccessful bid for directorship, challenged the organization in arbitration before the Sport Dispute Resolution Centre of Canada (the "SDRCC"). Among other things, the claimant argued the election had not been carried out in accordance with Cricket Canada's by-laws, and that the process had been compromised by discrimination and a lack of neutrality.

At the end of the proceeding, the arbitrator found no discrimination. However, he did find some "improprieties" in the election process. Specifically, the Award ordered Cricket Canada to amend its by-laws to include the following: i) that any person involved in selecting the members of the Nomination Committee be prohibited from running in the election; ii) that candidates who, as members of the board of a provincial sports organization, had voting rights to elect the board of Cricket Canada, must resign their position before the election; and iii) to prohibit the exchange of benefits for votes.

Cricket Canada brought an application before the Ontario Superior Court of Justice ("Court") to challenge the portion of the Award instructing it to amend its by-laws. It alleged that, even though there was no formal arbitration agreement as required by Cricket Canada's dispute resolution policy, the extent of the jurisdiction granted to the arbitrator was reflected in the provisions of the SDRCC Code, as well as in the party submissions in the arbitration. The Court agreed these documents did not grant the arbitrator the jurisdiction to order a change in the by-laws and policies of Cricket Canada because these were not part of the dispute. In the words of the Court: "[w]hile the Arbitrator could consider the by-laws as they affected [the claimant's] candidacy, he had no jurisdiction to tell Cricket Canada that they should be changed."

In the view of the Court, the aspects of the Award challenged by Cricket Canada were each a "core issue of internal governance" and outside the scope of authority of the arbitrator,

who had been called to determine the procedural fairness of the election process and not the rules that governed that process, provided such rules were in compliance with the CNCA. Following previous decisions suggesting that, absent gross irregularities in the electoral process, a decision maker should not readily interfere with the internal governance of a corporation, the Court asserted that "[n]on-profit organizations […] should not be required to adhere rigorously to all of the technical requirements of corporate procedure for their meetings as long as the basic process is fair." Finally, the Court concluded that introducing changes to Cricket Canada's by-laws, policies and procedures was a matter for the members to decide after their own negotiations and consultations, and could not be imposed unilaterally by the arbitrator.

5. Tribunal Upholds Religious School Right to Reject Applicants Based on Creed

On July 5, 2017, in *HS v The Private Academy*, the Human Rights Tribunal of Ontario (the "HRTO") dismissed three applications by a same-sex married couple (the "Parents") alleging discrimination by an Evangelical Christian school (the "School") that refused to admit their child into its preschool program. The Parents argued the School discriminated with respect to services against their child because of sex, creed, family status and marital status. However, the School responded that it was entitled to rely on the exemption in section 18 of the Ontario *Human Rights Code* (the "Code")[93] because it, as a "special interest organization", is primarily engaged in serving the interest of persons identified by a particular creed and it is entitled to restrict participation to parents who subscribe to its creed. This decision provides an important precedent concerning the application of the protection contained in section 18 of the Code for organizations primarily dedicated to providing services, goods and facilities to individuals identified by any of the prohibited grounds of discrimination, such as creed, sex, age, marital status, family status or disability, in their specific communities without the obligation to extend equal treatment to the broader public.

[93] *Human Rights Code*, RSO 1990, c H.19.

a) Background

The School was established as an alternative to the public school system for parents who shared the same Evangelical Christian values and traditions. It provided a "biblically-based curriculum in a Christ-centred learning environment", where "the school functions as an extension of the home, to support parents in their 'responsibility before God' to raise and teach children." Specifically, the School provided parents with a handbook (the "Handbook") containing its Mission Statement, Statement of Faith, Core Family Values, and Lifestyle Policy, which include the beliefs that a human being exists from the time of conception and that marriage is between one man and one woman.

b) Special Interest Organization Exemption

Section 1 of the Code prohibits discrimination when providing "services, goods and facilities" based on a person's "creed" or "race, ancestry, place of origin, colour, ethnic origin, citizenship, creed, sex, sexual orientation, age, marital status, same-sex partnership status, family status or disability." However, section 18 of the Code provides special interest organizations with an exception to the section 1 prohibition when the organization is "primarily engaged in serving the interests of persons identified by a prohibited ground of discrimination."[94]

In applying the requirements in section 18, the HRTO applied the following three-part test adopted in two cases of the tribunal: *Kostiuk v. Toronto Community Housing Corporation* and *Martinie v. Italian Society of Port Arthur*:

1. Is the entity a religious, philanthropic, educational, fraternal or social institution or organization?
2. Is the institution or organization "primarily engaged in serving the interests of persons identified by a prohibited ground"?
3. Is the membership or participation in the institution or organization restricted to those identified by that prohibited ground?

[94] *Ibid,* section 18.

While recognizing the harm caused by discrimination and the disadvantages that members of different groups face, the HRTO found the School had met all three elements and that it may rely on section 18 of the Code as a full defence to what would otherwise be discrimination. The School was allowed to restrict admission only to those who shared its professed creed.

The adjudicator further clarified that section 18 did not preclude special interest organizations from providing services to the broader community as long as they are "primarily engaged" in servicing members of a group identified by a prohibited ground, as it was in this case.

The HRTO held that the prohibited ground was the School's creed, and that the Handbook had a clearly stated mission to support parents who shared the faith-based beliefs supported by the School. It further held that, even though the Parents did not object to their child learning different views, "[t]o obligate the school to admit a child whose parents do not share those beliefs is to encroach on the rights of the parents served by the school to practice the creed and religion they sincerely believe in."

c) Commentary

This tribunal decision serves as a useful reminder that charities and not-for-profits, and particularly religious organizations, may be exempt from the requirement to provide equal treatment with respect to services, goods and facilities, without discrimination, under section 1 of the Code if they meet the requirements for the exemption under section 18 of the Code. However, the record of the HRTO on this point consists of very few decisions and the courts have yet to directly address what constitutes the requirements for the exemption under section 18 of the Code, although some principles can be drawn from the *Christian Horizons* case. Therefore, religious organizations that wish to rely on the section 18 exemption should remember that the protection provided under section 18 will largely depend upon the circumstances of each case and whether it meets the three elements referred to above.

I. CONCLUSION

The breadth and number of developments that have occurred in the area of charity law during the last 12 months underscore how complicated the law involving charities has become in Canada. As such, it is increasingly important for practitioners who are interested in working with the charitable sector to keep abreast of developments in the law with regard to charities as they occur. Hopefully this paper will have been of some help in this regard.

UPDATE ON CHARITY LAW

Current as of October 4, 2017

Terrance S. Carter

Carters Professional Corporation

J. CASE LAW APPENDIX

Boyes v Cook, (1880) 14 Ch D 53

Cricket Canada v Bilal Syed, 2017 ONSC 3301

Guindon v Canada, [2015] 3 SCR 3, 2015 SCC 41

HS v The Private Academy, 2017 HRTO 791

Kostiuk v. Toronto Community Housing Corporation, 2012 HRTO 388

Martinie v. Italian Society of Port Arthur (1995), 24 C.H.R.R. D/169 (Ont. Bd. Of Inquiry)

Ontario Human Rights Commission v Christian Horizons, 2010 ONSC 2105

Ploughman v The Queen, 2017 TCC 64

Re Burke, [1960] OR 26; 20 DLR (2d) 396

Teixeira v Estate of Maria Markgraf, 2017 ONSC 427

The Paul Sugar Palliative Support Foundation v Creighton Estate, 2017 BCSC 502

Wall v Judicial Committee for the Highwood Congregation of Jehovah’s Witnesses, 2016 ABCA 255

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TAB 5

Mind if I Cut In? When a Beneficiary's Creditor Joins the Trustee-Beneficiary Dance

Benjamin Arkin
Arkin Estate Law Professional Corporation

DAY TWO
October 17, 2017

cpd Continuing Professional Development

Mind if I Cut In?

When a Beneficiary's Creditor Joins the Trustee-Beneficiary Dance

Benjamin D. Arkin

Arkin Estate Law

Presented at

Law Society of Upper Canada

Estates and Trust Summit: Day 2

October 17, 2017

Mind if I Cut In?

When a Beneficiary's Creditor Joins the Trustee-Beneficiary Dance

Law Society of Upper Canada

Estates and Trust Summit: Day 2 – October 17, 2017

Benjamin Arkin, Arkin Estate Law[1]

Table of Contents

I. Introduction **3**

II. Enforcement by third parties: Notices of Garnishment and Writs of Execution **3**

A. Garnishment generally **4**

B. Writs of Execution generally **7**

III. Can a beneficiary's interest in an estate or trust be garnished? **11**

A. Only "debts" can be garnished **11**

i) Unpaid trust and estate distributions are debts 12

ii) A vested beneficial interest in money is a debt 12

iii) Unvested interests are not debts 17

iv) Estate money paid into court is not a debt 18

v) Non-monetary and future monetary obligations are not debts 19

vi) Money held in a solicitor's trust account is a debt unless it is a true retainer 22

vii) RRSPs are trusts and not debts 25

B. Notices of Garnishment must satisfy formal requirements **29**

i) Notice and service 29

ii) Full and fair disclosure 31

iii) Rule 75 is not an alternative to garnishment 31

IV. Writs of Execution against trusts and estates **32**

i) Execution against pecuniary interests in estates and trusts 32

ii) Execution against land held in trust 34

iii) Execution against contingent interests in land 37

V. Liability of the trustee **38**

VI. Conclusion **41**

[1] I extend my thanks to Jeanine Tang of Arkin Estate Law for research assistance with this article.

I. Introduction

The trustee-beneficiary relationship is usually a dance for two.[2] However, a beneficiary's creditor can swoop in to steal away the beneficiary's dance partner. The creditor's maneuver – serving a notice of garnishment or a writ of execution on the trustee – may have less flair than a silent film villain stealing the hero's consort at the ball, but it is just as effective at achieving the desired goal of taking what once rightfully belonged to the other.

What is a trustee to do when a creditor cuts in and looks to the estate or trust for satisfaction of the beneficiary's debt? This scenario puts the trustee in a perilous position: paying a creditor's demand without merit exposes the trustee to claims by the beneficiary; but making a distribution to the beneficiary in the face of a demand by a creditor exposes the trustee to claims by the creditor.

This article will examine a creditor's right to garnish or seize a beneficiary's interest in an estate or trust and give guidance to trustees who are presented with Notices of Garnishments or Writs of Execution.[3]

II. Enforcement by third parties: Notices of Garnishment and Writs of Execution

There is a comprehensive legislative scheme for enforcing court orders and collecting debts owing in Ontario, often referred to as "execution of judgment". Rule 60 of the *Rules*

[2] I will refer to all estate trustees and trustees of *inter vivos* and testamentary trusts generically as "trustees".

[3] Entirely different considerations apply if the debtor beneficiary is an undischarged bankrupt, which is outside the scope of this article. Also, this article considers the topic from the perspective of estates and trusts rather than from the perspective of drafting creditor-proof wills and trusts.

of Civil Procedure,[4] along with the *Execution Act*[5] and other ancillary legislation,[6] govern the process.

Two processes to enforce orders for the payment or recovery of money are most common: garnishment and writs of execution. To generalize, garnishment tends to be a simpler, faster, and more direct enforcement process, but is only available to intercept "debts" owing to the judgment debtor. In contrast, execution is indirect because it requires delegating enforcement to the sheriff,[7] which involves administrative delays and rule-based waiting periods. However, execution has the benefit of capturing the judgment debtor's non-debt property.

This article examines these two methods from the perspective of the trustee where the enforcement action is against a beneficiary of an estate or trust.

A. Garnishment generally

Garnishment refers, in its most basic sense, to a legal procedure by which a creditor can collect what a debtor owes by intercepting the debtor's property in the hands of someone other than the debtor. Historically, courts have referred to a debt that is subject to a garnishment order as an "attachable debt" and the enforcement procedure as an

[4] *Rules of Civil Procedure*, RRO 1990, Reg 194.
[5] *Execution Act*, RSO 1990, c E 24.
[6] See for example the *Wages Act*, RSO, 1990, c W 1 and the *Creditor's Relief Act*, 2010, SO 2010 c 6, Sch 4.
[7] In Ontario, the sheriff is a court officer responsible for enforcing civil orders. Pursuant to s. 141(1) of the *Courts of Justice Act,* RSO 1990, c C43 unless another act provides otherwise, civil court orders *shall* be directed to a sheriff for enforcement. Each county in Ontario has a sheriff and, pursuant to s. 3(2) of the *Creditors' Relief Act, 2010*, SO 2010, c 16, Sch 4, the garnished debt is usually paid to the sheriff for the county in which the debtor resides or, if the debtor resides outside the province, to the sheriff for the county in which the proceeding that gave rise to the judgment was commenced.

"attachment of debt". Garnishment is usually reserved for a creditor who has obtained a judgment or court order (the judgment creditor) against the debtor (the judgment debtor).

A common example is the garnishment of a judgment debtor's wages. A portion of the wages owed by the employer to the debtor employee is paid directly to the judgment creditor and bypasses the debtor's hands. The third party employer is called the garnishee. The garnishment process is not limited to garnishing wages; it extends to other debts such as funds in a bank account.

The purpose of the garnishment proceeding is to put the garnishee on notice that debts it owes to the debtor are to be repaid instead to the creditor.[8] The process is governed by subrules 60.08(1) to (23) of the *Rules of Civil Procedure*. The creditor obtains a Notice of Garnishment from the registrar after filing a requisition of garnishment, a copy of the order creating the judgment debt, and an affidavit setting out the particulars of the judgment debt including the amount owing, address of the debtor, name and address of the garnishee, etc.[9] The Notice of Garnishment is served on the garnishee with a blank garnishee's statement, and on the debtor with a copy of the affidavit required to obtain the Notice of Garnishment.[10] The garnishee must then pay the sheriff "*any debt of the garnishee to the debtor, up to the amount shown in the Notice of Garnishment*".[11] If the garnishee disputes the garnishment they must serve on the creditor and debtor and file with the court a completed garnishee's statement.

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[8] *International Union of Painters and Allied Trades, Local 200 v. S&S Glass and Aluminum* (1993) Ltd., 2004 CanLII 12611 (ONCA) at para. 23.
[9] Rule 60.08(4), *Rules of Civil Procedure.*
[10] Rule 60.08(7), *Rules of Civil Procedure.*
[11] Rule 60.08(11), *Rules of Civil Procedure.*

One reason to dispute the garnishment is that the garnishee owes no “debt” to the debtor. If there is no such debt, the garnishment is unenforceable against the purported garnishees and rule 60.08 is inapplicable.[12] Many of the cases discussed below turn on the question of whether the garnishee actually owed a “debt” to the judgment debtor. While the *Rules* do not define “debt”, there is some guidance in subrules 60.08(12) and (13) which provide that “debt of the garnishee to the debtor” *includes* a debt payable at the time the notice of garnishment is served and a debt payable (whether absolutely or on the fulfillment of a condition) after the notice is served and within six years after. However, a “debt of the garnishee to the debtor” *does not include*: money in an account opened *after* the notice of garnishment is served if the garnishee is a financial institution,; a debt arising out of employment that commences *after* the notice is served if the garnishee is an employer; or a debt payable under an insurance policy entered into *after* the notice is served if the garnishee is an insurer.

Garnishment is an equitable remedy, as noted by Nordheimer J. in ***20 Toronto Street Holdings Ltd. v. Coffee, Tea or Me Bakeries Inc.*** quoting from *Halsbury's Laws of England*:

> The court's power to make a garnishee order, whether it is an order *nisi* or an order absolute, is discretionary. A garnishee order is basically an equitable remedy, and it may be refused where the attachment of debt would work inequitably or unfairly or cause prejudice or injustice to some person or persons other than the judgment creditor.[13]

[12] *Richter LLP v. Big Truck TV Productions Inc*., 2015 ONCA 567 at para 19.

[13] *20 Toronto Street Holdings Ltd. v. Coffee, Tea or Me Bakeries Inc.* (2001), 53 OR (3d) 360 (SCJ) at para. 5 quoting *Halsbury's Laws of England*, 4th ed., vol. 17 at para. 539.

Justice Nordheimer concluded that, “as suggested by the use of the word ‘may’ in subrule 60.08(16) above, the court may therefore make whatever order it deems just in the particular circumstances of any given case.”[14]

The discretionary nature of garnishment orders was also addressed in ***International Union of Painters and Allied Trades, Local 200 v. S&S Glass and Aluminum (1993) Ltd.***[15] The Court noted that the language used in subrule 60.08(16), which governs garnishment hearings, is quite broad and not restrictive: “Any … interested person” may bring a motion pursuant to the subrule; the court “may” determine the “rights and liabilities of the garnishee” or “any other matter” in relation to a notice of garnishment. It “may” proceed in a summary manner.[16]

B. Writs of Execution generally

A writ of execution is a court document that gives the sheriff the authority to enforce court orders and judgments. An execution creditor is the person seeking to have the sheriff seize the debtor’s property in order to sell it to pay off a debt owing. An execution debtor is the person against whom a writ of execution is issued.

The definition of “property” that can be seized and/or sold by writ of execution is quite broad and includes: land;[17] goods, chattels and personal property including leasehold interests in any land and goods;[18] securities and security entitlements;[19] patents;[20]

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[14] *20 Toronto Street Holdings Ltd. v. Coffee, Tea or Me Bakeries Inc.* (2001), 53 OR (3d) 360 (SCJ) at para. 5 .
[15] (2004), 185 OAC 38 (CA) at paras. 19-20.
[16] See also *Wolf v. Anstett* 2012 ONSC 3220 at para. 19.
[17] *Execution Act*, RSO 1990, c E 24 s.9 (1).
[18] *Execution Act*, RSO 1990, c E 24 s.18 (1).
[19] *Execution Act*, RSO 1990, c E 24 s.14 (1).
[20] *Execution Act*, RSO 1990, c E 24 s.17 (1).

money, banknotes, surpluses of previous executions, negotiable instruments, accounts receivable, and choses in action;[21] and mortgages.[22] Interestingly, as will be discussed below, beneficial interests in trusts and estates other than beneficial interests in land are not mentioned in the *Execution Act*.

Pursuant to the *Execution Act*, there are different forms of writs, including: (a) a writ of seizure and sale; (b) a writ of seizure and sale of land; (c) a writ of seizure and sale of personal property; (d) a writ of sequestration; (e) a subsequent writ that may issue for giving effect to a writ listed in any of clauses (a) to (d); (f) an order for seizure and sale of personal property, real property or both real property and personal property; and (g) any other process of execution issued out of the Superior Court of Justice or the Ontario Court of Justice having jurisdiction to grant and issue warrants or processes of execution.[23]

The most commonly used writs of execution are writs of seizure and sale and writs of seizure and sale of land. If the debtor has been ordered by the court to pay the judgment creditor money but has not paid it, the judgment creditor can have the sheriff seize specific real estate and personal property owned by the debtor and sell the seized property at public auction so that the proceeds can be used to pay the judgment debt.

[21] *Execution Act*, RSO 1990, c E 24 s.19 (2).
[22] *Execution Act*, RSO 1990, c E 24 s.23.
[23] *Execution Act,* RSO 1990, c E 24, s. 1. An order for recovery or possession of land may also be enforced by a writ of possession, under rule 60.03. A writ of possession may be issued with leave of the court at the time an order entitling a party to possession is made (see subrule 60.10(1)). A writ of sequestration is issued where the property has not been delivered up under a writ of delivery (an order directing that personal property be taken from one person and delivered to another), and the court may order the issuance of a writ of sequestration to collect and hold any income from all or part of the property.

The judgment creditor can file a writ of seizure and sale of land against a debtor in any county or district where the debtor may own land or personal property. The writ would encumber any land or personal property presently owned or that may be purchased in the future.

The process of obtaining and having the sheriff enforce a writ of seizure and sale is set out in rule 60.07 of the *Rules of Civil Procedure*. First, the judgment creditor must file with the registrar where the proceeding was commenced a requisition setting out: the date and amount of any payment received since the order was made and the amount owing and the rate of post-judgment interest, together with a copy of the order as entered, and any other evidence necessary to establish the amount awarded and the creditor's entitlement.[24] If the creditor files the requisition electronically, neither the copy of the order entered nor any other evidence is required and the writ of seizure and sale will be issued electronically (note however that if six or more years have elapsed since the date of the order, leave of the court is required before you can requisition a writ). A writ of seizure and sale will then be issued. The creditor must file it with the sheriff in the county where the property is located. A writ that is issued electronically must be filed electronically.[25]

Next, a creditor who has filed a writ of seizure and sale can then file with the sheriff a copy of the order as entered, together with a direction to enforce (Form 60F) setting out certain required information including the date of the order and amount awarded, the rate of post-judgment interest payable, etc., and directing the sheriff to enforce the writ for the amount owing, subsequent interest and the sheriff's fees and expenses. If the writ is for

[24] Rule 60.07(1), *Rules of Civil Procedure*.
[25] Rule 60.07 (5.1-5.2), *Rules of Civil Procedure*.

the sale of land, the creditor must wait four months before directing the sheriff to sell the land. The creditor may file this direction to enforce electronically as well, in which case a copy of the order is not required.[26]

The sheriff may decline to enforce. In that case the creditor may make a motion to the court for directions.[27] Where a question arises in relation to the measures to be taken by a sheriff in carrying out an order, writ of execution, or notice of garnishment, the sheriff or any interested person may make a motion for directions.

Certain notices must be published before a sale of the debtor's property takes place and inventory of personal items must be made available.[28]

In order to determine the debtor's income and property, debts owed to and by the debtor, the debtor's present, past and future means to satisfy the order, etc., a creditor may examine the debtor in an examination in aid of execution.[29] Where any difficulty arises concerning the enforcement of an order, the court may make an order for the examination of any other person who the court is satisfied may have knowledge of the matter and make such order for the examination of any other person as is just.[30]

A debtor is entitled to certain exemptions from seizure of personal property such as: necessary clothing of the debtor and the debtor's dependants;[31] household furnishings and appliances that are of a value not exceeding the prescribed amount (currently

[26] Rule 60.07(13), *Rules of Civil Procedure*.
[27] Rule 60.07(13.1), *Rules of Civil Procedure*.
[28] Rules 60.07(15)-(21), *Rules of Civil Procedure*.
[29] Rule 60.18(1), *Rules of Civil Procedure*.
[30] Rule 60.18(6), *Rules of Civil Procedure*.
[31] s. 2(1)(1), *Execution Act*.

$13,150);[32] tools and other personal property of the debtor, not exceeding the prescribed amount in value, that are used by the debtor to earn income from the debtor's occupation (currently $29,100 for tillage of soil or farming, or $11,300 in any other case);[33] one motor vehicle that is of value not exceeding the prescribed amount (currently $6,600); [34] personal property prescribed by the regulations that is of a value not exceeding the prescribed amount (no amount prescribed);[35] principal residence of the debtor if it does not exceed the prescribed amount (currently $10,000);[36] and medical devices owned by the debtor that are required by the debtor or the debtor's dependants to assist with a disability or a medical or dental condition.[37]

III. Can a beneficiary's interest in an estate or trust be garnished?

A. Only "debts" can be garnished

A beneficiary's interest in an estate or trust can be garnished if the interest can be characterized as a debt. Specifically, garnishment requires a debt owing by the third party garnishee to the judgment debtor.

As noted above, "debt" is not defined in the *Rules of Civil Procedure*. Its definition must be found in common law. The Supreme Court of Canada in ***Diewold v. Diewold***[38] defined debt in relation to the *Farmers' Creditors Arrangement Act, 1934* as "a sum payable in respect of a liquidated money demand, recoverable by action". This definition was

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[32] s. 2(1)(2), *Execution Act*.
[33] s. 2(1)(3), *Execution Act*.
[34] s. 2(1)(4), *Execution Act*.
[35] s. 2(1)(5), *Execution Act*.
[36] s. 2(2), *Execution Act*.
[37] s. 2(4), *Execution Act.*
[38] [1941] SCR, 35, 1940 CanLII 52(SCC).

adopted by the Ontario Superior Court of Justice in the garnishment case of ***Building Solutions et. al. v. Benazzi***.[39]

i) **Unpaid trust and estate distributions are debts**

It seems to be settled law that a distribution to a beneficiary that has been allocated or declared but not paid is a debt. Similarly, a *sui juris* beneficiary's interest in a trust that he had the right to demand be paid and in fact demanded be paid is a debt until it is actually paid. However, as the following review of the cases shows, the boundaries of the definition of a debt are not necessarily clear in the context of estates and trusts.

ii) **A vested beneficial interest in money is a debt**

The 2009 Ontario Court of Appeal case of ***Ker Estate v. Stevenson***[40] seems to establish the rule that a beneficiary's vested interest in a cash legacy under a will is a debt and therefore susceptible to garnishment. It is worth noting that the reasoning in this case – which is binding in Ontario and does not seem to have any newer judicial treatment at the date of this article – is arguably at odds with the law of other provinces, older Ontario authority, and foundational principles of estate and trust law, as will be discussed below.

In *Ker Estate*, the testator, in her will, directed the trustees to use a certain amount of money to purchase a non-commutable life annuity for the beneficiary (i.e. an annuity that the beneficiary cannot collapse). On death of the beneficiary, any remaining value in the annuity would pass to the beneficiary's son. The life beneficiary was a judgment debtor. The judgment creditor obtained and served a Notice of Garnishment on the trustees. The

[39] 2015 ONSC 3948.
[40] 2009 ONCA 345.

trustees had not yet purchased the life annuity and they sought directions from the court on how to proceed.

The issue in the case was whether the beneficiary's interest in the estate was properly characterized as a debt, which is a precondition for garnishment.

In brief oral reasons, the motion judge concluded that the amount set aside to purchase the annuity had vested in her (that is, it was in the possession of, or assigned to her) on the death of the testator. Therefore, it was available to be garnished. The court relied on ***Re Robbins***, which established the rule that a *sui juris* beneficiary may elect to receive a cash legacy in the amount of the purchase price of an annuity rather than to receive the annuity mentioned in the will.[41] In that case, the testator by his will directed his trustees to purchase an annuity for his wife. The wife died before the husband's will was probated and before she made any election to take the value of the annuity in cash. The court held that the legacy and the right to take its present value in a lump sum vested in the wife at the time of her husband's death. Unless and until the trustees bought the annuity, it was regarded as a legacy of a definite sum vesting in the intended annuitant on the testator's death.

However, a key distinction between *Ker Estate* and *Re Robbins* – but one that seems to have gone unnoticed or at least unremarked on by the court – is that the gift to the wife in *Re Robbins* was absolute while the gift in *Ker Estate* was subject to a gift over to the life tenant's son.

[41] [1907] 2 Ch 8 (CA).

The court in *Ker Estate* also referred to ***Lotzkar v. McLean***, where the British Columbia Supreme Court applied the annuity rule in *Re Robbins*.[42] In *Lotzkar*, the testator left the residue of his estate to his children in two equal parts. He directed his trustees to purchase an annuity with each part. The children (who were two of the three trustees) sought directions from the court that each of them be paid a lump sum in lieu of the life annuities. The chambers judge followed *Re Robbins.* He concluded that the children each had an absolute beneficial interest and the trustees were bound to pay lump sums to each of them in lieu of the annuities on request.

The judge in *Lotzkar* also failed to notice or at least did not remark on the fact that, unlike in *Re Robbins*, the remaining value of the annuity on the death of the *Lotzkar* testator's two children was gifted over to the testator's remoter issue.

The Court of Appeal in *Ker Estate* examined the nature of an annuity and, in its review of the jurisprudence above, found that it could best be characterized as a legacy (a money gift under a will). The fact that it was "non-commutable" was not sufficient to persuade the court it should be characterized otherwise. As a result, it affirmed the motion judge's finding that the right to the annuity vested absolutely in the daughter at the deceased's death and could be garnished by the judgment creditor.

In both *Lotzkar* and *Ker Estate*, the court quoted the following excerpt from Jarman on Wills with approval:

> (vii) *Sum given to buy Annuity.* – Where there is a bequest of a sum of money to buy an annuity, the annuitant is entitled to have the money, because the annuity might at once be sold, and it would be idle to compel the annuitant to have an annuity which he could resell; this is the case even where the testator

[42] (1979) 15 BCLR 259.

> shows clearly that he means the annuity to be held by trustees as a personal provision for the annuitant, or even where he expressly declares that the annuitant shall not be allowed to accept the value of the annuity in lieu thereof, or that it shall cease on alienation, **unless such a condition is made effective by a gift over**.[43] [emphasis added]

However, in neither case did the court seem to consider the last phrase of this excerpt, which makes the annuities rule in *Re Robbins* inapplicable if there is a gift over. Nor does it appear from the Court of Appeal's reasons in *Ker Estate* that the law on vesting of successive and contingent interests and the rule in *Saunders v. Vautier* were argued explicitly.

Viewed through this prism, *Lotzkar* and *Ker Estate* are arguably incorrectly decided.

There is another feature of *Ker Estate* that puts it at odds with other garnishment cases, with which it is hard to reconcile.[44] The court treated the beneficiary's interest as a debt owing to her by the estate merely by virtue of the fact that the beneficiary's interest had vested. The court did not consider it necessary for the trustee to have declared a distribution. The beneficiary of the gift over raised this point on appeal. He argued that while his mother, the life tenant judgment debtor, may be able to call for payment of a lump sum in lieu of the purchase of an annuity, she had not actually done so. He asserted that a third party judgment creditor has no right to make that election in her place. However, Armstrong J.A., on behalf of the Court of Appeal held that: "In the view that I take of the applicable law, there is no basis to conclude that the trial judge erred in failing to make that distinction. According to the applicable law, the sum of money available for

[43] *Ker Estate*, *supra*, citing Jarman on Wills, 7th ed. (1930), vol. 2, p. 1109.

[44] E.g. cases such as *Re Bliss, Kirsh and Doyle et al; Montreal Trust Co., Garnishee*, 1983 CanLII 1626 (ONSC); and *Collins Barrow Leamington LLP v Tiessen*, 2014 CanLII 72252 (ON SCSM).

the purchase of the annuity vested in the [daughter] and therefore was subject to garnishment".[45]

With the notable exception of *Ker Estate*, the garnishment cases mostly seem to make a distinction between a merely vested interest in a trust or estate and a debt presently owing to a beneficiary from a trust or estate. *Ker Estate* may have erased that distinction in Ontario. Whether or not the rule in *Ker Estate* is appropriate as a matter of policy (and a strong argument can be made that it is), it undermines the internal consistency of long-established principles of trust law. A legacy that vests in a beneficiary at death may still abate if the estate does not have sufficient assets to pay its debts and the legacy in full. A trustee acting reasonably cannot be compelled to pay out a legacy until the estate's debts have been ascertained and paid. In other words, a vested legacy may not result in a debt to a beneficiary at all, a point that the court did not seem to take notice of.

On the other hand, as a matter of policy, it seems reasonable that creditors would have the right to garnish a beneficiary's vested but undistributed interest in an estate or trust on an if-and-when basis. There is no principled distinction between, say, garnishing an employee's future wages and garnishing a beneficiary's future distribution.

The facts in *Ker Estate* were unique and somewhat unusual. It would be interesting to see how the courts would deal with the garnishment of a simple specific legacy or gift of residue. Unfortunately, there are no reported cases dealing with the issue. A trustee served with a Notice of Garnishment would be well advised to consider the application of *Ker Estate*.

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[45] *Ker Estate v. Stevenson* 2009 ONCA 345 at para. 28.

iii) Unvested interests are not debts

Although vested interests in trusts or estates that have not been distributed/allocated may be debts pursuant to *Ker Estate*, it is unambiguous that unvested interests (e.g. an interest in a discretionary trust) are not debts.

In ***Wells (Hodgson) v. Hodgson***,[46] a father owed money for child support pursuant to an agreement entered into with the mother. The father's aunt died with a will giving him the right to reside in her house for as long as he wished to do so; and creating a discretionary trust to provide for his support during his life. The Director of the Family Responsibility Office served a garnishment notice on the estate trustees to garnish the father's interest in the estate.[47]

The trustees cut off any discretionary distributions to the husband to prevent the funds from being siphoned off by the mother as support arrears. The court noted that the mother seemed to have a "single-minded campaign" to secure over $300,000 from the estate, but her plan was doomed to fail because the father had only a discretionary life interest in the estate. Any actual distributions made to him could be garnished, but his interest in the estate was unvested and could not be garnished.

[46] 2011 ONCJ 704.

[47] The Family Responsibility Office has the authority to enforce spousal and child support by virtue of the *Family Responsibility and Support Arrears Enforcement Act, 1996,* SO 1996, c 31. Under s. 20(5) of the FRSAE, a notice of support deduction order is deemed to be a notice of garnishment made under provincial garnishment law.

iv) Estate money paid into court is not a debt

In ***Assaf Estate (Re)***,[48] the applicant was entitled to an annual payment from the estate of her late husband, but the estate assets had previously been liquidated and paid into court. In this chapter of the long-running case, the court authorized the Accountant of the Superior Court of Justice to pay to the applicant her annual payment out of the funds in court. However, the applicant already had outstanding costs orders against her and the judgment creditors (the estate trustees) served a Notice of Garnishment on the Accountant of the Superior Court of Justice to intercept the annual payment.

The applicant took the position that the funds payable to her out of court were not “debts” within the meaning of Rule 60.08.

Brown J. undertook a thorough review of the case law on this issue (including ***Royal Bank of Canada v. Van Buren and McKay***,[49] ***Canadian Imperial Bank of Commerce v. Smith***,[50] ***Provincial Treasurer of Alberta v. Zen***,[51] and ***Bland v Andrews***[52]) and concluded that there was no debtor-creditor relationship between the Accountant of the Superior Court of Justice and the judgment debtor. The Accountant is a servant of the Crown and owes its existence and authority to legislation. The legislative scheme did not allow for an interpretation in which the Accountant could owe a debt. The Notices of Garnishment were set aside.

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[48] 2008 CanLII 42420 (ONSC).
[49] [1927] 1 WWR 268 (Alta SC, MC) at paras. 16 and 17.
[50] [1976] 5 WWR 643 at p. 651.
[51] [1981] 5 WWR 188 (BCSC.
[52] (1880), 45 UCQB 431.

The court noted that the judgment creditor in this case was not without a remedy. There is a procedure for intercepting money paid, which is set out in rule 72.05 and section 23 of the *Creditors' Relief Act*. These gave the judgment creditors the appropriate tools to execute on funds that a court has ordered to be paid out to a judgment debtor.

v) Non-monetary and future monetary obligations are not debts

While the case of ***Hansen v. Danstar Mines Ltd.*** dealt mostly with a jurisdictional issue (the enforcement of an extra-jurisdictional garnishment order) the court also looked at whether bonds held in trust by a trustee for a beneficiary could be subject to a garnishment order.[53] Sullivan J.A. noted that there was no definition of debt given in the garnishment legislation of Manitoba, and went on to consider whether under the rules and the practice of the courts, garnishment "catches" assets other than those which are payable in some monetary form or its equivalent. For guidance, Sullivan J.A. turned to the Manitoba decision of ***McFadden v. James Kerr (Robert Kerr Garnishee)***[54] which dealt with the following situation:

> Where A has sold and conveyed land to B under an agreement that if B could at any time resell the property for a larger amount he would account to A for the excess, there is nothing upon which to base a garnishing order at the instance of a creditor of A, as there is neither any debt owing or accruing from the garnishee to the debtor, . . .[55]

In the scenario in *McFadden*, A was the judgment debtor and B would be the garnishee. The agreement between A and B was that if B sold the land and receive more than $1,800.00 for it, he would hold any surplus in trust for A, the judgment debtor. The judge

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[53] [1978] CanLII 1932 (MBCA).
[54] (1897-99) 12 Man R, 487.
[55] *Hansen v. Danstar* [1978] CanLII 1932 (MBCA) at para. 61.

in that case said that, "in a trust of this kind, it is impossible to say that the trustee is a debtor to his *cestui que* trust before he has, or but for some fault of his own might have had, the money which it would be his duty to pay over." The garnishee held land in trust for the judgment debtor which *might* at a future date be converted to a money obligation. The judge went on:

> It is clear, I think, that the judgment debtor's claim or demand against the garnishee arising out of the relation between them as trustee and *cestui que* trust is not one that he would require equitable execution to make available, or that could be made available to him by such means. … Whatever judgment the judgment debtor here might obtain against the garnishee for enforcing the trust, the Court would enforce it directly against the garnishee of his property; … The judgment creditor may have other remedies for availing himself of the debtor's interest in this land, but he cannot reach it, I think, by garnishing the trustee.

The Court in *Hansen* wrote the following concerning *McFadden*:

> In [*McFadden*], the garnishee held land in trust for the judgment debtor which might at a future date be converted into a money obligation. **The interest of the judgment debtor in the land could not be attached by garnishment**. In the case before us, the garnishee holds bonds in trust for the judgement debtor. They may at a future date be converted into a money obligation. If that happens; there will be a monetary obligation by the trustee in favour of the judgment debtor. **But until that happens, there is no money obligation and the judgment debtor's interest in the bond is not subject to garnishment**. This is not a case of *debitum in presenti, solvendum in futuro*, but one of no existing debt, claim or demand payable in money.[56]

Another Manitoba authority relied on in *Hansen* was ***The Lake of the Woods Milling Co. v. Collin***.[57] In that case, a creditor sought to garnish the insurance company against which the debtor had a claim for indemnity as a result of loss due to a fire. The insurance policy provided that a claim would not be payable until 30 days after the completion of

[56] *Hansen v. Danstar Mines Ltd.* [1978] CanLII 1932 (MBCA) at para. 63.
[57] (1900), 13 Man. R. 154.

proofs of loss. The question was whether the claim could be attached (garnished). On the one hand, it was an obligation or liability of the insurance company, but on the other hand, it was not payable in money at the time of the garnishing order. The language of the relevant garnishment legislation was very broad, referring to "debts, obligations and liabilities". The court in *The Lake of the Woods* held as follows:

> Now while the words 'obligations and liabilities' are very wide, it is clear from the nature and course of this legislation and from the accompanying provisions for working it out, that only a pecuniary liability can be attached. This consideration excludes any liability or obligation arising from a mere contractual relation under which the garnishee has bound himself to do any other act than the payment of money, unless and until he has made such a breach that a money demand has arisen against him. And the words 'debts, obligations and liabilities' are further limited by the words 'owing, payable or accruing due'.[58]

The court in *Hansen* noted that this reasoning was convincing and that it was "authority for the conclusion that bonds held in trust by a trustee for a beneficiary cannot be attached by the beneficiary's creditors by means of garnishment."[59]

The Ontario case of ***Building Solutions International Inc. v. Benazzi***[60] addressed the question of whether interests in mortgages held in trust are "debts" and therefore subject to garnishment. The plaintiffs (the judgment creditors), obtained Notices of Garnishment seeking to garnish monies and certain mortgages held by a lawyer and his professional corporation in trust for the judgment debtor, a mortgage investment corporation.

Relying on the cases of *Hansen* and *McFadden* discussed above, Brown J. concluded: "I read *Hansen* as meaning that interests in properties such as bonds and mortgages, held

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[58] *The Lake of the Woods Milling Co. v. Collin* (1900), 13 Man R 154 at p. 163.
[59] *Hansen v. Danstar Mines Ltd.* [1978] CanLII 1932 (MBCA) at para. 71.
[60] 2015 ONSC 3948.

in trust by another, are non-monetary obligations which cannot be subject to garnishment until they are converted into money obligations at a future date. Until that time, there is no existing debt, claim or demand payable in money."[61]

The mortgage held by the lawyer and his law firm in trust was not a liquidated money demand, and, therefore, not a debt until it was converted into money obligations. The lawyer was not a mortgagor in relation to the judgment debtor and had not given a covenant to pay a debt to the judgment debtors. Rather, he held mortgage interests in land in trust for the judgment debtor. Those interests did not constitute debts pursuant to rule 60.08. Brown J. went on to add that the lawyer, "does not dispute the fact that any payments received from the mortgagors and to the benefit of the judgment debtor are debts subject to garnishment."[62] An interest in land including a mortgage is not a liquidated money demand and is therefore not subject to garnishment.

vi) **Money held in a solicitor's trust account is a debt unless it is a true retainer**

In ***Toronto Dominion Bank v. Cooper, Sandler, West & Skurka***,[63] the court concluded that where a client is a judgment debtor, funds held in his or her lawyer's trust account as a "true retainer" for legal services are not subject to garnishment under rule 60.08(1) (nor subject to execution pursuant to s.19(1) of the *Execution Act*).

[61] *Building Solutions et al. v. Benazzi et al.,* 2015 ONSC 3948 at para. 8.
[62] *Building Solutions et al. v Benazzi et al.*, 2015 ONSC 3948.
[63] [1998] 37 O.R. 3d 729 (Gen Div), 1998 CanLII 18860 (ONSC).

The judgment debtor had retained the lawyer to defend him against criminal charges. The client paid the lawyer $15,000 in trust as retainer. The client's bank had obtained judgment against him and served a Notice of Garnishment on the lawyer.

The motion judge held that this was a "true retainer" and rejected the bank's argument that the retainer was analogous to a term deposit that had not yet matured and was susceptible to being garnished.[64] The motion judge quoted with approval Justice MacDonald in ***Johnson & Higgins Willis Faber Ltd. v. Mayo Helicopters***[65] that there, "is an essential difference between a term deposit and a true retainer. The former will ultimately become payable when the conditions of deposit are satisfied. The retainer may never become payable."[66]

The bank also argued the retainer funds were analogous to other garnishable funds such as payments under a building contract where an architect's certificate was required for payment[67] or the balance of funds held in a solicitor's trust account as proceeds of sale of the debtor's property, after the solicitor's fees and disbursement had been deducted.[68] The court held that these cases and circumstances were distinguishable. In the situations above:

> the moneys never lost the inherent characteristic of being owed to the judgment debtor by a third party, even when subject to certain conditions. The judgment debtor could demand and expect repayment in due course. These funds are really in the pocket of the judgment debtor and thus available to the

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[64] See *Bel-Fran Investments Ltd. v. Pantuity Holdings Ltd.,* [1975] 6 WWR 374, 62 DLR (3d) 140 (BCSC).
[65] *Johnson & Higgins Willis Faber Ltd. v. Mayo Helicopters Ltd*. (1978) 8 CPC 97.
[66]*Johnson & Higgins Willis Faber Ltd. v. Mayo Helicopters Ltd*. (1978) 8 CPC 97 at p.104.
[67] See *Sandy v. Yukon Construction Co*. (1960), 33 WWR 490, 26 DLR (2d) 254 (ABCA).
[68] See *Bank of Montreal v. Chantry*, [1979] 5 WWR 470 (Sask. Dist. Ct.) and *Canadian Imperial Bank of Commerce v. Campbell*, [1976] 1 SCR 341, 20 CBR (NS) 205.

> garnishee. This is not the case with respect to the true retainer; a solicitor continues to have an interest in the funds.[69]

The court concluded that, "as long as the moneys in the solicitor's trust account can be classified as a true retainer they do not belong to the client and are not subject to execution."[70] The court also examined s.14(3) of the *Law Society Act*[71] s.14(3) which states:

> Trust money is money received by a member that belongs in whole or in part to a client or that is to be held on the client's behalf or to the client's or another's direction or order, and includes money advanced to a member on account of fees for services not yet rendered or money advanced on account of disbursements not yet made.

The court found that this provision recognizes that the solicitor may hold money in a trust account as a bare trustee or as a retainer. Money in a solicitor's trust account, depending on the facts, could be available for garnishment and/or execution. However, on the facts in *Toronto Dominion*, the retainer was subject neither to garnishment nor to execution. The court concluded that:

> While the relationship of solicitor and client is extant, the solicitor continues to have an interest in the retainer for services rendered. Once the relationship is terminated by either party, for whatever reason, then depending on the circumstances, the balance of the funds may be owing to the client and subject to garnishment. On termination, the balance may also be encompassed by the broad definition of exigible property. Service of the notice of garnishment and/or seizure does not operate to terminate the relationship between the solicitor and client and the funds do not become available to the judgment creditor as a result of such service only. On the other hand, moneys in a solicitor's trust account are not invariably immune from the assault of judgment creditors. Only the true retainer that will benefit both solicitor and client is protected. However, the protection is very broad and is wide enough to

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[69] *Toronto Dominion Bank v. Cooper, Sandler, West & Skurka* [1998] 37 OR 3d 729 (Gen. Div.), 1998 CanLII 18860 (ON SC) at para.15.

[70] *Toronto Dominion Bank v. Cooper, Sandler, West & Skurka* [1998] 37 OR 3d 729 (Gen Div), 1998 CanLII 18860 (ON SC) at para. 23.

[71] RSO 1990, c.L.8.

> encompass matters within the contemplation of the parties at the time the retainer is given.[72]

The Divisional Court distinguished *Toronto Dominion* in the decision of ***Parker v. Parker***.[73] At first instance, the motion judge in *Parker* found that the funds held in trust by the judgment debtor's lawyers were not garnishable because they were not a debt owed by the law firm to the debtor. However, the Divisional Court found this conclusion to be in error. In *Toronto Dominion* the funds in the trust account were a retainer for legal services and not a debt owed by the law firm to the debtor. In *Parker*, the funds in trust were advanced by the judgment debtor to be paid to the judgment creditor to satisfy a mortgage debt. The funds could have been withdrawn by the judgment debtor had he changed his instructions, and, "accordingly, the funds were subject to garnishment."

Despite this error, the Divisional Court did not reverse the motion judge's decision. The court found that although the funds were garnishable, the equities did not favour garnishment. The motion judge described the Notice of Garnishment as an "oppressive step that should not be condoned by the court" and the Divisional Court found no basis to interfere with that exercise of discretion.[74]

vii) **RRSPs are trusts and not debts**

Registered Retirement Savings Plans (RRSPs) are trusts (unlike deposit accounts, which are choses in action and qualify as debts). The financial institution is a trustee for the planholder/annuitant beneficiary. Unlike in *Ker Estate*, the courts in the RRSP cases have

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[72] *Toronto Dominion Bank v. Cooper, Sandler, West & Skurka,* [1998] 37 OR 3d 729 (Gen Div), 1998 CanLII 18860 (ON SC) at para.25.

[73] 2014 ONSC 3398 (Div Ct).

[74] *Parker v Parker* 2014 ONSC 3398 (Div Ct) at para. 6.

typically (but not always) held that the beneficiary's interest in an RRSP is not a debt receivable and cannot be attached by garnishment.

In ***Re Minister of National Revenue and Gero***,[75] the court looked at whether the proceeds of an RRSP can be attached in garnishment proceedings. In this case the funds were said to, "resemble demand bank deposits made by [the judgment debtor] which are undoubtedly seizable," in garnishment proceedings. Walsh J. observed that, "it is arguable that these sums are not debts 'owing or accruing' to the judgment debtor unless and until he requests the trust companies to make payment to him, but it would be contrary to the whole principle of garnishment proceedings to adopt such an interpretation and hence provide a means for an individual to shelter his assets form seizure by his creditors."[76] The judgment debtor's RRSP was successfully garnished.

In ***McMahon v. Canada Permanent Trust Company***,[77] a bankrupt borrowed money from a trust company and used it as a contribution to his RRSP with the same trust company. The trustee in bankruptcy claimed the funds held by the trust company in the RRSP. The trust company refused to pay on the grounds that it had the right to set off the funds in the RRSP against the debt it was owed by the bankrupt, set-off being essentially the self-help cousin of garnishment. The British Columbia Court of Appeal said:

> As I have already mentioned, it was common ground that, notwithstanding the terms of the trust, the bankrupt, or his trustee in bankruptcy acquiring all his rights, could unilaterally terminate the registered retirement savings plan and recover the funds held in the plan. I am unable to find any reason to conclude

[75] 1979 CanLII 2554 (FC), 103 DLR (3d) 310.
[76] *Re Minister of National Revenue and Gero*, 1979 CanLII 2554 (FC), 103 DLR (3d) 310 at p. 312.
[77] (1980), 1979 CanLII 769 (BC CA).

> that the fact of bankruptcy itself in any way altered, varied or changed the trust.[78]

In other words, the right of set-off can be exercised against a debt, but not against a trust like an RRSP. The court ordered the trust company to account to the trustee in bankruptcy for the full value of the RRSP.

In ***Vancouver A&W Drive-Ins Ltd. v. United Food Services Ltd. et. al.***,[79] Justice Fulton concluded that the *Gero* case (which held that an RRSP is akin to a deposit account and can be garnished) could not be reconciled with the views expressed by the British Columbia Court of Appeal case in *Re McMahon* (an RRSP is a trust and not susceptible to set-off), by which he was bound. He noted that, "for although there is no doubt that in law bank deposits do create a debtor-creditor relationship and are therefore subject to attachment by garnishing order, our Court of Appeal has held that the deposit funds in an RRSP does not create a debtor-creditor relationship but rather an exclusively trustee-*cestui que trust* relationship".

In Ontario, the court in ***Re Bliss, Kirsh and Doyle et al; Montreal Trust Co., Garnishee*** commented:

> In this case it has not been shown that there is a duty or an obligation on the part of the judgment debtor to demand from Montreal Trust Company payment of the proceeds of the R.R.S.P. of which it is trustee. In the absence of such a duty, equity does not treat the demand as having been made. Without such a demand it cannot be said that the rule in *Saunders v. Vautier* applies to bring the trust to an end and to make the judgment debtor a creditor of Montreal Trust Company. There being no debt owing or accruing from Montreal Trust

[78] *McMahon v Permanent Trust* (1980), 1979 CanLII 769 (BC CA) at para.7.
[79] 1981 CanLII 778 (BCSC).

> Company to the judgment debtor, resort cannot be had to Rule 597 [garnishment].[80]

In ***National Trust Co. v. Lorenzetti***,[81] Trainor J. held that the proceeds of an RRSP on which a beneficiary had not been designated and on which an annuity had not been purchased were liable to execution under the *Execution Act,* but not through garnishment. This was because as *cestui que trust* under the plan, the judgment debtor held the equitable or beneficial interest in the fund and the *Execution Act* permits the sheriff to seize and sell any equitable interest in personal property of the judgment debtor.

The court reviewed the findings and conclusions in *Bliss*, *McMahon*, *Gero, A&W,* and *National Trust* in the 2014 (i.e. post-*Ker Estate*) case of ***Collins Barrow Leamington LLP v. Tiessen***.[82] The court concluded that:

> While the equities herein favour the Creditor in its efforts to collect on the Default Judgment from the RRSP, it is quite apparent that the law does not support or permit it to be accomplished by way of garnishment. . .Try as I might to enable the Creditor to recover based on the Notices of Garnishment, the case law simply does not support such a conclusion. Garnishments are used to intercept debts owing to the Judgment Debtor, but the existence of an RRSP in favour of the Judgment Debtor does not give rise to or create a debtor-creditor relationship. RRSPs give rise to and create a trust relationship for which the Judgment Debtor is the beneficiary and which represents personal property of the Judgment Debtor.[83]

Funds in an RRSP cannot be garnished because there is no debtor-creditor relationship. If the planholder were to demand payment of the proceeds, the plan would then collapse in whole or in part, the trust would end, and the planholder would become a creditor of the financial institution. However, there is no way to compel the planholder to take steps

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[80] *Re Bliss, Kirsh and Doyle et al; Montreal Trust Co., Garnishee,* 1983 CanLII 1626 (ONSC) at 12.
[81] (1983), 41 OR (2d) 772, 148 DLR (3d) 575 (HCJ).
[82] 2014 CanLII 72252 (ON SCSM).
[83] *Ibid.* at para. 50.

to withdraw the funds and, without a writ of execution, an RRSP cannot be forcibly collapsed.

The RRSP cases, which seem to forbid garnishment because RRSPs are trusts, are difficult to reconcile with the Ontario Court of Appeal case of *Ker Estate* where the court essentially commuted a life tenant's vested but undistributed interest and extinguished a gift over in order to satisfy a judgment creditor.

B. Notices of Garnishment must satisfy formal requirements

i) Notice and service

The case of ***Ontario (Director, Family Responsibility Office) v. Hay Estate***,[84] illustrates the importance to a judgment creditor of ensuring that the formal requirements for garnishment are met, and the importance to a trustee of considering the availability of technical defences to garnishment of a beneficiary's interest.

In this case, a beneficiary of an estate had several outstanding support orders against him. The Family Responsibility Office (FRO) served Notices of Garnishment on the estate trustees by mail. Subsequently the trustees paid out money from the estate to the judgment debtor beneficiary. The FRO then served a Notice of Garnishment on the trustees claiming that the trustees must personally pay the debt owing by the judgment debtor.

The trustees asserted that they did not know about the garnishment when they paid out the money to the beneficiary. The first Notice of Garnishment was sent to a post office

[84] 2002 CarswellOnt 999.

box for which only the judgment debtor had a key. He did not tell the trustees that he received a Notice of Garnishment.

The trustees acknowledged that they received the second Notice of Garnishment, but it was addressed to them personally and not in their capacity as trustees. Based on this, they disputed the Notice of Garnishment on the basis that neither of them owed the judgment debtor any money personally. When they received a third Notice of Garnishment properly addressed to them as trustees, they stopped payment of any further money to the beneficiary pending the garnishment hearing.

The court found that the first notice had not come to the attention of the trustees. Service by ordinary mail pursuant the *Family Law Rules* was *prima facie* evidence that the first notice was received by the trustees, but that they discharged the burden of proving, on a balance of probabilities, that they did not receive the document. The court believed the trustees' explanation that the judgment debtor intercepted the notice and that it had not come to their attention. The court found that the second notice was not valid because it did not mention the estate or the garnishees as the trustees and the trustees did not owe any debt personally to the judgment debtor. The third notice was found to be valid and the trustees were ordered to pay any further money that became owing and payable to the beneficiary to the judgment creditor. However, the trustees were not personally liable for any funds previously paid out to the beneficiary.

A succeeding trustee will be liable for effective notice of a transfer of rights given to the preceding trustee. In *Slattery v. Slattery*,[85] the succeeding estate trustees argued that

[85] *Slattery v. Slattery*, [1945] OR 811.

they should not be made liable as the notice of garnishment was made to the preceding estate trustees and they did not know about it. The court denied this defense and stated that the initial notice of garnishment to the first trustees was effective and the succeeding estate trustees would have had notice of it if they looked through all the preceding trustee's documents. That being said, if the preceding trustee does not leave a copy of the notice amongst the trust documents, the succeeding trustee may not be found liable.[86]

ii) **Full and fair disclosure**

A Notice of Garnishment is obtained from the court without notice to the judgment debtor. The judgment creditor must make full and fair disclosure in its affidavit filed in support of the Notice of Garnishment. Failure to do so is in itself a sufficient ground to set aside the Notice of Garnishment.

iii) **Rule 75 is not an alternative to garnishment**

In ***Belz v. Mernick***,[87] a judgment creditor took a different approach to trying to attach a beneficiary's interest in an estate. The beneficiary's judgment creditor brought an application for directions under Rule 75 (i.e. the rule governing contentious estate disputes) on the grounds that it had a "financial interest in the estate" as required for standing under rule 75.01. Justice Haley concluded that this does not qualify as "a financial interest in an estate", stating: "While it is true that the applicant as a judgment creditor may have a 'financial interest' in the estate . . . I think that interest can be more

[86] *Hallows v. Lloyd, (1888)*, 39 Ch D 686.
[87] [2000] 31 ETR (2d) 27, [2000] OJ No 542 (SCJ).

precisely expressed as an interest in the beneficial interest which [the beneficiary] has in the estate."

IV. Writs of Execution against trusts and estates

One lesson from the many unsuccessful garnishment cases is that judgment creditors choose garnishment proceedings to the exclusion of execution proceedings at their peril.

i) Execution against pecuniary interests in estates and trusts

It is not entirely clear whether a judgment creditor can execute against a beneficiary's pecuniary interest in an estate or trust; e.g. a legacy, interest in income during the beneficiary's lifetime, or an interest in the residue of an estate.

The few cases that deal with executions in the estates and trusts context deal with land held in trust, which is explicitly provided for in the *Execution Act*. There appear to be no cases dealing with execution against a beneficiary's pecuniary interest in a "typical" estate or trust. There are cases dealing with execution against RRSPs, which are technically trusts. For example, in ***Re Cameron***, the Federal Court made the following comment:

> I therefore conclude that a writ of execution delivered by a Sheriff on a financial institution holding, as Trustee, RRSP funds of a Judgment Debtor under a plan allowing the Judgment Debtor to collapse and redeem the account on demand is sufficient, without further specific order of the Court, to require the financial institution to sell the assets in the RRSP and remit the proceeds thereof to the Sheriff in satisfaction of the writ.[88]

The dearth of execution cases against estates and non-RRSP trusts could be because the situation does not arise frequently; because garnishment is the easier and less

[88] 2007 FC 319 (CanLII) at para. 7; referred to with approval in *Collins Barrow Leamington LLP v. Tiessen*, 2014 CanLII 72252 (ON SCSM).

expensive route for judgment creditors; or because there are fewer opportunities for these cases to come before the courts. In the garnishment context, a creditor, debtor, garnishee, co-owner of debt, or any other interested person may bring a motion to determine the rights and liabilities of the garnishee, the debtor, and any co-owner, or to determine any other matter in relation to a notice of garnishment.[89] No similar provision is available in the *Rules of Civil Procedure* for writs of execution. A creditor may make a motion to the court for direction where the sheriff is uncertain whether the writ of seizure and sale has been properly issued or filed.[90] Further, Rule 60.07, dealing with writs of seizure and sale, contains no provision permitting a person against whom a writ is sought to be enforced to move to set aside the judgment pursuant to which the writ was issued.[91]

In my view, considering the question as a matter of principle, in the context of the legislation and rules governing execution, and in light of cases about execution against RRSPs, there should be no bar to execution against a beneficiary's pecuniary interest in a trust or estate.

Execution against a beneficial estate or trust may fall under or be analogous to s. 19(2), paragraph 4 of the *Execution Act*, which allows the sheriff to seize choses in action. Interestingly, if the sheriff attempts to seize property under this section and fails, the judgment creditor may independently sue in the name of the sheriff. Alternatively, execution against and estate or trust may fall under s. 18(1), which allows the sheriff to seize and sell, "any right, property, interest … in respect of any … personal property."

[89] See Rule 60.08(16), *Rules of Civil Procedure.*
[90] Rule 60.07(13.1), *Rules of Civil Procedure*. There is only one reported decision dealing with this rule: *Sistem Mühendislik naat Sanayi Ve Ticaret Anonim Sirketi v. Kyrgyz Republic*, 2012 ONSC 4351.
[91] *Sistem Mühendislik naat Sanayi Ve Ticaret Anonim Sirketi v. Kyrgyz Republic*, 2012 ONSC 4351 at para.30.

Given the dearth of cases and the omission of any explicit provision allowing the sheriff to execute against pecuniary interests in trusts or estates, it would be sensible for a trustee to consider seeking directions from the court if faced with a writ of execution in these circumstances.

ii) **Execution against land held in trust**

Section 9(1) of the *Execution Act* allows a sheriff acting under a writ of execution against lands to seize and sell lands of the debtor. Key to the topic at hand is that this provision specifically includes an interest held in trust. The sheriff may seize and sell: "…*any lands whereof any other person is seized or possessed in trust for the execution debtor…*"

In the case of ***Banglar Progoti v. Ranka Enterprise Inc***.,[92] the court confirmed that a beneficiary's interest in a bare trust in land is exigible by writ of seizure and sale. In that case a numbered company held real property in a bare trust solely for the benefit of the judgment debtor. Pepall J. (as she then was) concluded that, "the evidence is clear, and there is no evidence to the contrary, that [the debtor] has a 100% beneficial interest in the [property]. [The applicant] is a judgment creditor and [the debtor] holds a real property interest in the [property] as required by Rule 60.07. It seems to me that judgment creditors of [the debtor] should be able to realize on that asset."[93]

In ***Michaud v. Coresiab Structures (Ont) Inc.***,[94] the applicant held certain lands in trust for a numbered company. He executed a declaration of trust but the declaration was not registered on title. The applicant had been prevented from conveying the lands to an

[92] 2009 CanLII 16292 (ONSC).
[93] *Banglar Progoti Ltd. v Ranka Enterprises Inc.* 2009 CanLII 16292 (ONSC) at para. 29.
[94] 2012 ONSC 355.

arm's length *bona fide* purchaser because of a writ of execution registered against the applicant's name. The court ordered that the writ be temporarily lifted to allow the sale to proceed and ordered the proceeds to be held in trust by the vendor's (the numbered company's) lawyer. The applicant sought an order that the writ of execution against his name did not attach to the lands that he held in trust and that the funds held by the lawyer should be disbursed as directed by the vendors. The applicant argued he owed a debt to the respondent in his personal capacity but not in his capacity as trustee.

The court noted that subsection 9(1) of the *Execution Act* provides that where another person is possessed in trust of land for the benefit of the execution debtor, then the sheriff may seize and sell the land. However, in this case the execution purported to attach to lands that were held by the execution debtor as trustee, not as beneficiary, which would be contrary to the scheme of the *Execution Act*.

The applicant's evidence that he never had an ownership interest in the lands in question other than as trustee nor had he personally benefited from the holding of title to the lands in question as trustee was unchallenged. The court concluded that s.9(1) does not permit the seizure and sale of real property held by the applicant in trust and that the declaration of trust ranked in priority to the writ of execution.

In ***Colantino v. Don Park LP et. al.***,[95] the applicant transferred legal title in a property she owned to her two sons, each as to an undivided one-half interest, but reserved a life interest for herself. The applicant also signed a declaration of trust that stated in part that the sons held the property as bare trustees on behalf of the mother and that as trustees

[95] 2013 ONSC 1059.

they, “agree at the written request and cost of [the mother] to transfer title to her or as she may direct.” The declaration also stated that, “notwithstanding that the ownership of lands may be registered in the names of the Trustees, the true and beneficial ownership,” is vested in the mother. The declaration was never registered on title to the property.

Eventually, the mother wanted the property to be re-conveyed to her so she could rent it out. However, before this could be done, one of the sons died. The estate trustees of the son’s estate agreed to re-convey the property back to the mother. However, certain judgment creditors of the deceased son had executions against him on title to the property which prevented clear title from being conveyed back to their mother. The son had advised the creditors that he lived at the property and that he owned the property free and clear, which the court noted was “false, or at the very least quite misleading.”

The applicant sought a declaration that she was the legal and beneficial owner of the property, that the son’s estate had no beneficial interest in the property, and that the writs of seizure and sale filed by the judgment creditors did not attach to and create an interest in the property. The applicant died before the hearing but the application was continued by her estate trustees on behalf of her estate.

The judgment creditor argued that there was no valid trust in the first place as it lacked certainty. The court noted that its task in interpreting the Declaration of Trust, as with interpreting a will, is to “give full effect to the testator’s [settlor’s] intentions as far as possible. Those intentions are to be determined in light of the circumstances existing when the Will [Declaration] was executed.”[96] Relying on the applicant’s sworn statement

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[96] *Colantino v. Don Park LP et al,* 2013 ONSC 1059 at para. 24

that she did not want to make her sons beneficial owners, the court concluded that a valid trust had been formed and that the writs of seizure and sale did not attach to, or create an interest in the property.

In summary, a beneficial interest in land is exigible to satisfy the beneficial owner's judgment debts. The beneficial interest need not be registered on title to be exigible. However, the debtor's interest must be beneficial; if a debtor holds legal title to the land in trust for another, the interest will not be exigible.

iii) Execution against contingent interests in land

As discussed above, a beneficial interest in land that is vested in possession is exigible. Section 29 of the *Execution Act* confirms that a beneficial interest in land is exigible if it is merely vested in interest:

> …any estate, right, title or interest in land which under section 10 of the *Conveyancing and Law of Property Act*, may be conveyed or assigned by any person, or over which the person has any disposing power that the person may, without the assent of any other person, exercise for the person's benefit, is liable to seizure and sale under execution against such person in like manner and on like conditions as land is by law liable to seizure and sale under execution, and the sheriff selling it may convey and assign it to the purchaser in the same manner and with the same effect as the person might have done.

Lawson v. Lawson[97] examined this provision under the predecessor *Execution Act*.[98] In *Lawson*, the debtor was entitled to a vested one-third interest in the residue of an estate. The court, after reviewing the relevant wording of the *Execution Act* and the *Conveyancing and Law of Property Act*, concluded that "it would appear, therefore, that the defendant's contingent interest in the land which forms part of the estate of the

[97] [1964] 2 OR 321-324 (HCJ).
[98] *Execution Act*, RSO 1960, c.126 section 25(1).

deceased is an asset which is liable to seizure and sale under execution against him and so might be rendered liable for satisfaction of the judgment."

V. Liability of the trustee

As mentioned in the introduction, a trustee faced with notice of garnishment or a writ of execution is in a perilous position.

On the one hand, it is trite to note that if the trustee gives a beneficiary's share of an estate or trust to a person who is not entitled to it, the trustee will be personally liable to the beneficiary.

On the other hand, the trustee's refusal to redirect amounts owing or assets due to a beneficiary to a duly entitled judgment creditor will result in the trustee being personally liable to the judgment creditor. A trustee that does not pay the amount set out in the notice of garnishment or does not serve and file a garnishee's statement is susceptible to an order at the motion of the judgment creditor to personally pay the debt.[99] ***Collins Barrow Leamington LLP v. Tiessen***, discussed above, serves as a cautionary tale to trustees about not taking garnishment proceedings seriously. In that case, the court held that a debtor's RRSP could not be garnished. Despite the fact that the judgment debtor successfully escaped his debts, the court held the garnishee bank (i.e. the financial institution holding the debtor's RRSP) *personally* liable to the creditor. The bank's downfall was its failure to respond to the Notice of Garnishment by serving a proper Garnishee's Statement and instead sending a form letter stating that it would not honour the garnishment. The court reasoned that, had the bank served a Garnishee's Statement

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[99] 60.08(17), *Rules of Civil Procedure*.

with all of the required detail about the nature of its refusal to honour the garnishment, the judgment creditor would have had an opportunity to issue a writ of execution instead, which would have been successful (the judgment debtor had since gone bankrupt and the judgment creditor could no longer take that step).

What should a trustee do in general when faced with garnishment or execution proceedings? In my view, a trustee should begin with due regard for her fiduciary obligations to the beneficiary and take all reasonable steps to ascertain that the enforcement proceeding cannot be avoided and must be honoured.

When served with a notice of garnishment or a writ of execution, the trustee should first check the technical elements of a garnishment notice or writ pursuant to the applicable rules and legislation, including proper notice and service, formalities of the writ or garnishment documents, full and fair disclosure, and whether garnishment or execution is applicable to the beneficiary's interest in the trust or estate.

With respect to garnishment, there must be a debt owing by the estate or trust to the beneficiary. There are several questions to ask:

- Has a distribution of money been allocated but not yet paid to the debtor beneficiary? If so, then the beneficiary's interest is garnishable;
- Has a beneficiary who is *sui juris* (e.g. a beneficiary of a bare trust) demanded a money payment? If so, then the beneficiary's interest is garnishable;

- Has the beneficiary's interest in money vested in possession? If not, it is probably not garnishable. If it is, it is garnishable pursuant to *Ker Estate* (although consider whether that case is correctly decided and should be revisited by the court);
- Is the beneficiary's interest non-pecuniary; i.e. land, goods, etc.? If so, the interest is not garnishable;
- Are the funds held in trust? If so, they are not garnishable.

Any trustee who wishes to dispute a garnishment must, within 10 days after service of the Notice of Garnishment, serve on the creditor and the debtor and file with the court a Garnishee's Statement (Form 60I) setting out the particulars of the dispute.[100]

In the garnishment context, the trustee in its capacity as garnishee (and also the creditor, debtor, co-owner of debt or any other interested person) may bring a motion to the court to determine any matter in relation to a notice of garnishment, including to determine any rights and liabilities, whether the alleged debt has been assigned or encumbered or to vary or suspend periodic payments.[101] As noted above, the court has broad discretion on such a motion.

With respect to execution against a purely pecuniary interest in an estate or trust – whether a legacy, gift of residue, or an interest in capital or income of a trust – there is a lack of judicial authority to give guidance and caution is required.

[100] Rule 60.08(15), *Rules of Civil Procedure*.
[101] Rule 60.08(16), *Rules of Civil Procedure*.

VI. Conclusion

A debtor’s bank accounts, home, wages, or other property and income may be garnished or seized by creditors to satisfy debts. Similarly, a beneficial interest in an estate or trust may fall into the clutches of the beneficiary’s creditors.

Trustees must exercise caution where a third party asserts an interest in the beneficiary’s share. If the trustee ignores the third party creditor’s interest and gives the beneficiary his share directly, she may be personally liable to the creditor. Conversely, if the trustee pays the creditor without taking adequate steps to ascertain the enforceability of the creditor’s claim over the beneficiary’s share, she may be personally liable to the beneficiary.

Arguably, a trustee’s fiduciary duty to beneficiaries extends to taking reasonable and appropriate steps to protect the beneficiary’s interest from falling into the hands of creditors. A trustee must therefore be in a position to evaluate the legitimacy of any claims by third parties to receive all or part of a beneficiary’s interest in an estate and take assert any technical defences to the enforcement of the debt against the estate.

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TAB 6

20TH ANNUAL
Estates and Trusts Summit

Why I Am Going to Sue You

Justin de Vries
Anna Alizadeh
de VRIES LITIGATION LLP

DAY TWO
October 17, 2017

cpd Continuing Professional Development

WHY I AM GOING TO SUE YOU

Justin W. de Vries and Anna Alizadeh[1]

1. INTRODUCTION

In Ontario, lawyers are regulated by the Law Society of Upper Canada (LSUC). The LSUC sets the ethical and professional standards of practice for lawyers across the province. One of the central duties of lawyers is to their clients, including a requirement to protect their clients' interests and to carry out their clients' instructions. In discharging this duty, lawyers must meet the requisite standard of care. If a lawyer falls below the standard of care expected of him or her, he or she may be held liable for negligence.

Lawyers may make any number of errors in making recommendations to a testator about his or her estate plans, drafting the will, or advising the estate trustees. When advising testators, common areas of concern include faulty tax advice, jointly held property passing outside of the estate, improperly funded trusts, and failing to provide for dependants on death. The will itself may contain any number of errors, flowing from a misunderstanding about the testator's intention and instructions or from sloppy drafting practices, such as spelling errors, ambiguous clauses, no gift-over or residue clauses, and numerical mistakes (for example, gifts amounting to more or less than 100% of the estate, or causing confusion by spelling a number (ex. "ten") that does not match the numerical value next to it (ex. "100")).

If the error amounts to negligence, the lawyer may be liable for damages. Determining negligence is fact-specific. However, the general duties and standards of care have been well-defined in the case law.

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2. DUTY OF CARE

A lawyer's primary relationship is to his or her client. As a result, a lawyer's principal obligation is a duty of care to his or her client. This duty arises in contract (under the terms of the retainer agreement) and as a professional duty imposed on all lawyers to act with skill and competence when serving their client.[2] However, in the estates world, a drafting solicitor's obligation often extends beyond his or her client. A drafting solicitor owes a duty of care to:

- the client/testator;
- to the client/testator's intended beneficiaries; and
- to the estate trustee(s) when the solicitor is providing legal services regarding the estate's administration.

The extension of a drafting solicitor's duty of care to the testator's intended beneficiaries was established in Canada in *Whittingham v Crease & Co.*[3] The principle was more recently summarized by the court in *Haljan v Mercer*[4] as follows:

> What is clear from the cases is that a court may grant a remedy to a disappointed beneficiary where the interests of the testator and the disappointed beneficiary are in harmony and there is no possibility of conflict.

As a result, where the testator clearly intended for someone to be a beneficiary of his or her estate and the gift to the intended beneficiary failed due to the act or omission of the solicitor, the "disappointed beneficiary" (i.e. the intended beneficiary) may sue the solicitor in negligence.

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[2] *Central & Eastern Trust Co v Rafuse* (1986), 31 DLR (4th) 481, [1986] 2 SCR 147 (SCC) ("***Central & Eastern Trust Co v Rafuse***"), which held (at para 66) that a solicitor is required to act with reasonable care, skill and knowledge in the performance of his or her services.

[3] *Whittingham v Crease & Co.,* (1978), 88 DLR (3d) 353 (BCSC).

[4] *Haljan v Mercer*, (2004), 11 ETR (3d) 172 (AB QB), at para 8.

However, to date, Canadian courts have declined to extend the duty of care to beneficiaries under a previous will.

Solicitor's Negligence

For a lawyer to be found liable, it must be shown that the lawyer's "error or ignorance was such that an ordinarily competent solicitor would not have made or shown it."[5] The court will look to the following to determine whether a lawyer is liable.

1. The source of the liability for negligence. The liability of a solicitor is a concurrent liability in contract, tort, and equity;[6]
2. Whether the lawyer met the standard of care. The standard of care is not perfection, but rather that of a "reasonably competent solicitor"[7]; and
3. Whether the plaintiff has proven that the misconduct caused the client's loss such that the client suffered damages.[8]

Sources of Liability for Negligence

As stated above, the liability of a solicitor is a concurrent liability in contract, tort, and equity. The source of the contractual liability comes from the retainer agreement between a lawyer and client.[9] Erroneous or improper legal advice also gives rise to a claim of negligence. Finally, a conflict of interest or failure to disclose a material fact will give rise to a claim for breach of fiduciary duty.[10]

In *Pilotte*, Justice Chapnik held:

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[5] *Pilotte v Gilbert, Wright & Kirby, Barristers & Solicitors*, 2016 ONSC 494, at para 34 ("***Pilotte***").
[6] *Pilotte*, at para 29.
[7] *Pilotte*, at para 32.
[8] *Pilotte*, at para 46.
[9] *Pilotte,* at para 29.
[10] *Pilotte*, at para 31.

> A negligent misrepresentation or omission to convey information by a solicitor to a client may give rise to a cause of action for breach of contract, negligence, or for the breach of a fiduciary duty. The misrepresentation or omission must, however, be shown to be material in the sense that it would have been likely to have influenced the client's conduct or operated on the client's judgment.[11]

Examples of misrepresentations or omissions that may lead to findings of liability include improper tax advice, failing to explain the consequences of holding property as joint tenants, or failing to advise a testator of his or her obligation to provide for his or her dependants on death.

3. STANDARD OF CARE

In *Pilotte*, Justice Chapnik described a lawyer's standard of care as follows:

> A solicitor is required to bring reasonable care, skill and knowledge to the performance of the professional service which he has undertaken ... The requisite standard of care has been variously referred to as that of the reasonably competent solicitor, the ordinary competent solicitor and the ordinary prudent solicitor.[12]

When it comes to the standard of care for lawyers advising an estate trustee, the court in *McCullough v Riffert*[13] held:

> At the outset estate practitioners should recognize that by accepting employment to render legal advice or other such services, they impliedly agree to use such skill, prudence and diligence as lawyers of ordinary skill and capacity commonly possessed and exercise in the performance of the tasks they undertake. If they fail to meet the standards of fellow practitioners in the same area of law, they may be held liable.[14]

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[11] *Pilotte,* at para 31.
[12] *Pilotte,* at para 32, citing to *Ristimakin v Cooper* (2006), 79 OR (3d) 648 (ONCA) and *Central & Eastern Trust Co v Rafuse*.
[13] *McCullough v Riffert,* 2010 ONSC 3891, at para 46 ("***McCullough***").
[14] *McCullough*, at para 46, citing to Ian Hull's paper presented at the Law Society's 2009 Continuing Education Program Annual Estates and Trust summit.

In British Columbia, the responsibility of a lawyer to the estate trustee is explained as follows:

> Lawyers practicing in the area of wills, trusts and estate administration should have a full understanding of the substantive law relating to the duties, responsibilities and potential liability of the personal representative (that is, the administrator, executor and/or trustee); this is necessary for the lawyer to be in a position to recognize those "out of the ordinary" issues and, in turn, to be able to provide appropriate advice to their clients.[15]

Justice Riley in *Millican v Tiffin Holdings Ltd.*[16] described what it means to be "skilful and careful" lawyer as follows:[17]

1. To advise her client on all matters relevant to her retainer, so far as may be reasonably necessary;
2. To protect the interests of her client;
3. To carry out his instructions by all proper means;
4. To consult with her client on all questions of doubt which do not fall within the express or implied discretion left to her; and
5. To keep her client informed to such an extent as may be reasonably necessary, according to the same criteria.

In *Pilotte*, the court noted the factors relevant to determining the standard of care. These include but are not limited to:[18]

1. Knowledge of the law: a prudent solicitor must have sufficient knowledge of the basic principles of the law.[19] To meet the standard of care, the lawyer must have "a combination of good working knowledge of the relevant law and further research, as necessary";[20]
2. Circumstances that affect the standard of care and corresponding liability;

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[15] Kim A. Karras of Brawn Karras & Sanderson, *Continuing Legal Education Society of British Columbia*, Professional Conflicts - Advising Personal Representative on their Duties and Interests as Beneficiaries.
[16] *Millican v Tiffin Holdings Ltd* (1964), 49 DLR (2d) 216 (Alta TD), confirmed (1967), 60 DLR (2d) 469 (SCC).
[17] *Pilotte*, at paras 36-37.
[18] *Pilotte*.
[19] *Pilotte*, at para 36, citing to *Central & Eastern Trust Co v Rafuse*.
[20] *Pilotte*, at para 37.

3. If the lawyer is an expert or specialist; and
4. Customary practice.

Therefore, the question addressed by a court is whether a lawyer was negligent and not whether the lawyer made an error. Errors happen. The lawyer will only be held liable if the error amounted to negligence.

To establish that a solicitor has been negligent, it must be shown that a reasonably competent lawyer, practicing at the time and place in question, would not have made the same error.[21]

Causation

It is not enough for a plaintiff to prove that his or her lawyer breached their duty of care. To establish a lawyer's negligence, the plaintiff must also prove that the lawyer's misconduct resulted in a loss to the client and that the client suffered damages.

In *Pilotte,* the Court held: "The general test for causation is the 'but for' test on a balance of probabilities. The plaintiff must show that the injury would not have occurred "but for" the negligence of the lawyer."[22] Specifically, in an action for solicitor's negligence, the plaintiff must demonstrate that if properly advised, he or she would have acted in a different manner and would have avoided the damages suffered.[23]

In *Folland v Reardon*, Justice Doherty held:

> "But for" factual causation has been employed in solicitor's negligence cases, particularly those where the plaintiff contends that he received negligent advice and would have acted differently had he received appropriate advice. In those cases, the plaintiff must show on the balance of probabilities that if properly

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[21] *285614 Alberta Ltd. v Burnett Duckworth & Palmer* (1993), 139 AR 31 at para 36.
[22] *Pilotte,* at para 46.
[23] *Pilotte*, at para 47.

> advised, he would have proceeded in a manner that avoided the damages suffered or obtained the benefit lost as a result of the negligent advice.[24]

4. WHEN CAN LIABILITY ARISE?

The obvious question is: can damages arise before the testator's death? If the error in the will or the solicitor's negligence advice is discovered before the testator passes away, the testator can revoke his prior will and execute a new one. More often then not, however, the mistake is discovered after the testator has lost the capacity to execute a new will or after the testator's death (when the will takes effect). In those cases, disappointed beneficiaries may sue the drafting solicitor for their loss.

The disappointed beneficiaries may commence a claim to rectify a will where a drafting solicitor failed to ensure that the testator's wishes were accurately reflected in his/her will. The disappointed beneficiaries may also seek to overturn the will, for example where the drafting solicitor failed to confirm that the testator had the requisite capacity and was not subject to undue influence. In both cases, the disappointed beneficiaries may seek to recover their legal fees from the drafting solicitor and/or damages for their lost inheritance.

In determining whether the solicitor's actions fell below the standard of care, the court will consider:

- Lack of detailed notes;
- Failure to include a residue clause or including multiple residue clauses;
- Errors in division of parts in the residue clause (ex., gifting 60% of the residue to A and 50% of the residue to B);

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[24] *Folland v Reardon*, 2005 CanLII 1403 at para 61, 74 OR (3d) 688 (ONCA), cited in *Pilotte* at para 48.

- Failure to include a specific bequest, contrary to the testator's instructions;
- Incorrectly naming beneficiaries (ex., charities);
- Permitting beneficiaries to witness the will;
- Failing to determine whether the client has the requisite testamentary capacity to execute a will;
- Failing to interview the client in depth to ascertain the nature of his or her assets (ex. jointly held property or beneficiary designations) and relationships (ex. dependant children or spouses);
- Failure to complete a will in a timely manner;
- Failure to detect and investigate suspicious circumstances;
- Allowing family members or interested parties to attend client meetings;
- Using ambiguous terms in a will that require interpretation;
- Taking instructions from an individual who is not the testator; and
- Failing to confirm instructions with the client.

Set out below are some of the most common reasons why solicitors are sued and wills are overturned or rectified:

A. *Failing to complete a will in a timely manner*

Intended (disappointed) beneficiaries may have a cause of action against the drafting solicitor if a testator dies before his or her will is completed and executed.[25] If a testator is (i) in poor health; (ii) elderly; or (iii) making significant changes to his or her will, the solicitor has a higher duty to complete the will quickly and should prioritize the completion of the will.[26] In these circumstances, Brian Schnurr[27] suggests:[28]

> … the solicitor should give serious consideration to the immediate preparation of an abbreviated "temporary" will (whether typed or handwritten) setting out the essence of the testator's intentions. Another approach would be to dictate a form of holograph will for the testator to create immediately. In this way the testator's intentions would be immediately in force while the solicitor attends to the drafting and subsequent revision of the "formal" will or other components from the testator.

Unreasonable delay in preparing a will is a question of fact.[29] Six factors are considered when determining whether a solicitor has acted reasonably in preparing wills:[30]

1. the terms of the lawyer's retainer (for example whether a precise timetable is agreed upon);
2. whether there was any delay caused by the client;
3. the importance of the will to the testator;
4. the complexity of the job (for example the more complex the will the more time required);
5. the circumstances indicating the risk of death or onset of incapacity in the testator; and

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[25] Schnurr, B., *Estate Litigation*, 2d ed (Carswell), Solicitors' Negligence in Estates 21.3(b) ("**Solicitors' Negligence in Estates**").
[26] Solicitors' Negligence in Estates 21.3(b).
[27] Brian Schnurr is a partner with Schnurr Kirsh Oelbaum Tator LLP, and author of Estate Litigation.
[28] Solicitors' Negligence in Estates 21.3(b).
[29] *Rosenberg Estate v Black*, 2001 OJ No 5051, 2001 CarswellOnt 4504 (ONSC) ("***Rosenberg***").
[30] *Rosenberg* at para 42, and *McCullough v Riffert* at para 50.

6. whether there has been a reasonable ordering of the lawyer's priorities.[31]

B. Improper execution or drafting of a will

A will (other than a will of a member of military forces on active service[32] or a holograph will[33]) is not valid unless it is in writing and:[34]

1. at its end it is signed by the testator or by some other person in his or her presence and by his or her direction;
2. the testator makes or acknowledges the signature in the presence of two or more attesting witnesses present at the same time; and
3. two or more of the attesting witnesses subscribe the will in the presence of the testator.

Unlike other jurisdictions in Canada, Ontario requires strict compliance to the formalities of executing a will. Failure to meet these requirements renders the entire will invalid. However, courts can rectify drafting errors contained within a validly executed will in certain circumstances.

Common types of drafting and clerical errors include:

- mirror wills: when the spouses intend to leave everything to each other on death, but one spouse's will actually leaves everything to him or herself;

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[31] *Rosenberg*, at para 42.
[32] *Succession Law Reform Act*, RSO 1990, c S 26 ("***Succession Law Reform Act***"), s 5.
[33] A testator may make a valid will wholly by his or her own handwriting and signature, without formality, and without the presence, attestation or signature of a witness: *Succession Law Reform Act*, s 6.
[34] *Succession Law Reform Act*, ss 3 and 4.

- spelling mistakes;
- errors in names;[35]
- errors in the number of parts in the division of the residue; and
- the absence of a residue clause.

In some cases, the court can rectify the error. The court in *Robinson Estate v Robinson*[36] described the situations in which an error may be rectified as follows:[37]

> Where there is no ambiguity on the face of the will and the testator has reviewed and approved the wording, courts will rectify the will and correct unintended errors in three situations: (i) there is an accidental slip or omission because of a typographical or clerical error; (ii) the testator's instructions have been misunderstood; or (iii) the testator's instructions have not been carried out by the drafting solicitor.

C. Will challenges

Any individual who has a financial interest in a deceased person's estate may challenge the validity of a will if he or she believes that the contents of the will do not represent the true wishes of the testator or that the testator was incapable of signing the will.

There is a presumption in law that the testator had the requisite testamentary capacity to execute his or her will if the will was executed with the mandatory formalities (i.e. the testator signed the document at the end and his or her signature was witnessed by two people). Testamentary capacity is assessed at the time the testator gives instructions for his or her will.

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[35] Errors in names of charities, for example, can result in a charity not receiving its bequest. When drafting a will with a charitable beneficiary, the solicitor should review the Canada Donor's Guide or the Canada Revenue Agency website to confirm the existence of a charity and the proper spelling of its name.

[36] *Robinson Estate v Robinson*, 2010 ONSC 3484 (affirmed by the Ontario Court of Appeal in 2011 ONCA 493) ("***Robison Estate v Robinson***").

[37] *Robinson Estate v Robinson*, at para 24.

However, the presumption of capacity can be rebutted if it can be shown that, on a balance of probabilities, there were "suspicious circumstances" leading to the execution of the will.

Suspicious circumstances include any fact or event that calls into question whether the testator had the mental capacity to sign a new will or that the free will of the testator was overcome by undue influence or fraud. Of particular importance are events that occurred around the preparation and signing of the challenged will. While the existence of suspicious circumstances do not in and of themselves invalidate a will, they are used to rebut the presumption that the will is valid and require an investigation into the validity of a will.

There are four main grounds on which to challenge the validity of a will:

1. Lack of testamentary capacity (i.e. the testator lacked the mental capacity to create a new will);
2. Undue influence (i.e. the testator was coerced into signing a testamentary document against his or her will[38]);
3. Lack of knowledge and approval of the contents of the will; and
4. Fraud (i.e. the will is a forgery or obtained by deceit).

The most common grounds for a will challenge are lack of testamentary capacity and undue influence.

Testamentary Capacity

The English case of *Banks v Goodfellow,*[39] which has been adopted in Ontario, sets out the criteria that must be satisfied for a testator to have the capacity to make a will.[40]

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[38] Solicitors' Negligence in Estates 21.3(d).
[39] *Banks v Goodfellow* (1870), LR 5 QB 549 (QB) ("***Banks v Goodfellow***").
[40] *Banks v Goodfellow*.

1. the testator shall understand the nature of the Act and its effects;

2. the testator shall understand the extent of the property of which he is disposing;

3. the testator shall be able to comprehend and appreciate the claims to which he ought to give effect; and, with a view to the latter object;

4. that no disorder of the mind shall poison his affections, pervert his sense of right, or prevent the exercise of his natural faculties – that no insane delusion shall influence his will in disposing of his property and bring about a disposal of it which, if the mind had been sound, would not have been made.

When a solicitor is concerned about a client's testamentary capacity, the solicitor should prepare the will, but obtain independent evidence regarding the testator's testamentary capacity. The solicitor should also document his or her concerns and the steps he or she took to investigate and address the concerns. If a solicitor fails to investigate his or her concerns or a client's capacity in circumstances where the solicitor should have been alarmed, the solicitor will likely be in breach of his or her duty of care.

If a testator's capacity is in question, he or she should be referred to a professional who conducts a thorough assessment to determine whether the person is capable of making a will pursuant to the criteria set out above. This may involve multiple meetings with the testator to review his or her assets and various tests to determine his or her cognitive abilities.

Undue Influence

A will that is the result of undue influence is invalid. Of first note, undue influence in the testamentary context is different than undue influence as it applies to *inter vivos* gifts. In the context of estate law in Ontario, there is no presumption of undue influence; the party advancing undue influence has the burden of proving it in every circumstance.

An often-cited definition of undue influence was established in *Banton v Banton*:[41]

> A testamentary disposition will not be set aside on the ground of undue influence unless it is established on the balance of probabilities that the influence imposed by some other person on the deceased was so great and overpowering that the document reflects the will of the former and not that of the deceased. In such a case, it does not represent the testamentary wishes of the testator and is no more effective than if he or she simply delegated his will-making power to another person.

Coercion remains the most important factor in proving undue influence. Persuasion, begging, and bargaining may all be legitimate means of convincing a testator to draft her will in a particular manner as long as the pressure does not amount to coercion.[42] Drawing the line between influence and undue influence is difficult, and the courts have established a high bar.

Despite the seemingly high standard, the courts have long recognized that what amounts to coercion will depend on the circumstances. In *Dansereau Estate v Vallee*[43] the court held:[44]

> We must first consider what the law means when it uses the term "undue influence." It is perhaps easier to begin with or comment about what it does not mean. Undue influence is more than mere persuasion, more than mere inducement, more than misplaced gratitude or pity. On the other hand, undue influence does not need to go so far as actual or threatened physical assaults or confinement. It would be coercion to so press a sick person to such a degree that the person is induced, for quietness sake, to do anything. As summarized in the Osterhoff workbook: "A testator may be led, but not driven."

Determining whether exerting influence over the testator has crossed the line to become undue influence depends on the facts and will change with the circumstances.[45] As a result, there

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[41] *Banton v Banton*, 1998 CanLII 14926 (ONSC), at para 89.
[42] See for example *Re Marsh Estate* (1990), 99 NSR (2d) 221, 270 SPR 221, 1990 CarswellNS 231 (NS Prob Ct), at para 46 ("***Marsh Estate***").
[43] *Dansereau Estate v Vallee*, 247 AR 342, 33 ETR (2d) 71, 1999 CarswellAlta 1337 ("***Dansereau Estate v Vallee***").
[44] *Dansereau Estate v Vallee*, at para 175.
[45] *Marsh Estate*.

is no one definition of undue influence. Justice Macaulay for the court in *Lowery v Falconer*[46] summarized the common law of undue influence as follows:[47]

1. Coercing the testatrix into doing that which she did not desire to do;
2. Imposing an influence so great and overpowering that the will reflects the intention of the person imposing the influence rather than the testamentary wishes of the executrix;
3. Delegating the will-making power of the executrix to another;
4. Showing that the will as drafted is inconsistent with any hypothesis other than its having been obtained by undue influence; and
5. Showing that it is right and expedient to save the testatrix from being victimized.

Below are examples of ‘red flags’ that all drafting solicitors should be on the alert for. Should any of these red flags be present, the drafting solicitor should take care to probe the client’s capacity and independence to make a will and keep careful notes of his or her efforts:[48]

- an elderly testator;
- a testator who has suffered significant ill health, particularly if the condition, the disease or required medication could affect the testator’s mental stability or general mental outlook of the testator;
- a testator who is unwilling to provide the solicitor with full information relating to the assets, liabilities or family condition and circumstances;
- the disposition of the estate is one that would generally be viewed as being unusual in the context of the objective circumstances of the testator;

[46] *Lowery v Falconer*, 2008 BCSC 516 (“***Lowery v Falconer***”).

[47] *Lowery v Falconer*, at para 79.
[48] Solicitors’ Negligence in Estates 21.3(d).

- a beneficiary of the will has been particularly involved in assisting the testator with the preparation of the will; and
- the dispositions set out in the will represent a drastic departure from the terms of the former will.

Further red flags include where a testator "(i) is socially isolated; (ii) has recently experienced family conflict; and (iii) has experienced recent bereavement."[49]

D. Administration of Estates

Solicitors representing estate trustee(s) must keep in mind that they are solicitors for the estate trustee(s) and not the beneficiaries. In these circumstances, a solicitor's duty of care is owed exclusively to the estate trustee and not to the beneficiaries. Therefore, the solicitor cannot provide legal advice with respect to an individual's equalization rights under the *Family Law Act*[50] or dependant support rights pursuant to the *Succession Law Reform Act*.

A solicitor for the estate trustee must also keep in mind that most people have little to zero experience as estate trustee or knowledge of what the role entails. Solicitors must make the duties and responsibilities of estate trustees clear to them. It would be prudent to provide estate trustees with a checklist of their duties and responsibilities at the outset of the retainer.

However, unhappy beneficiaries can sue not only the estate trustee(s) but also the estate trustee's solicitor. Such claims can arise, for example, if the solicitor performs an estate trustee's duties; the estate trustee and the solicitor did not take adequate steps to ascertain the beneficiaries of an estate (whether in accordance with the terms of the will or on intestacy

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[49] *Gironda v Gironda*, 2013 ONSC 4133 at para 77.
[50] *Family Law Act*, RSO 1990, c F 3.

pursuant to sections 44-47 of the *Succession Law Reform Act*); or when a solicitor incorrectly interprets a will.[51]

5. CONCLUSION

The above is a broad and non-exhaustive list of reasons why solicitors may be sued for negligence. Knowledge of common will challenges and solicitor's negligence claims should help you avoid finding yourself in similar situations. However, if you are or have been asked to provide your notes or files relating to a deceased's testamentary documents and/or estate, you should consider contacting LawPro.

Despite the challenges and liability associated with drafting wills and advising estate trustees, take comfort – errors leading to a finding of negligence and damages are fairly uncommon. Most errors can be avoided by keeping good notes, asking many questions, and proof-reading. And remember: these are lessons rarely learned by testators who draft their own wills.

[51] Solicitors' Negligence in Estates 21.3(e).

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TAB 7

20TH ANNUAL
Estates and Trusts Summit

Conflict of Laws Issues for Wills and Estate Administration

Carla Figliomeni
Miller Thomson LLP

DAY TWO
October 17, 2017

cpd Continuing Professional Development

CONFLICT OF LAWS ISSUES FOR WILLS AND ESTATE ADMINISTRATION

CARLA FIGLIOMENI, MILLER THOMSON LLP

CONFLICT OF LAWS ISSUES FOR WILLS AND ESTATE ADMINISTRATION

TABLE OF CONTENTS

Introduction 1
PART I – FUNDAMENTAL PRINCIPLES OF CONFLICT OF LAWS 2
(1) Which court? 2
(2) What law? 3
(i) Domicile 4
(ii) Habitual Residence 5
(iii) Nationality 5
(iv) Situs 5
(v) Other 7
(3) Will a decision be enforced? 7
PART II - WHY DOES CONFLICT OF LAWS MAKE ESTATE PLANNING COMPLICATED? 7
(i) Formal Validity, Revocation and Testamentary Capacity 8
(ii) Interpretation and Construction 9
(iii) Dependants Relief Claims and Forced Heirship 9
(iv) Tax issues 12
(v) Matrimonial Property Regime 13
(vi) Sharia Law 14
(vii) Renvoi 15
PART III - PLANNING AROUND CONFLICT OF LAWS 16
(i) European Union Succession Regulation 17
(ii) Example of The Estate of Maurice Jarre 18
Conclusion 20

CONFLICT OF LAWS ISSUES FOR WILLS AND ESTATE ADMINISTRATION

Carla Figliomeni, Miller Thomson LLP[1]

Introduction

Globalization has heightened the interconnection and integration among people, companies and governments of different nations with international trade and investment fueling such integration. As a result, an increasing number of individuals and families have their business, financial and proprietary interests dispersed over more than one country. For estate planners, this means that an increasing number of clients have connections to multiple jurisdictions. While globalization has made the mobility of people and money between borders more fluid, attempting to implement and administer a cross-border tax and estate plan is significantly less fluid, particularly when such tax and estate plan involves connections to both common law and civil law countries, there is property located in multiple jurisdictions, and each of these jurisdictions has its own set of succession and estate administration laws. Given the diversity of laws applicable in each jurisdiction, an increasing number of clients will face issues based on distinctions between domestic and foreign laws regarding succession. Lawyers practicing estates law should be mindful of the effect of one jurisdiction's laws upon another – that is, lawyers practicing estates law should be mindful of conflict of laws principles.

This paper will outline the conflict of laws issues that arise in testate succession. In particular, the first part of this paper will provide an overview of conflicts of law principles, including which court has jurisdiction to determine succession rights, what law is to apply to succession, and when will a foreign judgment be recognized. The second part of this paper considers issues that are of importance when advising and implementing a multi-jurisdictional estate plan. The issues considered are not an exhaustive list of issues and serve as a checklist of issues that practitioners should be mindful of. The third part of this paper discusses the EU Succession

[1] The author would like to thank Erin Elias and Pritika Deepak, Articling Students at Miller Thomson LLP, for their valuable contributions to this paper.

Regulation No. 650/2012 (the “EUSR”) and provides a summary of a recent Paris Court of Appeal decision dealing with a multi-jurisdictional estate. The discussion regarding the EUSR and the case summary highlight some tools for practitioners to consider when advising clients.

PART I – FUNDAMENTAL PRINCIPLES OF CONFLICT OF LAWS

Conflict of laws deals with the effect of one jurisdiction’s laws on another. In succession planning, conflict of laws principles are used to determine which jurisdictions are applicable where multiple jurisdictions have a connection to an estate. This area of law is particularly relevant where the application of each – or both – jurisdiction’s laws could have conflicting outcomes for beneficiaries. In Ontario, courts rely on the common law conflicts of law rules in order to determine which legal system – or systems govern the succession of the estate.

While conflict of laws is a diverse and expansive area of law requiring knowledge of various domestic succession laws, it focuses on three basic questions:

(1) which court has jurisdiction to determine succession rights?;

(2) what law is to apply to the succession?; and

(3) when will a foreign judgment determining succession be recognized and enforced?[2]

(1) Which court?

States consider different factors when determining which court is the proper venue for estate administration. Succession can be “opened” in civil jurisdictions in the place of last residence of the deceased.[3] Other systems look to where property is located, the place of residence, or the nationality of parties to the litigation.[4] Further, some systems determine the issue differently

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[2] Heather Mountford, *Conflict of Laws in Intestate Succession*, (Toronto: The Law Society of Upper Canada, 2012) at n 1.

[3] Richard Frimston & Michael Wells-Greco, “Conflicts of Law and Private International Law,” in *STEP Advanced Certificate in Cross-Border Estates Course Manual* (CLT International, 2017) at 29.

[4] *Ibid.*

based on whether or not the matter is disputed.[5] In Ontario, our legal system relies on common law principles to decide which jurisdiction's laws govern a cross-border estate.[6] Asserting jurisdiction is the first step in administering a multi-jurisdictional estate. However, it does not determine the applicable law.

(2) What law?

Generally, the principles of conflict of laws provide guidelines to determine whether a court of the forum jurisdiction will apply its law or the laws of one or more interested jurisdictions. Domestic laws diverge considerably when it comes to the regulation, or lack of regulation of testate succession. The application of the appropriate law is decided based on selected factors—such as domicile, situs, or nationality—and regimes—such as testamentary freedom, forced heirship, or regional governance. These key factors and regimes allow a court to see which law will govern the devolution of the deceased's estate.[7]

The traditional ordering process for determining choice of law issues in common law jurisdictions is that the law of the jurisdiction of domicile governs the disposition of "movables" (also referred to as personal property), and the law of the situs governs the disposition of "immovables" (also referred to as real property). Ontario makes this distinction. Civil law jurisdictions, however, often refer to nationality for determining choice of law issues.

In order to clarify the legal frameworks that apply to succession, this paper will first set out the common factors that are predominantly used.

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[5] *Ibid.*

[6] Mountford, *supra* note 2.

[7] Dale Ross, "Habitual Residence, domicile and nationality," in *STEP Advanced Certificate in Cross-Border Estates Course Manual* (CLT International, 2017) at 41.

(i) Domicile

While domicile was historically the most widely used connecting factor, it has been replaced by nationality in many jurisdictions including several European countries.[8] However, domicile remains crucial in the determination of succession law within many commonwealth jurisdictions including Ontario, and relates for the most part, to the place where the deceased had formed an intention to remain permanently. Although the exact meaning of domicile within particular jurisdictions remains context-dependent,[9] an individual can only have one domicile at any given time.[10]

There are three types of domicile: origin, dependency and choice.[11] A person's domicile of origin is often assumed to be their place of birth. However, in common law jurisdictions there is still a distinction between legitimate and illegitimate children. The domicile of legitimate children is based on their father and illegitimate children, their mothers.[12] As children do not have legal capacity to choose their domicile, they have a domicile of dependence. When an adult chooses a new domicile, he or she must abandon their old domicile.[13] Abandoning a domicile has a high threshold and requires an "intentional severance of links with the previous domicile."[14] To acquire a new domicile the individual must both reside in the new place and intend to permanently settle there.[15]

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[8] Ross, *supra* note 7 at 42.
[9] *Ibid*.
[10] *Ibid* at 42.
[11] Mountford, *supra* note 2 at n 7.
[12] Ross, *supra* note 7 at 42.
[13] *Ibid*.
[14] *Ibid*.
[15] Mountford, *supra* note 2 at 13-3.

(ii) Habitual Residence

Residence is commonly deemed to be too transient in nature to be relied upon as a connecting factor.[16] Habitual residence adds more stability to the factor and is the preferred measure for regional authorities such as the European Union with the introduction of the EUSR.[17] It is "a regular physical presence, enduring for some time, and a clearly stronger association than 'ordinary' or 'simple' residence."[18] While habitual residence has more permanency when compared to residence, it does not have the mental intention required to reach a domicile. An individual does not need to intend to remain connected with a particular country in order to habitually reside there.[19]

(iii) Nationality

Many civil law jurisdictions including most of mainland Europe determine the choice of law based on nationality.[20] Nationality is the legal relationship between an individual and an internationally recognized state—as opposed to a regional identity within a state that may accord with a domicile.[21]

(iv) Situs

When a court looks at situs, they are determining the applicable law of succession based on the location of the property as opposed to the other factors which focus on the individual. Before a court applies the factors to determine what law will apply, it is often necessary to characterize the property in the estate as moveable or immovable property as each may be treated differently. Further—within moveable property—a distinction between tangible and intangible property can be made. There may be difficulties as to the definition of movables. In France, for

[16] Ross, *supra* note 7 at 51.

[17] *Ibid* at 48.

[18] DWM Waters, *Explanatory Report to Hague 32*, *the Succession Convention of 20 October 1988*, at clause 51 at 546 as cited in Ibid at 49.

[19] Ibid at 48.

[20] *Ibid* at 42.

[21] *Ibid* at 52.

example, frescos from the 11th century have been found to be movable. And while land or a house will obviously be immovable, it is difficult to classify a timeshare in real property. In addition, in some jurisdictions, a lease of land for less than particular period of years may constitute a movable.[22]

When preparing an estate plan it is important to consider these differences. In addition, it is important to determine whether the jurisdictions involved will treat movables and immovables differently or not. Jurisdictions said to follow a "schismatic" system, like Ontario, treat movables and immovables differently in choosing the applicable law, and situs would determine the law for the immovable property, while moveable property would be determined based on the other factors that focus on the individual. As noted above, many common law jurisdictions make this distinction. The rationale to the schismatic system is that, with respect to real property, it is assumed that the situs jurisdiction has the greatest interest in who holds title to the property and that only a court in that jurisdiction can issue an enforceable decree affecting title. On that rationale, it is likely that a foreign judgment that does not respect the laws of the situs will be denied enforcement by the situs jurisdiction. With respect to personal property, however, the courts are more interested in the intent of the testator in disposing of his or her property. The assumption is that the testator is most familiar with the laws of his or her domicile, that the will has been prepared accordingly, and that the jurisdiction of domicile has the greatest relationship to the testator and the estate with regard to such personal property.

On the other hand, countries that follow a "unitarian" system, will not treat movables and immovables separately or differently. They will insist on treating the whole estate in the same way. Examples include Denmark, Morocco, and most recently with the EU Succession Regulation, the Member States defined therein (if there is no renvoi).[23]

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[22] *Ibid* at 49.
[23] *Ibid* at 50.

(v) Other

The factual circumstances of each case and the law of each jurisdiction will determine which factors are applied. Beyond the use of domicile and situs in common law jurisdictions as well as nationality in civil law jurisdictions, a testator's residence, the physical presence of the individual at the time of writing the will and the explicit choice of legal system within a testamentary instrument can play a significant role. Under Sharia law, for example, the operative factor is religion. In Pakistan, for example, Sharia law may apply to the succession of an estate irrespective of the testator's domicile.[24]

(3) Will a decision be enforced?

Whether or not a decision is enforced in a particular jurisdiction, is the subject of substantial commentary. Generally, a Canadian court will recognize and enforce a foreign judgement if the deceased either:

(a) left immoveable property located in that jurisdiction, or

(b) was domiciled in that jurisdiction before the date of death.[25]

PART II - WHY DOES CONFLICT OF LAWS MAKE ESTATE PLANNING COMPLICATED?

Using conflict of laws principles, jurisdictions may treat assets based in varying countries, differently. Laws may be mismatched as to how jurisdictions distribute property and given the contradictory nature of such laws, cross-border estate planning is complex. Part I of this paper provided an overview of the common factors that form the basis of conflict of laws rules in various jurisdictions. For estate practitioners, the overview in Part I provides the starting point for determining the applicable rules based on the jurisdictions involved and helps determine next steps in a cross-border estate plan or administration.

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[24] Hussain, Abid, *The Islamic Law of Wills and Inheritance*, Huddersfield: Wrentham Consultancy UK, 2015.

[25] Mountford, *supra* note 2 at 13-9.

The purpose of the following discussion is to provide an overview of issues to consider when advising and implementing a multi-jurisdictional estate plan. The following issues provide a non-exhaustive checklist for practitioners that span topics from validity and interpretation matters with respect to drafting to estate administration matters. Being mindful of the following issues can help practitioners to draft and plan accordingly.

(i) Formal Validity, Revocation and Testamentary Capacity

Special considerations with respect to wills need to be thought about because many choice of law issues arise with respect to wills. Starting from the basis that the forum is a common law jurisdiction, questions concerning statutory formalities, revocation, and capacity are decided by the normal application of the laws of the situs or domicile. For example, the situs jurisdiction is under no obligation to give effect to a disposition of real property if the will does not comply with its requirements, even if the will has been executed in accordance with the formalities of the testator's domicile. The same rationale would apply for personal property. While there is no obligation to comply with a will lacking formal validity, many jurisdictions have upheld a will or testamentary instrument if it complies with the requirements of any jurisdiction that is significantly related to the will.[26]

With respect to revocation, the local laws of the situs (with respect to real property) and the local laws of the domicile (with respect to personal property) are applied to the issue of the validity of the revocation of a testamentary instrument, either by physical act or by operation of law. In civil law countries, an intentional act of revocation is generally effective if it complies with the formalities of the place where it occurs.[27]

Similar to the rules with respect to revocation, capacity, of either the testator or the beneficiary, is determined based on the application of the local laws of the situs (with respect to real property) and the local laws of the domicile (with respect to personal property), unless it is clear

[26] Ross, *supra* note 7 at 44.
[27] *Ibid*.

that another jurisdiction has a stronger connection. This is interesting and particularly noteworthy because the situs jurisdiction may impose various restrictions like the inability of non-residents to own real property.

(ii) Interpretation and Construction

Interpretation and construction help the courts determine the meaning and effect of words contained in a will or testamentary instrument. Interpretation is a question of fact, which attempts to discover the actual meaning of the testator by looking at who drafted the instrument, the context and the circumstances. These factors are considered based on the evidentiary rules of the forum.[28] If the intent of the testator cannot be determined, the court will assign a legal meaning in accordance with the rules of construction of the applicable legal system – that is, the law applied to the succession. This can lead to significantly different results. For example, "heirs", "issue", and "spouse" can have very different meanings in different jurisdictions. For estate practitioners, ascertaining the intent of the testator and clearly drafting that intent is paramount in every file, however, when multiple jurisdictions are at play, it is particularly important to draft and define terms in a way that will make the intention clear regardless of which rules of construction may apply.

(iii) Dependants Relief Claims and Forced Heirship

A majority of states, regardless of whether they follow common law or civil law, ensure that a deceased's dependents are provided for under his or her estate.[29] Common law jurisdictions generally provide by statute that certain persons with a specific relationship to the deceased (e.g. children and spouses) may make a support claim against the estate of the deceased if the deceased did not adequately provide for them under the will. Advisors should be mindful of

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[28] *Ibid* at 46.

[29] Richard Frimston, "Introduction," in *STEP Advanced Certificate in Cross-Border Estates Course Manual* (CLT International, 2017) at 1.

these circumstances, as well as which assets, including foreign assets, are exposed to such dependant relief claims.

In most civil law and Islamic law states, forced heirship is an example of such state protection in estate distributions. Contrary to testamentary freedom, which is enjoyed in several common law states, where people are free to entitle or disentitle anyone they wish from their estate, forced heirship restrains a testator's freedom in disposing of his or her assets. It applies regardless of moral or natural claims on the testator. In jurisdictions that follow the forced heirship regime, legal mechanisms decide who the appropriate heirs are and what portion of the deceased's estate is available to be disposed of freely. The disposable portion of their estate depends on the number of heirs the decedent left.

The heirs under a forced heirship regime, occasionally referred to as 'forced heirs' are guaranteed their portion of the estate regardless of dispositions in the testator's will. The 'reserved share' of the deceased's estate is generally distributed to the spouse or the deceased's children, or in some cases, both (ie. Switzerland and France).[30] The method of determining the size and ultimate distribution of the reserved share varies from jurisdiction to jurisdiction and is usually stated as a percentage of the estate.[31]

For example, in France, if there is only one surviving child, that child's reserve share is one-half of the deceased's estate. If there are two children, each child will have a reserved share of one-third, and if there are three children, each child will be entitled to one-quarter of the estate. However, if there are four or more children, the reserved share is capped at 75%, so each child will get a portion accordingly. If the deceased leaves no children but a surviving spouse, the spouse will have a reserved share of 25% of the estate.[32]

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[30] Wells-Greco & Mrazek, *supra* note 3 at 12.

[31] *Ibid*.

[32] *Ibid* at 5-7.

On the other hand, in Germany the inheritance rights of descendants are limited under forced heirship to one-half of the share that the descendants would have received under intestacy rules.[33] In other jurisdictions, when there are inheritance rights granted under forced heirship and inheritance rights given by a Will, the beneficiary may elect between these rights, however the election must be made within a specific time limit.[34]

Generally, in civil law legal systems, forced heirship goes beyond 'death estate', property belonging to the deceased at the time of his or her death. The regime also considers gifts given by the deceased during his or her lifetime which may involve 'clawing-back' assets to satisfy the forced heirship requirements.[35] For example, in Switzerland the rule is that a gift made by the deceased up to five years before his or her death may be pulled back into the estate in the event of a forced heirship claim.[36] In another example, a British national domiciled in England gave away a significant portion of his property forty years before his death in France. However, becoming domiciled in France, the claw-back applied to the gifts he made forty years prior to his death when he resided in England.[37] Claw-backs can be a source of serious complications for clients who have property in jurisdictions that enforce this rule as they may limit the usefulness of tax planning tools.[38]

Estate practitioners should be mindful of these issues when dealing with potential dependent relief claims or with forced heirship regimes. In particular, if dependant's relief claims or forced heirship provisions apply in one jurisdiction and not in others or if the application is of differing proportions, complications may arise as to whether or not one jurisdiction will take into account assets received by beneficiaries in the other jurisdiction. Generally schismatic countries do not take other jurisdictional assets into account, whereas the unitarian countries do.

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[33] *Ibid.*
[34] *Ibid* at 13.
[35] *Ibid* at 14.
[36] *Ibid* at 8.
[37] Ibid at 14
[38] *Ibid.*

As discussed above regarding the interpretation and construction of a will, when jurisdictions define "spouse" differently, there can be an issue as to what laws will govern the determination of whether a spouse is entitled to a dependant's relief claim or a preferential share.

(iv) Tax issues

In an international context, conflict of laws regarding succession often create tax problems derived from disparate laws on general property and succession.[39] Issues arise as inheritance taxes vary: where some tax the estate, others tax the recipient of inheritance.[40] Further, there may be differences that vary by jurisdiction regarding valuation, timing and treatment of property.[41] Once the recipient who may be liable is identified, a range of factors may be used to link the individual to the tax system such as: domicile, habitual residence, or nationality.[42] For example, in the United Kingdom, inheritance tax is imposed based on the deceased's domicile while most civil law countries look to habitual residence. [43] Residence can also be deemed based on citizenship as is the case in the Netherlands. In Sweden, former Swedish residents are deemed to remain residents as long as they maintain relevant personal attachments–such as children–in Sweden. With a spectrum of factors linking individuals to a particular tax system, having property in multiple jurisdictions can lead to double taxation.

Double taxation is a critical issue in the application of international succession laws. Tax can be imposed by the state of residence of the deceased, the state of residence of the recipient, the state of property situs and the state of deemed residence of the deceased or the recipient.[44] Tax treaties may be able to provide some relief, however, there are 33 double tax treaties in the European Union which were developed to control or mitigate the consequences of double

[39] Timothy Lyons QC and Kelly Stricklin-Coutinho, "An Overview of Tax Considerations", in *STEP Advanced Certificate in Cross-Border Estates Course Manual* (CLT International, 2017) at 169.

[40] *Ibid.*

[41] *Ibid* at 170.

[42] *Ibid.*

[43] *Ibid* at 171.

[44] *Ibid* at 175.

taxation and they do not completely avoid it.[45] In addition, while many countries have entered tax treaties addressing estate tax, since Canada does not have an estate tax, death tax, or wealth tax, as referred to in various jurisdictions, there is often little relief for the capital gains tax paid in Canada and the estate tax paid in other jurisdictions.

Another tax issue that estate planners should be wary of is the potential for triggering capital gains tax on death. In Canada, capital gains can be deferred by the deceased if he or she transfers property on death to a spouse, common law partner or spousal (or common law partner) trust on a tax deferred basis.[46] The resulting tax consequence is that tax which would otherwise be payable upon testator's death will be deferred until the spouse, or trust disposes of the asset or is deemed to have disposed of it. Under the forced heirship regime, assets may automatically be distributed to children (who do not qualify for a spousal rollover) thereby triggering an immediate tax consequence. Since conflict of law rules in Canada state that *situs* applies for immovable property, Canadian income tax may be triggered if the property is located in jurisdictions that follow forced heirship and the property is thus distributed.

(v) Matrimonial Property Regime

Matrimonial property regimes often cause problems for practitioners because they are so regularly overlooked. These regimes are important to note because when a spouse is protected by a community of property regime, the estate will have to be wound up in order to determine what property is left. Where a spouse is not protected by a community of property regime, he or she may need protection from forced heirship, or a discretionary claim.[47]

Civil law jurisdictions tend to impose a form of community property over a relatively wide array of property. In contrast, North American jurisdictions reserve special treatment for the matrimonial home and there is a complete lack of marital effect on property in the United

[45] *Ibid* at 176.

[46] Income Tax Act (Canada), R.S.C., 1985, c.1 (5th Supp.), section 70(6).

[47] Michael Wells-Greco, Rebecca Fisher & Alexandra Mackenzie Smith, "Family Law," in *STEP Advanced Certificate in Cross-Border Estates Course Manual* (CLT International, 2017) at 77.

Kingdom.[48] A community of property is further defined by jurisdictional definitions of relevant time, source, and nature of assets. Time considerations can include either all assets owned by each spouse, or only the accrued value of assets over the time of the marriage in the community of property. In some jurisdictions, inheritances are a source of property that is excluded from the community of property if received during the marriage.

In certain jurisdictions, contractual opportunities exist which enable an individual to select which community of property applies. In France, for example, spouses enjoy complete contractual freedom to select whatever combination of community property they wish.[49]

(vi) Sharia Law

Sharia law is the primary source of Islamic Law. It is an abstract form of law based on the Quran and the Sunna, being subject to adaptations and different interpretations.[50] The application of Sharia law varies by jurisdiction, however, generally there are two ways of determining whether Sharia law is applicable or not: the first is to determine if the deceased was a Muslim or not. If the deceased was a Muslim, Sharia principles will mandatorily govern the Muslim's inheritance and succession. The heirs must be Muslim and a substantial number of rules apply to calculate each heir's portion. If the deceased was not a Muslim, Sharia law allows the deceased's estate to be distributed in accordance with the laws of the deceased's country of origin. To that end, the existence of a clear will stating what law should govern is important to have. The second way of determining whether Sharia law applies is to determine the nationality of the deceased. Sharia law of succession may apply if the testator is a national of a country where Sharia law applies automatically (e.g. Kuwait). In some countries (e.g. Lebanon) a choice of law is available.

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[48] *Ibid* at 75.

[49] *Ibid* at 77.

[50] Michael Wells-Greco & Yann Mrazek, "Differences between common law, civil law and sharia law systems (and those that are hyprid)," in *STEP Advanced Certificate in Cross-Border Estates Course Manual* (CLT International, 2017) at 4.

Estate planners must recognize that if Sharia law applies, Sharia law is a form of forced heirship, which can significantly alter the intention of a testator. If we consider a Muslim marriage (between Muslim individuals) there is only one applicable regime (always subject to the Sharia Court's final decision). The Muslim husband's inheritance is ½ of his wife's assets if the couple were childless or ¼ if there are children; and the Muslim wife's inheritance is a ¼ of her husband's estate if there were no children or 1/8 if there are children.

In the event that a Muslim male is married to a non-Muslim woman, the surviving spouse will not inherit any assets from the deceased Muslim spouse. On the other hand, if the Muslim individual leaves a will favouring his non-Muslim spouse, the surviving spouse will be able to receive the assets as described in the will in his or her favour irrespective of the religion, so long as the will provisions do not conflict with other rules under Sharia law and the deceased's assets designated in the will are within the limit of 1/3 of the estate. In addition, heirs must be Muslim, cannot have wilfully caused the death of the deceased, and cannot be illegitimate or adopted children.[51] Under Islamic law, both moveable and immovable property are treated identically.[52] Besides descendants and spouses forced heirs may include parents, grandparents, brothers and sisters, following order for priority.[53]

(vii) Renvoi

Renvoi is a French word meaning "reference back". In a conflict of laws analysis it creates additional uncertainty. Once a court has decided that it has jurisdiction over a particular matter, it must then decide what is to be the applicable law. In this process of deciding the applicable law, the doctrine of renvoi may be invoked. This is because when a court establishes that the laws of another state apply, the question is what is meant by the term "law". That is, whether the term "law" of another state means the internal or domestic law of that state, or the law of that

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[51] *Ibid* at 5.
[52] *Ibid* n 9.
[53] *Ibid* at 7.

state including all or some of the conflict of law rules of that state. If it is the latter, this could mean that the laws of the foreign state would refer the matter back to the state of the forum or to a third state.[54]

By way of example, if an Ontario court determines that the laws of another country should apply, it raises the question of which "laws" are to apply. Is it simply the laws of that country with respect to succession or is it the conflict of law rules of that country with respect to succession? If it is the former, the Ontario court could simply decide on the matter at issue using the laws of the other country. However, if it is the latter, the Ontario court may have to determine if the conflict of laws rules would "refer back" to the laws of Ontario or to the laws of a third country.

Many jurisdictions have included statutory provisions to aid in this decision-making. For example, in Ontario, the *Succession Law Reform Act*[55] includes conflicts of law provisions that avoid the doctrine of renvoi for determining the validity and construction of wills. Under the EUSR, if no valid choice of law provision is made pursuant to Article 22, and if the state of habitual residence is not a Member State, as therein defined, then Article 34 prohibits the acceptance of such renvoi and the applicable law would be the internal domestic law of the state of habitual residence.[56]

PART III - PLANNING AROUND CONFLICT OF LAWS

The issues in Part II of this paper provide a non-exhaustive checklist of matters to be wary of when advising on multi-jurisdictional estate planning. The purpose of this Part III is to highlight some examples of the tools available to estate practitioners. The first such tool that will be discussed is the EUSR. The second is a summary of a case involving the estate of Maurice Jarre. While this case summary is fact-specific, it highlights some planning options.

[54] Richard Frimston, "Renvoi," in *STEP Advanced Certificate in Cross-Border Estates Course Manual* (CLT International, 2017) at 61.

[55] R.S.O. 1990, c. S.26

[56] Frimston, *supra* note 54 at 63.

(i) European Union Succession Regulation

Succession Regulation has changed the landscape of estate law in the European Union as it assumes that one will shall govern the worldwide estate. [57] The purpose of the EUSR is to harmonize legislation, to reduce complications and to ease the administration and judicial burden of international succession. To achieve this objective, Regulation No. 650/2012 was introduced and applies to estates in which the deceased died on or after August 17th, 2015. However, it should be noted that not all European nations are party to this regulation: the United Kingdom, Ireland and Denmark are not bound by the EUSR.[58]

The EUSR was established to counteract several existing problems which include:

> (i) the different conflict of laws rules for succession that were present in each of the EU states;
>
> (ii) the fact that many states held that succession was governed by the law of an individual's nationality regardless of the type of property (moveable or immovable) in question; and
>
> (iii) unclear interpretations of what "law" meant– did it mean a state's internal law or did it include its conflict of laws.[59]

Until the establishment of the EUSR in 2015, there was no agreement amongst the states, thereby rendering court decisions from an outside state invalid.[60] The irreconcilable conflicts between states caused exorbitant estate litigation expenses and prompted the EU's interest in regional law reform in this area of law. [61]

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[57] Frimston, *supra* note 38 at 6.

[58] Wells-Greco & Mrazek, *supra* note 34 at 25.

[59] Frimston, "EU Regulation 650/2012," in *STEP Advanced Certificate in Cross-Border Estates Course Manual* (CLT International, 2017) at 150.

[60] *Ibid.*

[61] *Ibid.*

One of the most important aspects of the EUSR is that in states where the EUSR applies, jurisdiction over an estate is now held by the jurisdiction where the deceased was habitually resident at the time of his or her death.[62] If the deceased's habitual residence is not a Member State, then the hierarchy set out in Article 10 of the Regulation applies to determine which court will have jurisdiction.[63] The EUSR, under article 21 and 23 no longer applies multiple jurisdictional forums for succession thereby deeming that movables and immovables are governed under the same law regardless of situs.[64] This section of the EUSR made the EU a unitarian system.[65]

Additionally, and most advantageous for estate planning purposes, testators under the EUSR, can elect for the law of their nationality to apply to govern their succession. [66] If the deceased made a choice of law option in favour of another Member state, Article 5 of the EUSR states that "parties concerned" (referring only to beneficiaries or heirs, but not creditors) may agree that the other Member state has jurisdiction to govern the estate.[67]

It is important for estate practitioners to consider the impact of the recent regulations to ensure compliance and efficient estate planning for their clients. Clients who own property in a Member State but are nationals of another country may be able to rely on the EUSR to have the law of their nationality apply to the devolution of their property on death. The EUSR is therefore a tool that can be used to plan around forced heirship.

(ii) Example of The Estate of Maurice Jarre

In a recent case, the Paris Court of Appeal made a seminal ruling affecting property owned in France by a foreign domiciliary. On May 2016, the Paris Court of Appeal confirmed a judgment

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62 *Ibid.*
63 *Ibid* at 153
64 Frimston & Wells-Greco, *supra* note 2 at 30.
65 *Ibid.*
66 Frimston, supra note 52 at 154.
67 *Ibid* at 152.

handed down by Paris High Court on Dec 2, 2014 regarding the estate of Maurice Jarre ("Maurice"). This case concerns the governance of a French composer's estate, named Maurice Jarre. He was married four times and had two children from his first two marriages. He moved to California in 1984 and died there in 2009. In 1991, Maurice and his fourth wife, Mrs. Khong, settled the Jarre Family Trust under laws of California and were the sole settlors and trustees of the trust. In 1995, Maurice and Mrs. Khong created a Societe Civile Immobiliere ("SCI") into which they contributed an apartment located in Paris. All the moveable and immoveable assets of Maurice were moved into trust in 2008 according to a Will he executed. In the Will, he explicitly declared that he intentionally and willingly omitted all provisions concerning his heirs, namely his two children.[68]

The main issue in this case was whether the estate of Maurice Jarre could be distributed without being subject to the forced heirship rules of France and whether or not the SCI created was fraudulent. Maurice's two children initially obtained a freezing order for his estate to suspend distributions requested by Mrs. Khong. However, the Paris Court of Appeal confirmed that a US domiciliary who died prior to August 2014 can dispose of his or her French estate (which consisted of movable property) as he or she wishes without being subject to French forced heirship rules. The Paris Court further stated that a US trust is fully recognized by French law even where settlor who is also the trustee and primary beneficiary. Lastly, the Court held that transferring French real estate into a SCI to transform real estate property to moveable assets is not fraudulent. [69]

This case provides an example of how different tools, including trusts and SCIs, can be used to transfer property outside the parameters of forced heirship. Solutions to forced heirship must be fact specific and tailored to the particular mechanisms of the jurisdiction. Stemming from the

[68] Jean-Marc Tirard, "Paris Court of Appeal Rules on Forced Hiership, US Trusts and Legitimacy of Transforming Real Estate into a Moveable Asset using an SCI Structure, *McDermott, Will & Emery* (May 23, 2016) at 1, online: https://www.mwe.com/~/media/files/thought-leadership/publications/2016/05/paris-court-of-appeal-rules-on-forced-heirshipmay2016.pdf

[69] *Ibid*.

principles in the schismatic system that distinguishes between movables and immovables, generally, the consequences of forced heirship can be planned around by owning property located in civil law countries through an intermediary like a corporation, or holding shares in a corporation that holds the immoveable property. Of course such planning is complicated and must be looked at from various aspects - jurisdictions involved, tax consequences (in all jurisdictions involved), claw back rules, etc. to ensure such planning works.

In addition, a limited number of civil law jurisdictions with forced heirship allow for inheritance contracts.[70] These agreements are entered into directly between the person entitled to inherit under forced heirship and the testator while the testator is still alive. Through these agreements, testators and their heirs can agree on a form of future division of the estate other than the one set out in the forced heirship requirements. Germany, France and Italy each allow a form of inheritance contract although Italy's is limited to business assets.[71]

Conclusion

When advising clients with multi-jurisdictional assets in both common law and civil law countries estate practitioners should understand conflict of law rules, domestic and foreign legal systems, tax consequences, client objectives, and testamentary wishes. With awareness of the key factors and the appropriate tools, the jurisdictional, cross-border and enforcement issues can be successfully navigated.

[70] Frimston & Wells-Greco, *supra* note 3 at 36.
[71] *Ibid*.

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TAB 8

20TH ANNUAL
Estates and Trusts Summit

Tax Update

Joan Jung
Minden Gross LLP

DAY TWO
October 17, 2017

TAX UPDATE

Joan E. Jung

Partner, Minden Gross LLP

INDEX

INDEX 1

2017 FEDERAL BUDGET – PRIVATE CORPORATION CONSULTATION 2

Tax on split income – current rules 3

Tax on split income - effect of the July 18, 2017 Draft Legislation 7

Expanded categories of "split income" 8

Who is the "specified individual" subject to TOSI? 8

What is included in income at the top marginal rate pursuant to TOSI? 10

An adult "specified individual" and the reasonableness test 11

Extended application of transmogrification rule 12

The Lifetime Capital Gains Exemption 13

Current rules for minors and trusts 14

Effect of the July 18, 2017 Draft Legislation 15

New Restrictions 15

Election available in 2018 17

The Pipeline and the July 18, 2017 Draft Legislation 19

2017 FEDERAL BUDGET - CORPORATE AND BENEFICIAL OWNERSHIP 20

AMOUNT PAID TO BENEFICIARY IN CONTRAVENTION OF TERMS OF TRUST 20

ISSUING INFORMATION SLIPS FOR DISTRIBUTIONS OF CAPITAL TO A NON-RESIDENT 22

EVOY ESTATE v. THE QUEEN 2016 TCC 263 23

GRIMES v. THE QUEEN 2016 TCC 280 26

CONCLUDING COMMENTS 27

TAX UPDATE

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This paper will summarize Canadian income tax developments of interest to estates and trusts practitioners in 2017. The selection of developments is inherently a matter of judgement and the below selection should not be interpreted as a precis of all "important" income tax matters.

2017 FEDERAL BUDGET – PRIVATE CORPORATION CONSULTATION

In the 2017 Federal Budget, the government announced that it was reviewing tax planning strategies involving private corporations and would release a paper identifying issues and proposed policy responses. Little information was provided in the 2017 Federal Budget other than identification of three areas of apparent concern. The three bullet points from the 2017 Federal Budget are reproduced in full below:[1]

- "Sprinkling income using private corporations, which can reduce income taxes by causing income that would otherwise be realized by an individual facing a high personal income tax rate to instead be realized (e.g., via dividends or capital gains) by family members who are subject to lower personal tax rates (or who may not be taxable at all).
- Holding a passive investment portfolio inside a private corporation, which may be financially advantageous for owners of private corporations compared to otherwise similar investors. This is mainly due to the fact that corporate income tax rates,

[1] See 2017 Budget, caption "Tax Planning using private corporations" available on the Department of Finance website: http://www.budget.gc.ca/2017/docs/download-telecharger/index-en.html . See chapter 4 of the Budget Plan.

which are generally much lower than personal rates, facilitate accumulation of earnings that can be invested in a passive portfolio.

- Converting a private corporation's regular income into capital gains, which can reduce income taxes by taking advantage of the lower tax rates on capital gains. Income is normally paid out of a private corporation in the form of salary or dividends to the principals, who are taxed at the recipient's personal income tax rate (subject to a tax credit for dividends reflecting the corporate tax presumed to have been paid). In contrast, only one-half of capital gains are included in income, resulting in a significantly lower tax rate on income that is converted from dividends to capital gains."

On July 18, 2017, the Minister of Finance announced the launch of 75 day consultation period ending October 2, 2017 by releasing draft legislation relating to income splitting and the conversion of corporate income into capital gains together with a discussion paper on "Holding Passive Investments Inside a Private Corporation".[2] Draft legislative proposals were not released in respect of the latter. The draft legislation is complex and far reaching and have been the subject matter of considerable criticism for the rhetoric of the language of the Minister's letter and accompanying Executive Summary (a distinctly unusual approach for the release of tax legislation). There has been much agitation for extension of the consultation period, but as at the date of writing, no announcement regarding same.

The below will provide some detail regarding the proposals. The discussion paper on "Holding Passive Investments Inside a Private Corporation" will not be discussed below.

Tax on Split Income – Current Rules

The July 18, 2017 draft legislation proposes extremely broad ranging changes to what have been referred to as the "kiddie tax" rules. The existing rules are found in s.120.4 of the Income Tax Act (Canada).[3] To appreciate the extent of the proposed changes, it is instructive to revisit the existing rules.

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[2] The Consultation Document: "Tax Planning Using Private Corporations" and draft legislation may be accessed on the Department of Finance website. See http://www.fin.gc.ca/n17/17-066-eng.asp

[3] R.S.C. 1985, c. 1 (5th Supp.) as amended (the "ITA"). Unless otherwise indicated, all statutory references herein are to the ITA.

The existing rules were introduced in the 1999 budget largely in response to the structures sanctioned by the courts in the cases of *Neuman v. The Queen*[4] and *Ferrel v. The Queen.*[5]

Neuman involved dividend sprinkling shares held by a spouse who was not involved in the business. Canada Revenue Agency was unsuccessful in its assertion that the dividends received by such spouse should be included in the income of the husband on the basis of subsection 56(2), ITA, i.e., as a payment made pursuant to the direction of or with the concurrence of the husband as a benefit that the husband desired to have conferred on the spouse. This had also been litigated by CRA unsuccessfully in *McClurg.v. The Queen.*[6]

In *Ferrel*, a family trust provided management services to a family holding corporation. Father was the settlor and sole trustee of the trust. The beneficiaries of the trust were his children. A management fee was paid by the corporation to the trust which was allocated to beneficiaries who were lower income members of the family. There was a written management services agreement between the corporation and the trust. There was a written agreement between Father in his personal capacity and the Trust where father agreed to manage the services to be provided by the Trust to the corporation. The fee paid by the corporation was presumably deductible by the corporation – there was no evidence that deductibility was challenged on the basis of being unreasonable in amount. The fee was therefore taxable in the hands of the lower income members of the family at their particular marginal rates.

Section 120.4 as currently enacted applies to a minor only and clearly does not apply to a spouse or other adult. The person to whom section 120.4 applies is defined as the "specified individual". The current legislation defines a "specified individual" as an individual under age 17, not a non-resident of Canada and having a parent resident in Canada at any time in the year. As a result, these rules became known colloquially as the "kiddie tax" rules. It should be noted that the "kiddie tax" rules marked a departure from other income splitting rules in the ITA which generally take the form of attribution rules to tax the amount in the hands of the "transferor" or other appropriate individual. Instead, the "kiddie tax" rules tax

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[4] 98 DTC 6297 (SCC).
[5] 97 DTC 1565 (TCC) affd 99 DTC 5111(FCA).
[6] 91 DTC 5001 (SCC).

the amount in the hands of the “specified individual”, i.e., the minor, at the top marginal rate and without any deductions or credits (other than the foreign tax credit and dividend tax credit).

The amount which is subject to tax in the hands of the “specified individual”, i.e., the minor, is defined as “split income”.

Under the current rules, the categories of “split income” are:

- dividends on unlisted shares, i.e., private corporation shares; and
- income from a partnership/trust where the partnership/trust provides services or provides property to:
    - a business carried on by a person related to the specified individual which pays a fee or other amount to the partnership/trust for the provided services or property, or
    - a corporation where a person related to the “specified individual” is a “specified shareholder” of the corporation and the corporation pays a fee or other amount to the partnership/trust for the provided services or property.

Income earned by the trust in the *Ferrel* case and allocated to a minor beneficiary would constitute “split income”. In *Ferrel*, the trust earned fees from management services provided to a family company. Where dividends are declared on private corporation shares (such as those in *Neuman*) and the shares are held by a minor or a trust with minor beneficiaries and allocated to such minor beneficiaries, the dividends would be “split income”. For purposes of the ITA, related person is a defined concept[7] and without delving into the nuances and details of the concept, suffice it to say that grandparent – parent – child are related persons and brothers and sisters are related persons but an aunt/uncle is not related to his/her niece/nephew. A “specified shareholder” is a defined concept[8]. Specified shareholder status basically requires a 10% share ownership threshold although the definition also deems a person to own those shares owned by non-arm’s length persons.

[7] See section 251, ITA.
[8] See subsection 248(1), ITA.

Under the current rules, there is a limited exclusion from "split income", referred to as an "excluded amount". In the following two instances, both relating to inherited private corporation shares, dividends on such inherited shares are an "excluded amount" and therefore not included in "split income":

- private corporation shares are inherited upon the death of a parent.
- private corporation shares are inherited from anyone else, where the individual is in full time attendance at a post-secondary educational institution,

Anti-avoidance rules in subsections 120.4(4) and (5) were added in 2011 to address certain tax planning techniques which attempted to convert what would be dividend income taxed in the hands of a minor to a capital gain. If the rule applies, the entire capital gain realized is treated an ineligible dividend. The typical steps carried out in such planning were as follows:[9]

- A private corporation pays a stock dividend in the form of a high/low shares to a discretionary family trust with minor beneficiaries.
- For income tax purposes, the amount of the dividend is equal to the paid-up capital of the shares received and accordingly, the trust only reports a nominal dividend.
- The trust sells the shares to a non-arm's length person (generally the parent) and realizes a capital gain on the disposition equal to the difference between the redemption value and the adjusted cost base of the shares (the latter being nominal).
- The related person (i.e. the parent) sells the shares to a holding company in return for a promissory note and, essentially, has no taxable income since the acquisition price of the shares from the trust is equal to the amount for which they are sold (i.e. the shares are sold and acquired at the redemption amount of the shares).

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[9] Interested readers are directed to the following cases (pre-dating the introduction of subsections 120.4(4) and (5)) in which the above structure was unsuccessfully challenged by CRA using the General Anti-Avoidance Rule in section 245, ITA. See *Gwartz v. The Queen* 2013 TCC 86 and *McLarty Family Trust v. The Queen* 2012 TCC 80.

- The trust allocates the taxable capital gain to the minor(s) beneficiary, who either pays tax at his/her low marginal tax rate or no tax if he/she can use the lifetime capital gains deduction.
- The private corporation and the holding company may amalgamate, or the private corporation may thereafter redeem the preferred shares thereby providing the holding company with funds to pay the promissory note held by the related person (i.e., parent) who in turns uses such funds to pay the trust.

The rules in subsections 120.4(4) and (5) technically apply where a specified individual would have a taxable capital gain from the disposition of private corporation shares that are transferred directly or indirectly in any manner whatever to a person with whom the specified individual does not deal at arm's length. In the structure described above, the minor is a "specified individual" who is non-arm's length with the parent and the taxable capital gain was realized on a disposition of private corporation shares that were transferred to a person non-arm's length with the "specified individual". The effect of subsections 120.4(4) and (5) is that the capital gain realized by the trust on the sale would be recharacterized as a dividend. Although the policy rationale for the introduction of these rules may have been the structures outlined above, the wording of subsections 120.4(4) and (5) have broader reach. Because of the mere requirement for taxable capital gain of a "specified individual" resulting from a non-arm's length transfer of private corporation shares, current subsections 120.4(4) and (5) also catch most internal crystallizations and the case where a related family member buys shares from a family trust. Current subsections 120.4(4) and (5) are sometimes referred to as transmogrification rules because of their recharacterization effect.

Tax on Split Income - Effect of the July 18, 2017 Draft Legislation

The July 18, 2017 proposals are proposed to apply as of January 1 2018. Therefore, the existing rules will apply for the balance of this year, 2017.

In a nutshell, section 120.4 as proposed to be amended can no longer properly be referred to as a "kiddie tax". Rather, the draft amendments can apply to adults as well as minors. As a

result, the acronym TOSI (Tax on Split Income) is now used in reference to section 120.4 as proposed to be amended rather than "kiddie tax".

What has caused much consternation is the proposed introduction of a reasonableness test applicable in certain circumstances. There has always been a reasonableness test in section 67, ITA which limits the deductibility of an outlay or expense (e.g. a salary) to an amount which is reasonable in the circumstances. Section 67 will continue to apply to items such as salary to family members. Salary or bonuses paid to family members, including minors, will not be subject to the revised TOSI rules. As has always been the case, the question of whether an amount of salary or bonus is properly deductible in computing the income of the payer entity (whether a corporation, partnership or sole proprietorship) will depend on whether the amount is reasonable in the circumstances. As described below, the proposed reasonableness test must be considered where an adult is a "specified individual" to determine whether TOSI may apply to certain income.

Expanded categories of "split income"

The categories or types of income which constitute "split income" as described above with reference to the current rules will continue but have been expanded to include the following:

- interest or other income on debt obligations;
- capital gains or other income from the disposition of property (if income from the property would otherwise be "split income"); and
- second generation income or secondary income, i.e., income earned on income which is "split income".

Who is the "specified individual" subject to TOSI?

For a minor, the "specified individual" test is the essentially unchanged except that the Canadian residency requirement is tested at the end of the year.

Under the July 18, 2017 draft legislation, an adult can be the "specified individual" and therefore potentially subject to TOSI but there is a requirement in the definition of "specified individual" which embeds a certain level of connectivity to the business which is the source of income. This contrasts with the case of a minor who is a "specified

individual" where there is no similar requirement. An adult who is resident in Canada at the end of the year is a "specified individual" if:

- The adult's income for the year includes income from property, a taxable capital gain or other income from the disposition of property, a shareholder benefit pursuant to section 15, ITA or a more broad based benefit pursuant to section 246, ITA.
- The foregoing amounts "can reasonably be considered" to be "derived, directly or indirectly from a business".
- With reference to the particular year or any previous year, the business is carried on by:
    - Another individual resident in Canada who is related to the adult. Under the proposed amendments, the related person definition has been specifically expanded so that an aunt or uncle is related to his/her niece or nephew.[10]
    - A corporation of which such other individual is a "specified shareholder" or in respect of which the other individual is a "connected individual". The concept of "specified shareholder" was discussed above, generally meaning a minimum 10% shareholder including for this purpose, shares owned by non-arm's length persons. "Connected individual" is a new concept[11] which among other things, will capture:
        - A corporation which is not legally controlled but rather factually controlled by the other individual or a related group of which the other individual is a member. It should be noted that for purposes of the ITA, there is a body of jurisprudence regarding the concept of *de facto* control.
        - The other individual owns shares of or property which derives, directly or indirectly, all or part of its value from the shares of a corporation

[10] See draft subsection 120.4(1.1). All references herein to "draft" sections refer to the draft legislation released by the Department of Finance on July 18, 2017.
[11] See definition in draft subsection 120.4(1).

which carries on a business of providing services where the services are primarily provided by the other individual in question.

It is not surprising that there should be some connectivity requirement between an adult and the business which is the source of income as a prerequisite to finding the adult to be a "specified individual". This effectively operates as a threshold level of influence of the adult over the business before TOSI becomes an issue.

By way of example, suppose a trust for the benefit of a minor (with a Canadian resident parent) holds 1% of the common shares of a private corporation. The minor is a "specified individual" and dividends paid on such shares would be split income. If an adult holds 1% of the common shares of a private corporation, the adult is not automatically a "specified person". Rather, further investigation is necessary including whether non-arm's length persons resident in Canada own shares which when aggregated with the adult's 1% ownership will exceed 10%; or whether a related individual has an interest in the entity from whose business a dividend on the adult's 1% share ownership derives.

What is included in income at the top marginal rate pursuant to TOSI?

In the case of a "specified individual" who is a minor, any amount received as "split income" is caught by TOSI and taxed at the top marginal rate. Therefore, dividends on any private corporation shares (whether held directly or by means of a discretionary trust but allocated to a minor beneficiary) are included in income and taxed at the top marginal rate pursuant to TOSI. There is no requirement that the minor's parent control the private corporation or even be a "specified shareholder", i.e., having a minimum 10% share ownership.

In the case of a "specified individual" who is an adult, not all "split income" is included in the adult's income under TOSI. Rather, it is only the "split portion" of "split income" which is included in the adult's income under TOSI. If the amount is excluded from the "split portion" of "split income", then the usual rules of the ITA apply to determine the manner in which the amount is taxed (rather than included at the top marginal rate).

It should be noted that if the income of the "specified individual" is already at the level where the top marginal rate applies, then "split income" is deemed to be NIL.

An adult “specified individual” and the reasonableness test

In the case of a “specified individual” who is a minor, TOSI essentially operates as it did prior to July 18, 2017.

In the case of a “specified individual” who is an adult, a reasonableness test applies to determine whether an amount is a “split portion”. This is important because, as mentioned above, where the “specified individual” is over age 17, only the “split portion” of “split income” is subject to TOSI. The reasonableness test asks if the particular amount exceeds what would have been paid or payable by an entity operating at arm’s length with the adult “specified individual” having regard to functionality, contribution, risk and prior payment as set out below:[12]

(A) The functions relating to the business performed by the individual;

(B) The assets contributed, directly or indirectly, by the individual in support of the business;

(C) The risks assumed by the individual in support of the business; and

(D) The total of all amounts paid to the individual in respect of the business.

Where the “specified individual” is less than age 24, the reasonableness tests are modified and become more onerous.[13]

- Part time service will not suffice. For purposes of the measurement of functions performed in respect of the business, the 18-24 year old must be actively engaged on a regular continuous and substantial basis in the activities of the business in order to be considered to have performed any functions.
- To measure the value of property contributed or risks assumed, a prescribed rate calculation is imposed, i.e., the value of the property contributed or risks assumed is

[12] See draft subparagraph (b)(iii) of the definition of “split portion” in subsection 120.4(1).

[13] See draft subparagraph 120.4(1.1)(e)(iii).

multiplied by the prescribed rate (presently 1%, although this rate can change each calendar quarter).[14]

In addition, there are deeming rules which:

- deem no functions performed in respect of the business if the business is what might loosely be described as an investment business;[15] and
- deem no contribution of property to have been made if the property was transferred in connection with a related person providing financial assistance to the specified individual.[16]

Where property is inherited, there is effectively deemed continuity of functions performed, assets contributed, risks assumed and amounts paid – continuing from the deceased person to the person inheriting.[17]

Extended Application of Transmogrification Rule

Earlier in this paper, there was discussion of an anti-avoidance rule in current subsections 120.4(4) and (5) which were likely introduced to respond to structures which attempted to convert an amount which would otherwise be dividend income in the hands of a minor to a capital gain. Current subsections 120.4(4) and (5) recharacterize or transmogrify the amount to a capital gain for income tax purposes. The draft amendments to subsections 120.4(4) and (5) retain the essential elements of the current provisions as follows:

- A "specified individual" has a taxable capital gain from the disposition of private corporation shares.
- The shares are transferred, directly or indirectly, in any manner whatever, to a person with whom the "specified individual" does not deal at arm's length.

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[14] See Regulation 4301(c) which is generally benchmarked against 90 day Government of Canada treasury bills for the first month of the preceding calendar quarter.
[15] See draft clause 120.4(1.1)e)(ii)(A) applicable where the "principal purpose" of the business is to earn income from property (such as interest, dividends, rents or royalties), or if more than 50% of the income of the entity for the year is income from property or taxable capital gains from the disposition of property.
[16] See draft clause 120.4(1.1)(e)(ii)(B).
[17] See draft clause 120.4(1.1)(e)(ii)(C).

However, because a "specified individual" is no longer limited to a minor, subsection 120.4(4) and (5) have far reaching implications.

Inter vivos intergenerational sales of shares of a private corporation from parent to child may be caught by draft subsection 120.4(4), resulting in all or some portion of the capital gain otherwise realized on the sale by parent being transmogrified to a dividend. It is also irrelevant that the transaction may occur at fair market value with full consideration passing.

Draft subsection 120.4(4) may also have consequences upon death where there is, for income tax purposes, a deemed disposition of capital property immediately before death. Pursuant to subsection 70(5), ITA, a taxpayer is deemed to dispose of capital property immediately before death for proceeds of disposition equal to fair market value and any person who as a consequence of the taxpayer's death acquires any property is deemed to acquire it at the time of death as a cost equal to the fair market value immediately before death. An individual and his/her estate are generally considered by CRA to be non-arm's length.[18] Thus, it would appear that a deemed disposition of shares of a private corporation immediately upon death may be subject to draft subsection 120.4(4) thereby transmogrifying all or some portion of the capital gain into a dividend.

The above situations and others have been the subject of discussion and submissions to the Department of Finance. Interested readers are directed to the comprehensive submissions made by STEP Canada and by the Joint Committee on Taxation of The Canadian Bar Association and Chartered Professional Accountants of Canada.[19]

The Lifetime Capital Gains Exemption

The July 18, 2017 draft legislation contain proposals applicable to dispositions after 2017 that will restrict the use of the lifetime capital gains exemption ("LCGE"). This will affect the use of the LCGE by minors and where a trust (other than an "eligible LCGE trust" as defined in the draft legislation) disposes of or has held "qualified farm or fishing property" or "qualified small business corporation shares". The latter are defined terms in the ITA.

[18] See Income Tax Folio S1-F5-C1, "Related Persons and Dealing at Arm's Length", paragraph 1.52.
[19] For the submission by STEP Canada, see the October 3, 2017 press release by STEP Canada at http://www.step.ca/pressRoom.aspx . Submissions also available from the Thomson Reuters subscription service TaxnetPro.

The definitions are detailed and it is beyond the scope of this paper to delve into the definitional requirements. It should be noted however, that it cannot be assumed that shares of a private corporation are necessarily "qualified small business corporation shares" so as to qualify for the LCGE under current legislation and without regard to the July 18, 2017 draft legislation.

Current rules for minors and trusts

At present, minors may claim the benefit of the lifetime capital gains exemption ("LCGE"). Often, this may arise in a corporate structure where a discretionary *inter vivos* trust holds the common shares of a corporation. A trust which is resident in Canada throughout the year and which realizes a capital gain may flow through the character of such income to a beneficiary.[20] Provided that such common shares satisfy the definition of "qualified small business corporation share" in the ITA, the resultant taxable capital gain from a sale of such shares may be allocated by the trust to beneficiaries in accordance with the terms of the trust and designated in its return pursuant to subsections 104(21) and (21.2) of the ITA. The result is that the particular beneficiary is deemed to have an eligible capital gain from the disposition of capital property that is a "qualified farm or fishing property" or "qualified small business corporation shares", as the case may be. In other words, although the trust disposed of such property, the foregoing mechanism permits a beneficiary to include the taxable capital gain in his/her income and because he/she is deemed to dispose of the "qualified farm or fishing property" or "qualified small business corporation shares" which was disposed of by the trust, the individual beneficiary may claim the benefit of the LCGE.

Current restrictions and/or requirements to the flow through of a capital gain realized by a trust pursuant to subsection 104(21), ITA are:

- The trust must be resident in Canada throughout the particular year.
- The particular beneficiary must be resident in Canada in the particular year.
- Because it is necessary that the amount may reasonably be considered to be part of the amount which is included in income of the particular beneficiary (having regarding to all the circumstances including the terms and conditions of the trust),

[20] See subsection 104(21). The trust must designate the amount in its return of income.

the amount must be "payable" to the beneficiary within the meaning of subsection 104(24), ITA. This means that the amount (being the taxable capital gain) is payable either to an income beneficiary or capital beneficiary depending on the terms and conditions of the trust and in particular the definition of income therein.[21]

Effect of the July 18, 2017 Draft Legislation

<u>New Restrictions</u>

The following will apply to dispositions after 2017.

- A person who has not attained age 17 before the beginning of the year may not claim the LCGE.[22] This means that in the calendar year in which the individual attains age 18, he/she may claim the LCGE.

- A capital gain will be notionally reduced by the portion of the appreciation in value of the property which accrued up to January 1 of the year in which the individual attains age 18.[23] This means that appreciation in value of property while held by a minor will not be eligible for the LCGE.

- In the case of property held by an *inter vivos* trust, tax planning often permits the property to be transferred or distributed to a beneficiary without triggering income tax to the trust. This is sometimes referred to as a "roll-out" pursuant to subsection 107(2), ITA. Where this subsection applies, the trust is deemed to dispose of the distributed property at cost and the beneficiary is deemed to acquire at same.[24] In the case of a property distributed by a trust other than an "eligible LCGE trust" after 2017, the capital gain will be reduced by the amount of accrued gain to the date of the subsection 107(2) "roll-out".[25] In other words, the appreciation in value while

[21] See Joan E. Jung, "Income and Payment: Key Trust and Income Tax Differences", Estates Trusts & Pensions Journal, Vol. 36, No. 4, p.350.
[22] See draft paragraph 110.6(12)(a.
[23] See draft paragraph 110.6(12)(c).
[24] This assumes that the beneficiary is resident in Canada and further, that the so-called reversionary trust rule in subsection 75(2), ITA never applied to the trust.
[25] See draft paragraph 110.6(12)(e).

the property is held in a trust (other than an "eligible LCGE trust") will not be eligible for the LCGE.

- If the individual has attained age 17 before the year of disposition, and the capital gain would be included in the individual's "split income", then the capital gain is not eligible for the LCGE.[26]

Where property is held by a trust and disposed of by the trust which realizes a capital gain, the July 18, 2017 draft legislation proposes that only a capital gain flowed through an "eligible LCGE trust" to a beneficiary will be eligible for the LCGE. This is a special sub-category of trusts and the typical *inter vivos* discretionary trust will not fit the definition. An "eligible LCGE trust" is defined in the draft legislation as:[27]

- An alter ego trust, meaning a trust settled by an individual who had attained age 65 under which the individual is entitled to receive all of the income of the trust that arises before the individual's death and no person other than the individual may, before the individual's death, receive or otherwise obtain the use of any of the income or capital of the trust;

- A testamentary spousal trust meaning a trust created by the will of a taxpayer who died after 1971 under which the deceased's spouse or common-law partner is entitled to receive all of the income of the trust that arises before such individual's death and no person other than such individual may, before such individual's death, receive or otherwise obtain the use of any of the income or capital of the trust; or

- An *inter vivos* joint partner trust meaning a trust settled by an individual who had attained age 65 under which the individual in combination with his/her spouse or common-law partner is entitled to receive all of the income of the trust that arises before the later of the death of the individual and his/her spouse or common-law partner and no other person other than the individual could, before the later of those

[26] See draft paragraph 110.6(12)(d).
[27] See definition in draft subsection 110.6(1).

deaths, receive or otherwise obtain the use of any of the income or capital of the trust,

provided in all cases, that no amounts are distributed in the year from the trust other than to a "qualifying beneficiary", meaning the particular individuals referenced above for the particular trust.

An "eligible LCGE trust" will also include trust which holds shares of a corporation for the benefit of employees in the circumstances set out in subsection 7(2), ITA.

Election available in 2018

The July 18, 2017 draft legislation proposes an election mechanism pursuant to which gains accrued up to a chosen day in 2018 can be deemed realized so as to permit an individual to claim the LCGE. The election results in a deemed disposition of the property for proceeds of disposition equal to a designated amount.[28] But the election is not available in the following cases.

- An individual who has not attained age 17 by January 1, 2018 will not be eligible for the election where the property is shares of a corporation.
- A trust will not be eligible to make the election to flow out a capital gain from a notional or deemed disposition of shares of a corporation to a beneficiary who had not attained age 17 by January 1, 2018.

The property which is the subject of the election must be identified and owned continuously from the end of 2017 until the chosen disposition day in 2018. Further, while the property must be "qualified farm or fishing property" or "qualified small business corporation shares", the definitional requirements are proposed to be relaxed for this purpose only. Specifically, while such definitions have asset value, use or holding period requirements which look back 24 months from the date of disposition, the July 18, 2017 draft legislation proposes to use a 12 month test solely for the purpose of determining whether the property is eligible for the election.[29] Although the test period in the relevant definitions has been

[28] See draft subparagraph 110.6(18.1)(a). Note that the designated amount cannot be less than the adjusted cost base of the property so that it is not possible to elect to trigger a capital loss.
[29] See definition of "eligible property" in draft subsection 110.6(17) and in particular paragraph (d) therein.

shortened to 12 months, given that the chosen disposition day for purposes of the election must be in 2018, this means that purification steps (if necessary to satisfy the definitional requirements) must be completed before December 31, 2017.

The due date for the filing of the election is the taxpayer's "balance due date" for the taxation year which includes the chosen disposition date in 2018. For an individual, the "balance due date" is most likely April 30, 2019 while for a trust, the "balance-due date" would most likely be March 30, 2019. However, the July 18, 2018 draft legislation contemplates that the election may be late filed until December 31, 2020 provided that a penalty is paid. The penalty is equal to 1/3 of 1% of the taxable capital gain so triggered for each month from the due date for the election as described above until the month in which the election is filed.[30] An election may also be amended or revoked within that period. However, there are adverse consequences to electing in excess of 110% of the fair market value of the property on the chosen disposition date:

An election cannot be amended or revoked if the designated amount exceeds 110% of the fair market value of the property on the disposition date.[31]

Generally, the designated amount is the deemed proceeds of disposition of the property and the taxpayer is then deemed to reacquire the property at a cost equal to the designated amount. However, if the designated amount exceeds 110% of the fair market value of the property on the disposition date, then the taxpayer's cost of the reacquired property will be reduced by the amount by which the designated amount exceeds 110% of fair market value[32]

Before making the election, consideration should be given as to whether the triggered capital gain may result in alternative minimum tax ("AMT") for the particular individual. AMT is charged under section 127.5, ITA and generally requires an adjusted computation of income; the adjustment includes adding back items which might be considered tax preferences. By way of example, while ½ of a capital gain (referred to as the taxable capital gain) is included in income for "regular" Part I tax purposes, the adjusted taxable income computation for AMT purposes includes 4/5 of the capital gain. AMT is calculated at a flat

[30] See draft subsection 110.6(29).
[31] See draft subsection 110.6(28).
[32] See draft subparagraph 110.6(18.1)(a)(ii).

rate of tax (presently 15%) on the adjusted taxable income in excess of $40,000. The election to trigger a deemed capital gain so as to make use of the LCGE may result in AMT for the particular taxpayer, depending on his/her other income.

As a transitional measure, if a minor or a trust under which a minor is a beneficiary disposes of shares of a corporation in 2018, and the share was owned by such minor or trust continuously from December 31, 2017 to the date of disposition, then the current rules (and not the July 18, 2017 draft legislation) will apply.[33] This means that the minor may be able to claim the LCGE and the draft TOSI rules will not apply. For this purpose, the definitional requirements for "qualified farming or fishing property" and "qualified small business corporation share" are relaxed so that the tests therein relating to 24 month holding period, asset value and use are deemed to be 12 month tests. It should be noted that although the draft TOSI rules will not apply, current subsections 120.4(4) and (5) will operate to prevent an internal crystallizations.

The Pipeline and the July 18, 2017 Draft Legislation

The post mortem tax planning strategy known as the "pipeline" has effectively been eliminated by proposed amendments in the July 18, 2017 draft legislation to section 84.1, ITA. Because of the lack of grandfathering or any transitional rules, deaths which occurred prior to July 18, 2017 are adversely affected, including estates which arose more than one year prior to July 18, 2017 and are therefore outside the one year period to implement subsection 164(6), ITA planning.

At a September 25, 2017 conference hosted by the Canadian Tax Foundation, "Tax Planning Using Private Corporations: Analysis and Discussion with Finance", officials from the Department of Finance provided some comments and observations in the final panel – "Reactions & Closing Observations: Department of Finance and Practitioners Panel". The replies or comments of the Department of Finance have not been published in written form.[34] No pronouncements or commitments were made. However, there seemed to be recognition that double or multiple taxation on death should be addressed in some fashion.

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[33] See draft paragraph 110.6(30.1).

[34] The archived video of the conference including the above panel is available on the Canadian Tax Foundation website to registrants of the conference.

On a more specific vein, the Department of Finance official indicated that perhaps the scope of subsection 164(6), ITA should be expanded beyond the current 12 month deadline and in addition, there was suggestion that there may be some sort of grandfathering or transitional rules applicable to deaths which occurred prior to July 18, 2017.

On October 3, 2017, following the end of the 75 day consultation period, the Department of Finance issued a news release, "Next Steps in the Government's Plan for Tax Fairness and a Strong Middle Class",[35] which stated among other things, that the government will base its next steps on certain key principles which appear to be motherhood statements. Point 4 of the key principles may be considered noteworthy: "Recognize the importance of maintaining family farms, and work with Canadians to ensure we don't affect the transfer of a family business to the next generation." It would be conjecture to comment on the meaning of the foregoing statement in relation to the elimination of the pipeline in the July 18, 2017 draft legislation or the draft amendments to subsections 120.4(4) and (5).

2017 FEDERAL BUDGET - CORPORATE AND BENEFICIAL OWNERSHIP

The 2017 Federal Budget also announced its intention 'to strengthen the transparency of legal persons and legal arrangements and improve the availability of beneficial ownership information" and to enhance tax reporting requirements for trusts to enable collection of information regarding beneficial ownership.[36]

AMOUNT PAID TO BENEFICIARY IN CONTRAVENTION OF TERMS OF TRUST

CRA document no. 2016-0663971I7[37] is a recent technical interpretation involving taxation of an amount paid by a personal family trust to a beneficiary. It is axiomatic to think that where income of a trust is actually paid by the trust to a beneficiary, the amount is deducted from the income of the trust and included in the income of the beneficiary. However, this technical interpretation provides CRA's views where the amount is paid in contravention of the terms of the trust. CRA's position leads to double taxation.

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[35] Available on the Department of Finance website http://www.fin.gc.ca/n17/17-091-eng.asp

[36] See 2017 Federal Budget, caption "Strengthening Corporate and Beneficial Ownership Transparency" available on the Department of Finance website: http://www.budget.gc.ca/2017/docs/download-telecharger/index-en.html . See chapter 4 of the Budget Plan.

[37] November 1, 2016.

The particular trust in the interpretation included an anti-subsection 74.4, ITA clause. In particular, an article of the agreement provided that no minor beneficiary shall receive or otherwise obtain the use of any of the income or capital of the trust while being a "designated person" as defined in section 74.5, ITA. Such a clause is often included in a trust agreement in circumstances of a corporate estate freeze to fit within the statutory exemption from the operation of section 74.4, ITA. Pursuant to section 74.4, ITA where an individual (e.g., the freezer) has transferred property directly or indirectly by means of a trust or by any other means whatever, to a corporation and one of the main purpose of the transfer may reasonably be considered to be to reduce the income of the individual and to benefit, directly or indirectly, a "designated person", there is an imputed interest amount which is included in the individual's income each year. In general terms. a "designated person" is a non-arm's length minor or spouse of the individual in question. This section is commonly referred to as the "corporate attribution" rule. However, unlike other attribution rules in the ITA, it is not based on the attribution of income actually earned, but rather takes the form of a quasi-investment income calculation. For example, if a parent transfers a property to a corporation pursuant to section 85(1), ITA in consideration of redeemable retractable preferred shares and steps are taken so that the common shares are issued to a discretionary family trust for the benefit of his/her minor children, section 74.4, ITA is a concern.

Section 74.4, ITA will not apply if either:

> The corporation is and remains a "small business corporation" as defined[38]
>
> Subsection 74.4, ITA applies:
>
> > (a) The only interest that the designated person has in the corporation is a beneficial interest in shares of the corporation held by a trust.
> >
> > (b) By the terms of the trust, the designated person may not receive or otherwise obtain the use of any of the income or capital of the trust while being a "designated person" in respect of the individual.

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[38] See subsection 248(1), ITA. This is a rather stringent test as it requires ongoing diligence to ensure that "non-active business assets" do not exceed 10% of the fair market value of all assets of the corporation.

(c) The designated person has not received or otherwise obtained the use of any of the income of capital of the trust, and no deduction has been made by the trust pursuant to subsection 104(6) in respect of amounts paid or payable to a designated person.

While the particular trust agreement did contain a clause as described above, income was nonetheless paid to a minor beneficiary. There was no discussion in the technical interpretation about the effect of same on the application of the exemption from section 74.4, ITA.

In CRA's view, an amount may only be deducted from the income of the trust pursuant to subsection 104(6) where the amount is income "that became payable in the year to" a beneficiary. Because of the anti-section 74.4 provision in the trust agreement, it was not possible for an amount to become payable in the year to the minor beneficiary (being a "designated person"). Accordingly, the amount could not be deducted from the income of the trust.

The amount paid to the minor beneficiary was included in his/her income as a benefit. There is a specific benefit rule applicable to trusts. Subsection 105(1), ITA provides that the value of all benefits to a person from or under a trust shall be included in computing the person's income except to the extent that the value is otherwise included in the person's income. In this case, there was no other provision which included the amount in the minor beneficiary's income and as a result, CRA's view was that subsection 105(1) applied.

The result of contravening paying the amount to a minor beneficiary in contravention of the anti-section 74.4 provision was double taxation – the amount remained income of the trust subject to tax in the trust's hands but was also considered a benefit, taxed in the beneficiary's hands.

ISSUING INFORMATION SLIPS FOR DISTRIBUTIONS OF CAPITAL TO A NON-RESIDENT

A distribution of income by a trust or estate to a Canadian resident beneficiary must be recorded on information return T3 issued by the trust or estate to the beneficiary. However,

a distribution of capital by a trust or estate to a Canadian resident beneficiary need not be reported on such a slip.

A distribution of income by a trust or estate to a non-resident beneficiary must be reported on Form NR4 ("Statement of Amounts Paid or Credited to Non-Residents of Canada") issued by the trust or estate to the non-resident beneficiary. Part XIII tax (i.e., non-resident withholding tax) at 25% may apply subject to reduction pursuant to any applicable international tax treaty. Specifically, Part XIII tax applies to every amount that a Canadian resident rust or estate pays or credits as income to a non-resident beneficiary.[39] This applies to amount included in a beneficiary's income under subsection 104(13) or an amount that can reasonably be considered to be the distribution of a capital dividend. Where there I a distribution of capital to a non-resident beneficiary, subsection 212(11) deems such a distribution to be income, albeit for Part XIII tax purposes only. However, by virtue of subparagraph 212(1)(c)(ii), only distributions of capital described therein, i.e., a capital dividend received by a trust from a corporation resident in Canada, will be subject to withholding tax.

CRA recently stated in a technical interpretation[40] that while only the above distribution of capital is subject to withholding tax, all distributions of capital must be reported on Form NR4 using a code to denote that the amount is exempt from withholding tax. Form NR4 must be filed no later than 90 days after the end of the taxation year in which the amount was paid. CRA also indicated that it will not waive the filing obligation.

The above would appear to be a new and stricter obligation now being enforced by CRA.

EVOY ESTATE v. THE QUEEN 2016 TCC 263

Evoy Estate involved multiple testamentary trusts. Today this estate planning would not achieve the same tax planning benefit because a testamentary trust (which is not a graduated rate estate[41] or qualified disability trust[42]) is taxed at the highest federal marginal rate. Prior

[39] See paragraph 212(1)(c), ITA.

[40] CRA document no. 2015-0608201E5, December 22, 2016. This document is in French, interpretation available on Taxinterpretations.com.

[41] See definition in subsection 248(1), ITA.

[42] See definition in subsection 122(3), ITA.

to amendments applicable to the 2016 and subsequent taxation years[43], a testamentary trust enjoyed the benefit of the marginal rates and therefore provided an income splitting opportunity. Multiple testamentary trusts could multiply access to the marginal rates. For example, the Will of the deceased could provide for a number of trusts, e.g., a trust for the benefit of child #1 and issue; a trust for the benefit of child #2 and issue; a trust for the benefit of child #3 and issue; a trust for the benefit of both child #1 and #2 and issue; a trust for the benefit of both child #2 and #3 and issue and so on. Each testamentary trust could benefit from the marginal rates. In addition, it was possible to make an election pursuant to subsections 104(13.1) or (13.2) to tax income in the trust yet distribute the income to a beneficiary. Such an election has now been limited to circumstances where the trust has losses.[44] Thus the enhanced income tax benefits from multiple testamentary trusts have now been eliminated.

The spectre of subsection 104(2), ITA hung over the old multiple testamentary trust planning. Subsection 104(2) provides the Minister with discretion to tax multiple trusts as a single trust where certain conditions are met as follows:

> (a) substantially all of the property of the various trusts has been received from one person; and
>
> (b) the various trusts are conditioned so that the income thereof accrues or will ultimately accrue to the same beneficiary, or group or class of beneficiaries.

If subsection 104(2) applied, the multiple trusts established in the Will of the deceased would be taxed as one testamentary trust with one set of marginal rates. There was little jurisprudence[45] on the potential application of subsection 104(2) until *Evoy Estate*.

In *Evoy Estate*, the Minister exercised his discretion pursuant to subsection 104(2) to designate three trusts established under the Will of the late George Evoy as one trust. The deceased was survived by his wife, Pauline and three children, David, Karie and Wendy. The three trusts are referred to herein as D's Trust; K's Trust and W's Trust.

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[43] See amendment to the preamble to subsection 122(1) pursuant to S.C. 2014,c. 39,s. 38(1)

[44] See subsection 104(13.3), ITA.

[45] See *Mitchell v. MNR* 56 DTC 521 (TAB).

The deceased held shares of a private corporation which passed upon his death to his Estate and then to the trusts. The property of the three trusts was virtually identical, but for a nominal difference in the number of shares of a particular class of the particular corporation.[46]

In each trust, Pauline (the surviving spouse) was entitled to all of the net income during her lifetime thereby meeting the requirement for a "rollover" to a testamentary spousal trust pursuant to subsection 70(6) of the Act. Following Pauline's death, in the case of D's Trust, David and his children were entitled to all of the income in such proportions as the trustees determined and upon termination of D's Trust, David was to receive all the capital. D's Trust could be terminated no earlier than the 3rd anniversary of Pauline's death and no later than the 21st anniversary of her death. K's Trust had identical terms, but for the substitution of Karie and her children. Similarly, W's Trust had identical terms but for the substitution of Wendy and her children.

The Minister applied subsection 104(2) for the 2008, 2009 and 2010 taxation years. Pauline was alive in those years and as a result, all of the income of the three trusts was paid to her.

The issue in the case was whether condition (b) in subsection 104(2) was satisfied, i.e., whether all of the trusts were conditioned so that the income accrues or will ultimately accrue to the same beneficiary or group or class of beneficiaries. The argument appeared to be based on the fact that in each of the years in question, Pauline (the surviving spouse) received all of the income of D's Trust, K's Trust and W's Trust.

The Tax Court held that condition (b) was not an annual test to be applied for a single taxation year of a trust but rather, a test to be considered over the "entire lifetime" of a trust. Emphasis was placed on the use of the word "ultimately" in condition (b). Further, applying the test based on an annual review of income allocation suggested a need to "re-designate" in a subsequent year where the income of the trusts did not accrue to the same beneficiary and the court held that there was no such provision in the legislation. B. Paris, J. noted that such an interpretation as advocated by CRA would lead to uncertainty.

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[46] D's Trust and K's Trust held 947,623 Class A shares whereas W's Trust held 947,622 Class A shares. D's Trust and K's Trust held 476,048 Preference Shares whereas W's Trust held 476,049 Preference Shares.

The Tax Court also disagreed with the argument that there was a single group or class of beneficiaries, being the spouse and issue of George Evoy given the terms of the trusts in question. B. Paris J. noted that the three trusts had no common beneficiaries following Pauline's death. As a result, the income of the three trusts could not accrue to the same group of class of beneficiaries.

On the basis of the above, the appeal was allowed and the three separate testamentary trusts were taxed as three testamentary trusts.

GRIMES v. THE QUEEN 2016 TCC 280

In *Grimes*, the trustees of the Ozerdinc Family Trust No.2 ("Trust 2") appealed CRA's determination of the fair market value of property held by Trust 2 on the deemed disposition day under subsection 104(4), ITA. This is commonly referred to as the "21 year deemed disposition rule". The issue was the value of shares of a private corporation held by Trust 2 being one (1) common Class A share and 2,699,900 First Preferred Shares of 1634158 Ontario Inc. ("Holdco"). The remaining shares of Holdco being 100 First Preferred Shares and 12 Fifth Preferred shares were held by Kathleen Grimes ("Kathleen"). Kathleen and her husband, Ersin were the two trustees of Trust 2 whose beneficiaries were the children of the marriage of Kathleen and Ersin. Kathleen and/or Ersin were directors, officers and/or key management of Holdco or its subsidiary entities.

With respect to the shares held by Trust 2, the First Preferred Shares were valued at their aggregate redemption amount which did not appear to be in dispute. With respect to the value of the one common Class A share, the Tax Court agreed that it was reasonable to apply a minority discount of 12.5% and a marketability discount of 15%. The two discounts were described as follows:[47]

> "A minority discount will be applied to make an adjustment or discount for lack of control associated with minority shareholdings. A marketability (or liquidity) discount will be applied when there is a

[47] At paragraph 174, *Grimes*.

> lack of marketability for the shares. Marketability has been defined as follows ….."the ability to convert the business ownership interest to cash quickly, with minimal transaction and administrative costs in so doing and with a high degree of certainty of realizing the expected amount of proceeds". It is clear from those two definitions that the minority discount and the marketability discount are two different concepts."

The Tax Court also rejected the view that the valuation of the shares of Holdco should take into account the income tax payable by the shareholder upon a redemption of the shares held by such shareholder (referred to as "embedded income tax").

Grimes is noteworthy for the judicial acceptance of marketability and minority discounts in the context of a family controlled enterprise. The 12 Fifth Preferred shares held by Kathleen had a nominal redemption amount of $1 but represented 68.97% of the voting rights attached to all issued and outstanding shares. The taxpayer's valuation expert attributed a small control premium to these shares in his report, which was noted by the Court, but not the subject of comment.

CONCLUDING COMMENTS

Much of this paper has been devoted to a discussion of the July 18, 2017 draft legislation and related proposals. These proposals are easily among the most significant and far reaching income tax changes affecting private corporations and related estate planning in many years. At the date of submission of this paper, the consultation period had ended but the path forward is unclear. This is particularly troubling given the proposed effective dates of certain provisions of the July 18, 2017 draft legislation.

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TAB 9

Jurisdictional Issues in Powers of Attorney

Paul Taylor
Borden Ladner Gervais LLP

DAY TWO
October 17, 2017

cpd Continuing Professional Development

Jurisdictional Issues in Powers of Attorney

Paul W. Taylor[1]

A. *Introduction*

Much has been written on the increasing connectedness and complexity of our aging population in a globalized world. Ideally (but less often than one would hope), an individual will have a power of attorney for property ("Power of Attorney")[2] in each jurisdiction in which he or she holds assets. In her excellent paper from the 16th Estate and Trusts Summit in 2013, Margaret O'Sullivan gives us examples how and why this would be done.[3]

I commend Margaret's article to you. In this paper I will focus on issues that arise where the requisite planning has not been completed in accordance with her advice and we are seeking to apply a Power of Attorney in a jurisdiction other than that in which it was created. We will pay particular attention to the interactions between Canada's various provinces, as it can be quite common for individuals to move to be closer to their families as capacity deteriorates, and new Powers of Attorney are not always top of mind.

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[1] Paul Taylor is a senior associate in the Family Wealth Counsel group of Borden Ladner Gervais LLP in Ottawa. His practice includes tax, estate, trust, and incapacity law. This paper would not have been possible without the assistance of Braek Urquhart and William Dion-Bernard, associates in the Ottawa and Montréal offices of BLG, respectively, and the guidance of Thomas Grozinger of RBC Wealth Management. All errors are Paul's. Please note that Paul is called to the bars of Ontario and Nunavut and, accordingly, where the laws of other jurisdictions are at issue appropriate local advice should be sought.
[2] "Power of Attorney" in this paper refers to a continuing or enduring power of attorney for property.
[3] See O'Sullivan, Margaret, "Conflict of Laws Issues in Drafting and Using Powers of Attorney for the Mobile Client", *LSUC 16th Annual Estates and Trusts Summit* (Toronto: November 12, 2013).

We will discuss conflicts of laws rules in respect of the formal validity of a Power of Attorney, the performance of a Power of Attorney, and the treatment of investment portfolios, which can be particularly troublesome.

B. Formal Validity

In Canada, each province treats foreign Powers of Attorney differently.[4] This treatment largely depends on whether that province's Power of Attorney conflict of law rules come from a common law, statutory, or civil law source.

i) Common law jurisdictions

In common law provinces without statutory conflict of law provisions (Nova Scotia, Newfoundland, Prince Edward Island, New Brunswick and Alberta), the common law conflict of law rules apply.[5] The rules provide that the governing law is that law, if any, that the Power of Attorney explicitly specifies. Where the Power of Attorney is silent, the proper law is likely the donor's domiciled jurisdiction, although the donor's intention ultimately governs. For example, the chosen law may be that law under which the attorney was intended to act, so long as the formalities required under that particular law have been met.[6]

Once the foreign Power of Attorney's governing law is determined, any third party seeking to rely on the Power of Attorney must satisfy itself that the Power of Attorney is valid under that governing law and survives incapacity. The third party must also satisfy itself that the Power of Attorney

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[4] Note that the term "foreign" includes from another province.

[5] These provinces' Power of Attorney legislation does not provide foreign Power of Attorney validity rules, so the common law applies. See: Newfoundland & Labrador: *Enduring Powers of Attorney Act*, RSNL 1990, c E-11; Nova Scotia: *Powers of Attorney Act,* RSNS 1989, c 352; Prince Edward Island: *Powers of Attorney Act,* RSPEI 1988, c P-16; New Brunswick: *Property Act,* RSNB 1973, c P-19; and Alberta: *Powers of Attorney Act,* RSA 2000, c P-20.

[6] See *Chatenay v Brazilian Submarine Telegraph Co,* [1891] 1 QB 79, *Sinfra Aktiengesellschaft v Sinfra Ltd,* [1939] 2 All ER 675 (KB), and *Re Cane* (1968), 66 DLR (2d) 741 (Man QB).

meets any additional requirements in the organization's jurisdiction. For example, some provinces impose additional rules on Powers of Attorney used for real estate transactions.

ii) Statutory jurisdictions other than Quebec

In the remaining provinces (Manitoba, Saskatchewan, British Columbia and Ontario), statutory conflict of law rules govern foreign Powers of Attorney.[7] Generally, each of these provinces' statutes requires the Power of Attorney to (1) be valid in its home jurisdiction, and (2) endure after the donor's incapacity. For example, Ontario's provision is as follows:

> *Conflict of laws, formalities*
> **85.** (1) As regards the manner and formalities of executing a continuing power of attorney or power of attorney for personal care, the power of attorney is valid if at the time of its execution it complied with the internal law of the place where,
> (a) the power of attorney was executed;
> (b) the grantor was then domiciled; or
> (c) the grantor then had his or her habitual residence.
>
> *"Internal law"*
> (2) For the purpose of subsection (1), "internal law", in relation to any place, excludes the choice of law rules of that place.
>
> *Revocation*
> (3) Subsections (1) and (2) apply with necessary modifications to the revocation of a continuing power of attorney or power of attorney for personal care.
>
> *Legal requirements outside Ontario*
> (4) If, under this section or otherwise, a law in force outside Ontario is to be applied in relation to a continuing power of attorney or a power of attorney for personal care, the following requirements of that law shall be treated, despite any rule of that law to the contrary, as formal requirements only:
> 1. Any requirement that special formalities be observed by grantors answering a particular description.
> 2. Any requirement that witnesses to the execution of the power of attorney possess certain qualifications.
>
> *Alteration in law*
> (5) In determining for the purposes of this section whether or not the execution of a continuing power of attorney or power of attorney for personal care conforms to a particular law, regard shall be had to the formal requirements of that law at the time the power of attorney was executed, but account shall be taken of an alteration of law affecting powers of attorney executed at that time if the alteration enables the power of attorney to be treated as properly executed.
>
> *Application*

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[7] See the relevant provisions at Manitoba: *The Powers of Attorney Act,* CCSM c P-97, s 25; Saskatchewan: *Powers of Attorney Act,* SS 2002, c P-20.3, s 13; British Columbia: *Power of Attorney Act,* RSBC 1996, c 370, s 38; and Ontario: *Substitute Decisions Act, 1992,* SO 1992, c 30 ("*SDA*"), s 85.

(6) This section applies to a continuing power of attorney or power of attorney for personal care executed either in or outside Ontario.[8]

In Ontario, foreign execution requirements are to be dealt with as formalities only, and a foreign Power of Attorney will be recognized where it complies with the internal law of the place the Power of Attorney was executed, the grantor was domiciled, or the grantor was habitually resident.[9]

In addition to the requirements of the other statutory jurisdictions, it is notable that British Columbia regulations also require a lawyer's certificate from certain foreign jurisdictions indicating that the Power of Attorney (1) endures after the donor's incapacity; (2) was made by a person who was ordinarily resident in Canada, the United States, the United Kingdom, Australia or New Zealand (the "Certificate Jurisdictions"); and (3) was valid in that jurisdiction where the person was ordinarily resident.[10] For Powers of Attorney from non-Certificate Jurisdictions, the common law conflict of law rules described above continue to apply.

iii) Quebec

Quebec's rules are different from those of other provinces, as the C*ivil Code of Quebec* does not provide for a continuing or enduring Power of Attorney in the event of incapacity. While there are powers of attorney in Quebec, they cease to be effective on the incapacity of the Grantor. Incapacity planning in Quebec is achieved through the creation of a mandate in anticipation of incapacity. The mandate authorizes a person to act on the incapable individual's behalf, but the mandate is only effective after it has been "homologated". The process for homologating a mandate is loosely comparable to the process for probating a Will, and can only be done by the Quebec court or, in

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[8] *SDA* s 85.
[9] *SDA*, s 85(1).
[10] BC Reg 20/2011 as amended by BC Reg 111/2011.

non-contentious matters, by a Quebec notary (though only for a resident of Quebec, which can pose problems if the individual appointed has moved from Quebec to another jurisdiction).[11]

Even though a mandate is often included in the same instrument as the power of attorney that applies where the individual is capable and may often look similar to Powers of Attorney from other provinces, a third party may not rely on the mandate unless the third party is provided with proof of homologation. Homologation can be a time-consuming, expensive process. Even where a mandate is homologated, many organizations are not familiar with dealing with such a document. Quebec clients in particular should consider obtaining a local Power of Attorney in other jurisdictions where they keep assets, as a homologated mandate is not the equivalent of a continuing or enduring Power of Attorney and, accordingly, will generally not be recognized under foreign conflict of laws rules in the same manner.

Where a foreign Power of Attorney is presented for use in Quebec, the *Civil Code* conflict of laws provisions apply. Like the common law rules discussed above, these provisions involve a case by case analysis, and an enduring Power of Attorney that is valid in its home jurisdiction will likely provide an attorney with the proper authority to deal with property in Quebec.[12] Like the other provinces, a legal opinion on the foreign Power of Attorney's validity in its home jurisdiction will often be required by the third party before it accepts such a document.

iv) Other Countries

While Canadian Powers of Attorney will possibly be valid in other countries, third parties in other countries will generally require a court order or at least a solicitor's opinion to validate the Power

[11] *Civil Code of Quebec*, SQ 1991, c 64 ("*Civil Code of Quebec*"), Article 2166; *Code of Civil Procedure*, c C-25.01, s 302.
[12] *Civil Code of Quebec*, Article 3085.

of Attorney. Clients should be encouraged to obtain Powers of Attorney in those countries where they hold assets in order to minimize uncertainty and delay.

C. ***Validity in Performance***

Significant issues may arise where the laws of a jurisdiction (the "jurisdiction of validity") grant an attorney under a Power of Attorney powers that are not available in the jurisdiction where the attorney seeks to act (the "jurisdiction of performance"). In such circumstances, does the jurisdiction of validity or the jurisdiction of performance govern an attorney's actions?

i) Common Law Jurisdictions

One example where this issue could arise involves a British Columbia resident who grants a valid Power of Attorney, governed by British Columbia law, to an attorney who is also a British Columbia resident. Under British Columbia's laws, an attorney is permitted to designate a beneficiary under one registered plan (e.g., an RRIF) as a designated beneficiary under a subsequent registered plan (e.g., an RRSP) where the prior plan matures.[13] However, common law generally treats such designations as testamentary in nature, and such a designation is not generally permissible in common law jurisdictions unless a statute states otherwise.

Courts address jurisdictional discrepancies such as these by distinguishing between the law governing the "substance" of a contract and the law governing its "performance." The substance of a contract[14] must be determined by the proper law of the contract, but that contract's performance

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[13] *Wills, Estates and Succession Act*, SBC 2009, c 13, s 90.
[14] Powers of attorney were initially agency contracts. The continuing or enduring Power of Attorney is a statutory modification of that contract that allows it to survive incapacity and also imposes fiduciary obligations on the attorney. While Courts are often willing to find that those obligations are "trust-like" in nature, the genesis of the document itself and, absent statutory guidance otherwise, its treatment for conflict of laws purposes is as a contract.

must comply with the law where the contract will be performed.[15] For example, the British Columbia Court of Appeal has refused to enforce a contract relating to collecting rent in Washington State, entered into under the proper law of British Columbia, when the party collecting rent did so without first obtaining the required Washington state license.[16] This rule stems from the presumption that contracting parties intend a contract to be performed consistently with local legal requirements.[17]

In the above-described scenario, where a British Columbia attorney seeks to exercise his or her powers in a foreign jurisdiction, British Columbia law applies to the extent it is not illegal in the jurisdiction of performance.[18] Accordingly, a British Columbia attorney, acting in a common-law jurisdiction such as Ontario without similar statutory powers, would not be able to designate a designated beneficiary under a second registered plan in where the first registered plan matures.

Conversely, consider the scenario where an Ontario resident, validly appointed as attorney for another Ontario resident under an Ontario Power of Attorney, seeks to exercise his or her powers in British Columbia. The Ontario attorney would be bound by Ontario law as the proper law of the contract when dealing with property in British Columbia, and could not rely on the more expansive British Columbia rules to name designated beneficiaries. As stated in *Montreal Trust Co v Stanrock Uranium Mines Ltd*:

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[15] *Montreal Trust Co v Stanrock Uranium Mines Ltd*, [1966] 1 OR 258, 1965 CarswellOnt 215 at para 35 [*Stanrock*]; see also *Gillespie Management Corp v Terrace Properties*, 62 DLR (4th) 221 (BCCA) [*Gillespie*]; 1998 ABQB 714 at 68; and 2002 MBQB 277.
[16] *Gillespie*, *ibid*.
[17] Castel & Walker, *Canadian Conflict of Laws*, 6th Ed (Toronto: LexisNexis Butterworths (loose-leave revision 39-8/2013), 31.5.h.
[18] *Stanrock*, *supra* note 3 at paras 60-61.

> …the substance of the obligation is to be determined by one law only, i.e., the proper law of the contract. The method and manner of performance may be regulated by the law in place of performance notwithstanding that this is not the proper law of the contract. In this respect there may be a "split" but only to performance.[19]

The Court's analysis in this case is consistent with the rule that, generally, in a conflict of laws scenario, conveying, assigning or otherwise dealing with property must generally be carried out in accordance with the property law of the jurisdiction of performance.[20]

As Ontario law is the proper law of the Power of Attorney, the Ontario attorney has the ability to do anything Ontario law, and only Ontario law, permits an attorney to do. Regardless of British Columbia's more permissive attorney beneficiary designation regime, an Ontario attorney in these circumstances would be governed by the substance of Ontario's common-law rules. British Columbia law may "regulate" the manner in which the Ontario attorney performs his or her duties, but such regulation of the attorney's performance would not expand the substance of the attorney's authority.

This analysis assumes that the attorney's ability to appoint beneficiaries would be considered part of the "substance" of the Power of Attorney, and therefore governed by the Power of Attorney's proper law. Difficulties may arise in characterizing the "substance" of a Power of Attorney as comparted to its "performance." However, the practical effect of this of this conflict of laws rule likely means that the law of the more restrictive jurisdiction would dictate an attorney's permissible powers.

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[19] *Stanrock*, *supra* note 3 at para 34.
[20] *Castel & Walker*, *supra* note 5 at 31.5.i, 31.5.j, 31.5.l.i.

ii) Quebec

Under Article 3109 of the *Civil Code of Quebec*, the form of a foreign Power of Attorney is governed by the law of the location where it is entered into and will be acknowledged in Quebec as long as it conforms to the applicable foreign law. Where Quebec is the jurisdiction of performance, the applicable rules of the *Civil Code of Quebec* are substantively similar to common law rules: in principle, the British Columbia Attorney's range of permissible actions is determined by the foreign Power of Attorney and foreign applicable law as long as it does not infringe Quebec public policy.[21]

For example, Article 2446 of the *Civil Code of Quebec* allows the designation of beneficiaries under insurance policies to be made by any written document:

> *The designation of beneficiaries or of subrogated policyholders is made in the policy or in another writing which may or may not be in the form of a will.* [22]

If our validly appointed British Columbia Attorney seeks to designate a beneficiary under one registered plan as a designated beneficiary under a subsequent registered plan when the prior plan matures, and both plans are designed in accordance with and are subject to Quebec law, whether the British Columbia Attorney designation will be recognized under Quebec law remains doubtful. For instance, one could argue that any designation effected in the Province of Quebec has to be done *personaliter* and, as a consequence, any designation or appointment effected by a third party

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[21] *Civil Code of Quebec*, Article 8. *A person may only renounce the exercise of his civil rights to the extent consistent with public order.*
Civil Code of Quebec, Article 9. *In the exercise of civil rights, derogations may be made from those rules of this Code which supplement intention, but not from those of public order.*
[22] *Civil Code of Quebec*, art 2446.

infringes Quebec public policy. It may therefore be appropriate to appoint the beneficiary through the Power of Attorney so as to avoid any ambiguity.

D. *Status of Investment Accounts*

A common issue that arises with mobile clients is the law that governs investment accounts and an individual's interactions with them, for example, as attorney under a Power of Attorney. As an investment account is intangible personal property, for many purposes it is dealt with in accordance with the laws of the domicile of the individual who owned it. However, the laws applicable to the validity of the creation of the account and rules governing it, as well as the performance of any actions in relation to the account, will be governed by the proper law of the account.

An investment account will be governed by the account agreement entered into to create the account. As noted above in respect of the common law applicable to the formal validity of Powers of Attorney, the account agreement will be the starting point for any analysis of the law of formal validity of the investment account. Where the account agreement is clear and unambiguous in respect of the intent of the parties it is likely that the Courts will uphold a choice of law provision in an investment account agreement..

Where the investment account agreement is unclear or unenforceable as to the applicable laws, the conflicts of laws rules would apply. In general, the proper law of the jurisdiction where the account was created would be the proper law.[23] While there is limited directly applicable case law, what is available is consistent with this interpretation:

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[23] Janet Walker, *Canadian Conflict of Laws,* 6th ed (Markham: Butterworths, 2005) (loose-leaf revision 2017 supplement), ch 24 at 24-1 [Walker].

(i) In *Re Anziani,*[24] the English Court of Chancery considered the appointment and assignment of intangible property in England by an English woman living in Italy. The Court held that the governing law was the place of the assignment of property, which was also the law of the assignor's domicile. As the governing document had been created in Italy while the woman was living in Italy, the Court held that Italian law applied.

(ii) The Quebec case *Drolet c. Trust général du Canada*[25] involves a joint account opened in Florida by Quebec residents. The Quebec Court of Appeal applied Quebec law as the law of the account holder's domicile. It distinguished between the joint account holders' relations with each other, and their relation with the financial institution. The Court held that the right of survivorship applied to the account as a "matter of contract", and the son was authorized to withdraw the money. However, ownership of the funds was a "matter of succession" and Quebec law determined the estate owned the funds.

(iii) While the case *Century Credit Corp. v. Richard*[26] deals with tangible movable property (as opposed to intangible movable property such as investment accounts), the conflict of laws rules applied remain relevant. The Ontario Court of Appeal considered the sale of a vehicle in Quebec, following which the vehicle was taken to Ontario and sold in Ontario. The Quebec sale was conducted in accordance Quebec law, but would have failed to meet Ontario's requirements and would be invalid under Ontario law. As the vehicle was now located in Ontario, at issue was whether the title acquired in Quebec was invalidated because it was not done in accordance with Ontario laws. The Court of Appeal held that

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[24] *Re Anziani; Herbert v. Christopherson,* [1930] 1 Ch. 407.
[25] 1989 CarswellQue 280, 31 Q.A.C. 103, 1989 CanLII 571 (QCCA) see also *Gauthier c. Gauthier,* 2016 QCCS 2333.
[26] [1962] O.R. 815.

the transfer of a tangible movable was valid and effective if done in accordance with the *situs*, and title to the movable would remain valid even if the movable was removed from the jurisdiction where title was acquired. Accordingly, despite the fact that the Quebec vehicle sale did not comply with Ontario laws, the title acquired in Quebec was valid in Ontario.

As noted above, Courts address jurisdictional discrepancies by distinguishing between the law governing the "substance" or validity of a contract such as an investment account agreement and the law governing its performance. The substance must be determined by the proper law of the contract, but that contract's performance must comply with the law where the contract will be performed.[27]

Consider the case of an investment account where may have a Power of Attorney created in one jurisdiction (e.g. Ontario), a registered plan account created in another (e.g. British Columbia), and a client who has moved to that second jurisdiction (e.g. to British Columbia). In this case, as the grantor is resident in British Columbia, the statutory conflict of laws rules would apply and the mandated certificate would be required. As the Power of Attorney was created in Ontario, the attorney could not rely on the ability under British Columbia law to make a beneficiary designation for the client, even though the account itself would be governed by British Columbia law.

In the above example, it becomes clear that incapacity planning should be updated regularly and should involve local counsel in all relevant jurisdictions. If not, hopefully this paper will provide some assistance in untangling the web of applicable laws.

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[27] *Montreal Trust Co v Stanrock Uranium Mines Ltd*, [1966] 1 OR 258, 1965 CarswellOnt 215 at para 35 [*Stanrock*]; see also *Gillespie Management Corp v Terrace Properties*, 62 DLR (4th) 221 (BCCA) [*Gillespie*]; 1998 ABQB 714 at 68; and 2002 MBQB 277.

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LET RIGHT PREVAIL

TAB 10

Musings on the Effects of Trump's Tax Proposals on Canada-U.S. Cross Border Estate Planning

Katherine Cauley, Esq.
Graham Leonard, Esq.
Hodgson Russ LLP

DAY TWO
October 17, 2017

Continuing Professional Development

Musings on the Effects of Trump's Tax Proposals on Canada-U.S. Cross Border Estate Planning

Katherine E. Cauley, Esq.
Graham S. Leonard, Esq.
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Introduction

The United States (U.S.) federal taxation regime taxes the transfer of assets both during life and at the death of a taxpayer. U.S. estate, gift and generation-skipping transfer ("GST") taxes (collectively, "transfer taxes") affect U.S. citizens (even if residing outside the United States), non-U.S. citizens domiciled in the United States, and non-U.S. citizens not residing in the United States to the extent they own "U.S. situs" property.[1]

However, the future of the U.S. federal transfer tax system is unsettled. On September 27, 2017, President Donald J. Trump, the U.S. Senate Committee on Finance, and the U.S. House Committee on Ways and Means released a document that proposed a number of broad changes to the U.S. federal tax system (the "Framework").[2] If enacted, the Framework's proposed changes would represent the "most sweeping tax overhaul" to the U.S. federal tax system in decades.[3] As for federal transfer taxes, the Framework proposes the complete repeal of the estate tax, happily referred to therein as the "death tax," and the complete repeal of the GST tax.

Beyond the Framework, there are currently few details regarding the proposed changes to the U.S. federal transfer tax system. Indeed, the Framework itself provides no details beyond advocating for the repeal of the federal estate and GST taxes. Thus, U.S. estate planners

are left with significant uncertainty regarding what the future may bring for the U.S. transfer tax system.

Yet although it is not possible at this stage to predict the exact future of the U.S. transfer tax system, it is possible to address the potential effects of the proposed changes in the Canada-U.S. cross border estate planning context. It may also be possible to plan around some of this uncertainty. Moreover, even though avoidance of federal transfer taxes may be the primary driver of this sort of planning currently, there are other important benefits available as well, including possible avoidance of state level transfer taxes. Notably, the Framework only addresses federal transfer taxes. Several U.S. states have their own transfer taxes, which are discussed in more detail and summarized in a table below. Presumably, many state level transfer taxes would continue to exist even after a repeal of the federal estate and GST taxes.

This outline begins with a summary of the existing U.S. transfer tax regime as it applies to citizens and non-citizens (including both non-citizens residing in the U.S. and those not residing in the U.S.). The outline then moves to a discussion of the proposed changes to the U.S. federal transfer tax system advocated by the Framework. The outline concludes by addressing the effects of these proposed changes on select cross-border planning techniques.

A. U.S. Transfer Taxes

The U.S. transfer tax system applies differently to citizens and non-citizens of the United States. The following discussion applies to the federal transfer tax system. As noted, some states also impose a transfer tax (or taxes), which are separate from the federal transfer tax system.

1. United States Citizens

(a) Estate Tax

U.S. estate tax is imposed on the taxable estate of every decedent who is a citizen of the United States at the time of his or her death.[4] The starting point for calculating the taxable estate is a determination of the gross estate. The gross estate of a U.S. citizen decedent is comprised of the value at death of all property, real or personal, tangible or intangible, situated anywhere in the world, owned by the decedent at death.[5] This includes property owned individually by the decedent and jointly with another[6], life insurance owned by the decedent[7], annuities[8], assets over which the decedent has a general power of appointment[9], and assets transferred during life revocably[10], with a retained interest[11], or with a reversionary interest[12]. For property owned jointly by a husband and wife, one-half of the value of the joint property is includable in the estate of the first to die, although a different rule applies in non-spousal joint tenancy situations.[13] Unlike the Canadian deemed disposition tax, which taxes only an asset's gain at the death of the owner, the entire value of an asset is included in a decedent's gross estate for U.S. estate tax purposes. This can seem particularly harsh from a Canadian perspective.

After the gross estate is determined, credits, deductions and exclusions may be available to arrive at the taxable estate on which estate tax is imposed.[14] Deductions are available for, among other things, the decedent's funeral expenses, estate administration expenses, state estate taxes paid, and creditor's claims, as well as for qualifying charitable and marital bequests, discussed in greater detail below.[15]

For gross estates in excess of the available exemption (discussed more below), an estate tax return, Form 706, is due 9 months from the decedent's date of death.[16] Any estate tax liability must also be paid at that time.

Estate Tax Exemption. U.S. citizens are entitled to an estate tax exemption.[17] The amount of this exemption is adjusted for inflation and has steadily increased to its current high of $5.49M[18] in 2017.[19]

Charitable Deduction. Any assets left to qualifying charities at death are eligible for an unlimited charitable deduction from the U.S. estate tax. Qualifying charitable organizations can include foreign charities, so long as they meet the same requirements imposed on U.S. charities.[20]

Marital Deduction. An unlimited marital deduction from the estate tax is available for assets left in a qualifying manner to a surviving spouse.[21] This includes assets left outright to the surviving spouse as well as in qualifying trusts (namely a QTIP – qualified terminable interest property trust). In order to qualify for the marital deduction, the surviving spouse must be the only beneficiary of the QTIP during his or her lifetime and must receive all the income from the trust at least annually.[22] In addition, the Executor of the decedent's estate must elect to treat the trust as a QTIP on the estate tax return. Any assets remaining in the QTIP at the death of the surviving spouse are includible in his or her gross estate.

Thus, if all property (or at least property in excess of the exemption) passes from the estate to charity or a surviving U.S. citizen spouse (either outright or in a qualifying trust), there is no U.S. estate tax on the death of the first spouse.

Income Tax Considerations. Generally, all assets included in a decedent's taxable estate receive a basis step-up to the fair market value of the asset as of the decedent's date of death (regardless of whether estate tax is actually paid).[23]

(b) Gift Tax

U.S. citizens are subject to gift tax on transfers made during life, subject to the exclusions, exemptions, and deductions discussed below. The gift tax rate is generally the maximum estate tax rate in effect (currently 40%).[24] Taxable gifts must be reported (and any associated gift tax paid) on a Form 709 due on April 15th of the year following the year the gift was made.

Annual Gift Tax Exclusion. U.S. citizens have an annual gift tax exclusion of $14,000 per donee, per year (indexed for inflation).[25] Use of the annual gift tax exclusion does not require the filing of a gift tax return.[26] Annual exclusion gifts generally must be of a present interest, and not a future interest. There are therefore certain additional requirements that must be followed when making annual exclusion gifts to a trust on behalf of a donee.

Tuition & Medical Expenses. There is also an unlimited gift tax exclusion for amounts paid on behalf of a donee for educational or medical purposes, provided that the gift must be made directly to the educational or medical provider.[27]

Lifetime Gift Tax Exemption. In addition to the annual gift tax exclusion, U.S. citizens have a lifetime gift tax exemption in the amount of $5.49M for 2017, which is adjusted annually for inflation. Use of any of the $5.49M gift tax exemption reduces the available U.S. estate tax exemption on a dollar-for-dollar basis, and must be reported on a Form 709. In this way, the estate tax and the gift tax are said to be "unified," i.e., the estate and gift taxes work together, with lifetime taxable gifts that exceed the annual gift tax exclusion amount ultimately reducing the amount of property that can pass free of estate tax on an individual's death.

Marital Deduction. Gifts made to a U.S. citizen spouse during life, of any amount, qualify for the marital deduction from gift tax.[28] As discussed more below, the marital deduction is limited to a certain annual amount (presently $147,000) if the donee spouse is not a U.S. citizen.[29]

Charitable Deduction. As with the marital deduction, gifts of an unlimited amount can be made to qualifying foreign or domestic charities without the imposition of gift tax.[30]

There is no income tax event associated with gifts. The donee of the gift assumes the donor's basis in the gift.[31] The donor of a gift is primarily liable for paying the gift tax.[32] A donee may also be liable for the gift tax if it is not paid by the donor.

(c) Generation-skipping Transfer Tax

U.S. citizens are also subject to GST tax on transfers that "skip" a generation (for example, a gift from grandparent to grandchild, thereby avoiding gift or estate taxation at the

child's generation).[33] U.S. citizen taxpayers have a $5.49M GST tax exemption, just like the estate and gift tax exemption. The GST tax exemption is also adjusted annually for inflation. Transfers subject to GST tax over the exemption are taxed at a top marginal rate of 40%.

2. Non-U.S. Citizens

Non-citizens of the United States are divided into two categories for U.S. transfer tax purposes – Resident Aliens (RAs) and non-Resident Aliens (NRAs).

(a) Resident Aliens Domiciled in the U.S.

(i) Estate Tax

As with U.S. citizens, U.S. estate tax is imposed on the worldwide estate of every decedent who is domiciled in the United States at the time of his or her death ("Resident Aliens"). Thus, Resident Aliens are, for estate tax purposes, subject to U.S. estate tax on their worldwide assets just as a U.S. citizen is. A Resident Alien is entitled to the same estate tax exemption amount as a citizen ($5.49M as of January 1, 2017).

Marital Deduction. Bequests to non-citizen spouses are treated significantly different than bequests to a U.S. citizen spouse, however. Based on the concern that a non-citizen surviving spouse would leave the United States, and thus the property would escape estate taxation in the second spouse's estate, a bequest to a non-citizen spouse is not eligible for the marital deduction unless the bequest is in the form of a qualified domestic trust (a "QDOT").[34] In order to qualify as a QDOT, the trust must satisfy all the requirements of a

Qualified Terminable Interest Property trust, the trust for a U.S. citizen spouse eligible for the marital deduction. There also must be at least one U.S. citizen or U.S. corporate trustee[35], and the U.S. trustee must have the right to withhold QDOT tax from any trust distribution.[36] U.S. estate tax is imposed on distributions of capital from the QDOT to the surviving spouse during his or her lifetime (unless for "hardship")[37], and any remaining balance is included in the estate of the surviving spouse at death.[38]

With respect to jointly-held property, where the surviving joint tenant is someone other than a U.S. citizen spouse, 100% of the value of the joint property is includable in the estate of the first joint tenant, unless it can be demonstrated what value the surviving joint tenant contributed toward the property.[39]

Credit for Taxes Paid. The estates of U.S. decedents and residents can claim a credit against U.S. estate tax for Canadian tax paid at death.[40]

(ii) Gift Tax

The gift tax rules applicable to U.S. citizens generally apply to Resident Aliens, except the gift tax unlimited marital deduction is not allowed for gifts to a spouse who is not a U.S. citizen. Rather, an annual exclusion amount (currently $147,000 and adjusted annually) is allowed for outright gifts made to a non-citizen spouse that otherwise would qualify for the marital deduction if the donee spouse were a citizen.[41]

(iii) GST Tax

Resident Aliens are subject to GST in the same manner as U.S. citizens. Transfers made from a grandparent to a grandchild or younger generation, during life or at death, are taxed at a top marginal rate of 40% to the extent they exceed the GST tax exemption of $5.49M.

While Resident Aliens are treated similarly to U.S. citizens in many ways, proper planning is essential to take advantage of all relief provided by U.S. law and applicable treaties.

(b) Non-Resident Aliens

(i) Estate Tax

Non-Resident Aliens ("NRA"s) are treated quite differently than U.S. citizens and Resident Aliens for estate tax purposes. U.S. estate tax applies only to the portion of an NRA decedent's gross estate which at the time of his or her death is situated in the United States.[42] U.S. situs assets include:[43]

- real property located in the U.S.;
- tangible personal property located in the U.S.;
- stock in a U.S. corporation; and
- debt obligations of U.S. persons, the U.S. government or any political subdivision thereof (with some exceptions).[44]

There are some less obvious rules that may result in exposure to U.S. estate tax for an NRA. If an NRA transfers property in trust, either during life or at death, the transferred

property is deemed situated in the United States if it was situated in the United States at the time of transfer or at the time of death. If an NRA holds shares in a mutual fund, the situs may be deemed to be the situs of the assets held by the fund (if it is not taxable as a corporation for U.S. tax purposes). Thus, a mutual fund organized as a trust may be deemed a U.S. situs asset to the extent the mutual fund itself holds U.S. situs assets. An interest in a partnership or an entity taxable as a partnership (e.g., a "Limited Liability Company" or "LLC") may be a U.S. situs asset if the underlying partnership assets are located in the United States, although the law is unclear in this area. Annuities, stock options, and retirement proceeds, to the extent the obligation is that of a U.S. person or entity, are U.S. situs, although life insurance (even if provided by a U.S. company) is not.[45] Generally, amounts on deposit at U.S. banks (unless connected with a U.S. business) are not U.S. situs under a special exemption rule.[46]

These are only general guidelines. Because of the intricacies of these rules, and because some areas of the law in this area remain unsettled, any investment by an NRA that has a U.S. component should be examined carefully to determine any potential U.S. estate tax implications.

Estate Tax Exemption. Under U.S. domestic law, an NRA has only a $60,000 estate tax exemption equivalent.[47] For Canadian citizens and residents, the Third Protocol to the U.S. - Canada Treaty (the "Treaty") affords additional relief. Under the Protocol, a Canadian citizen and resident is entitled to a potentially greater U.S. estate tax credit that exempts an amount equal in ratio to the credit for U.S. citizens as the value of the Canadian's U.S.-situs assets is to the value of his or her worldwide estate (the "pro-rated credit").[48] This exemption

amount is determined by multiplying the applicable estate tax exemption for U.S. citizens by a fraction, the numerator of which is the value of the decedent's U.S. situs assets and the denominator of which is the value of the decedent's worldwide assets.

As with the exemption, the deductions an NRA is permitted to take against his or her U.S. estate tax are also prorated based on the proportion of the value of the U.S. situs assets to the decedent's worldwide assets.[49]

Thus, while the non-U.S. situs assets of a decedent are not subject to U.S. estate tax, they are relevant to determining the applicable U.S. exemptions and deductions.

Marital Credit. A marital credit is also available, in addition to the pro-rated exemption, for property that passes to a surviving spouse in a manner that would qualify for the marital deduction if the surviving spouse was a U.S. citizen.[50] The credit is available if (1) the decedent was a U.S. citizen at the time of death or a resident of Canada or the U.S.; (2) the decedent's surviving spouse is a resident of either Canada or the U.S.; and (3) both the decedent and the surviving spouse were U.S. residents at the decedent's death or one or both was a Canadian citizen. The marital credit essentially doubles the pro-rated estate tax exemption. If the marital credit is utilized, however, the marital deduction (and QDOT election) discussed below is not available.

Marital Deduction. The marital deduction is available for transfers by an NRA to a U.S. citizen spouse or in a QDOT to a noncitizen spouse to the same extent allowed to a U.S.

citizen or RA. As mentioned above, the marital deduction (and QDOT election) is not available if the marital credit is elected.

Charitable Deduction. A U.S. estate tax deduction is allowed for certain bequests made by an NRA to qualifying U.S. charities.[51] Bequests to non-U.S. charities are not eligible for the deduction.[52]

Credit for Taxes Paid. Under the Treaty, the estates of Canadian decedents can claim a deduction against Canadian income tax for U.S. estate tax paid on property situated in the U.S. at death.[53] It is therefore generally advisable to incur Canadian deemed disposition taxes and U.S. estate taxes in the same tax year (as opposed to, for example, U.S. property owned by a Canadian citizen that does not qualify for Canadian spousal rollover but could be covered by the marital credit for U.S. estate tax purposes) to ensure an offsetting credit can be obtained.

(ii) Gift Tax

NRAs are subject to U.S. gift tax on gifts of U.S. real property or tangible personal property situated within the United States at the time of the gift.[54] Lifetime transfers of intangible property, such as stock in a U.S. corporation, are not taxed for gift tax purposes.[55] As with the estate tax, an NRA's charitable deduction from gift tax is limited to gifts made to qualifying U.S. charities.[56]

(iii) GST Tax

For NRAs, U.S. GST tax is applicable on transfers that are subject to U.S. estate or gift tax.[57] Every NRA has a GST tax exemption of $5.49M.[58]

While the Treaty does afford some relief to NRAs, it does not rise to the level of U.S. citizens and residents. Even if the applicable exemptions are sufficient to avoid U.S. estate taxation, properly structured Wills are needed to prevent any U.S. situs assets from again being exposed to U.S. estate tax in the estate of the surviving spouse.

A comprehensive discussion of planning considerations for NRAs is beyond the scope of this outline. However, in the Canadian cross-border planning context, it should be noted that Canadian ownership of U.S. real property, while perhaps the most obvious trigger of the U.S. transfer tax regime, is only one consideration. Subtler U.S. connections should also be explored for possible U.S. transfer tax implications. An investment portfolio that includes stock in U.S. companies will trigger U.S. estate tax on death. Canadian parents of children living in the U.S., who may not have personal exposure themselves, should nonetheless consider the impact of U.S. estate tax on the children when structuring the children's inheritances. The failure to recognize a U.S. connection can have unintended and costly results. Identifying the U.S. tie and then planning for it is key.

B. Proposed Changes to the U.S. Transfer Tax System

As noted in the introduction to this outline, President Donald J. Trump and members of the U.S. Congress released the Framework on September 27, 2017, which advocated

for the repeal of the federal estate tax and the GST tax, among other changes to the U.S. federal tax system. Beyond advocating for the repeal of such taxes, details are relatively scant regarding the future of the U.S. federal transfer tax system. Notably, the Framework only advocates for the repeal of two of the three federal transfer taxes, i.e., the estate tax and the GST tax, and is completely silent on the third transfer tax, the gift tax.

The proposed changes only apply at the federal level. As summarized in a table below, several states have their own transfer tax regimes. While state transfer taxes are often linked to the federal transfer tax system at least conceptually, the current proposed changes only apply at the federal level. Thus, even if the federal estate and GST taxes are repealed, transfer taxes could (and presumably, would) continue to exist at the state level.

1. Repeal of the estate and GST taxes

The Framework advocates for the complete repeal of the estate tax and the GST tax. With no estate tax, an individual who would otherwise be subject to such tax if it was in effect could theoretically transfer an unlimited amount of property on his or her death without paying any transfer taxes. In addition, with no GST tax, if such a transfer was to a trust, the property transferred could theoretically be free from transfer taxes for as long such property could remain in trust under state law. In some states, property can remain in trust forever[59] and in others for up to 1,000 years.[60] In Florida, property can remain in trust for up to 360 years. Thus, with the repeal of the estate tax and the GST tax, vast sums of wealth could potentially be held in trust for many generations, and in some cases forever, without being subject to transfer taxes.

Yet as noted, details are scant here. It is not clear if the repealed estate tax would be replaced with a different type of tax. On the campaign trail, President Trump had proposed a capital gains tax for assets held until death and valued at more than $10M, which would be a system conceptually similar to the Canadian deemed disposition tax.[61] But if this is the case, presumably the current rules that provide for a step-up in basis for assets on an individual's death would have to be modified or eliminated. Under current law, property owned by an individual at death generally gets a step-up in basis to that property's fair market value as of the date of death.[62] An elimination or modification of the stepped-up basis rules, sometimes known collectively as the "Angel of Death," would represent a significant change from the current system.

However, at this stage, it is uncertain what the future has in store for the estate tax and the GST tax.

2. What about the gift tax?

As noted above, although the Framework advocates for the repeal of the estate and GST taxes, it is silent on the gift tax. This leaves significant uncertainty regarding the future of the gift tax, especially considering that the gift tax and the estate tax currently function as a "unified" tax regime, i.e., that lifetime taxable gifts that exceed the annual exclusion amount ultimately reduce the amount of property that can later pass free of estate tax on an individual's death. If just one half of this joint regime is repealed, i.e., the estate tax, it is unclear exactly how the gift tax would function on its own if it is not also repealed. Would there still be a lifetime

gift tax exemption ($5.49M in 2017)? Would all gifts be subject to tax? It is not possible to say at this stage.

Nevertheless, it should be noted that the gift tax may serve a purpose even without the estate tax. In addition to the transfer tax regime, the gift tax is also important to the U.S. income tax system both at the federal and state level. First, the gift tax prevents wealthy individuals in high federal tax brackets from gifting assets to family members in lower federal tax brackets, thereby reducing the total tax that a family can pay as a whole while preserving the same income level.[63] Without a gift tax to prevent such transfers between family members, it would be possible for wealthy families to game the income tax system by shifting assets among themselves, potentially paying less income tax as a result. In addition, the gift tax also protects the income tax systems of the various states by preventing gift transfers from individuals in high tax states (like New York) to individuals (or trusts) in low or no tax states (like Florida). Thus, it is not inconceivable that the gift tax could survive the repeal of the estate tax. But only time will tell.

C. Effects of Proposed Changes to Tax Law on Select Cross-Border Planning Techniques – Planning for Uncertainty

Even if the federal estate tax and GST tax are repealed, several cross-border planning techniques still provide valuable benefits for Canadian citizens and residents with U.S. connections, primarily in the areas of U.S. real property ownership and inheritance planning for U.S. based children of Canadians. Although avoidance of U.S. federal transfer taxes may be a primary motivation for implementing these techniques currently, other available benefits include creditor protection, U.S. probate avoidance, and protection against state transfer taxes. In

addition, these techniques can also be used to protect the inheritances of U.S. based children and grandchildren of wealthy Canadians.

1. Planning for ownership of US situs real property – does a residence trust still make sense if there is no US estate tax?

For many years, the residence trust has been the preferred US estate tax avoidance technique for married Canadians purchasing US real property. Typically**,** one spouse is the settlor/grantor of the trust and contributes all the funds towards the purchase of the property (the "grantor spouse"). The trust is for the benefit of that grantor's spouse (the "beneficiary spouse") and descendants, and the trust acquires the property. The trust generally provides that (1) someone other than the grantor act as Trustee (the grantor spouse MAY NOT be a Trustee), (2) the beneficiary spouse has lifetime rent-free use of the property (but may pay the expenses needed to maintain it), and (3) distributions from the trust may be made to the beneficiary spouse and/or descendants for health, education, maintenance and support in reasonable comfort (referred to in the US as an "ascertainable standard"). Optimally, the trust provides for the appointment of an independent trustee. The independent trustee has the ability to distribute income or capital of the trust for any reason, and the ability to decide to terminate the trust (which might be important given the Canadian "21 year" rule, for example). The grantor spouse may live in the property only at the "sufferance" of the beneficiary spouse (this is the actual terminology used by the IRS!), so that does not create a retained interest or prohibited "string" for US estate tax purposes.[64]

Logistically, a residence trust may pose problems if the property is already titled in the name of both spouses, or if neither spouse has a bank account in his or her own name.

Practically, this structure can be difficult if there is marital discord down the road, or if a beneficiary becomes a U.S. person. For singles, it is usually not an option at all.

But what if the U.S. estate tax goes away? Then the primary motivator for these trusts goes away too, right? Maybe, but there are other reasons to use a trust.

<u>Probate avoidance</u>. For the married couple, this is less compelling. With no federal estate tax, joint tenancy (or tenancy by the entireties, at it is known in Florida) is no longer taboo. But probate becomes an issue on the death of the survivor.

<u>Estate Tax: What? I thought it was repealed?</u> Though the U.S. federal estate tax may be repealed, some individual **states** continue to have a separate estate tax and/or inheritance tax. Happily, Florida does not, so that condo in Naples is safe. But the ski chalet in Ellicottville, New York is exposed. Planning techniques utilized to avoid federal transfer taxes can also be effective to avoid some state transfer taxes. A table listing the states that currently have their own transfer taxes is listed in Paragraph D, below.

<u>Creditor protection</u>. This may be particularly relevant if the clients rent the property while they are not using it, but it is also protects against spendthrift tendencies and overreaching spouses of adult children.

Even if a residence trust no longer makes sense, clients should consider additional planning to minimize administrative headaches. Having a separate Will to deal just with the U.S. property (the residence, its contents and any related “toys” like cars, boats and the like) is highly

recommended. Care should be taken to identify who may act as fiduciary. New York, for example, does not allow a non-resident fiduciary to serve without bond.

Finally, if your clients spend significant time in a U.S. jurisdiction, they should have U.S. powers of attorney and health care directives.

2. Planning for U.S. children/grandchildren

U.S. advisors assisting Canadian counsel with drafting Wills for high net worth Canadians are often charged with protecting the inheritance of U.S. children and grandchildren from U.S. transfer taxes. Typically, this involves a trust, either testamentary or *inter vivos,* and frequently the trust has dynastic, or generation-skipping, features. But even if the federal estate and GST taxes are repealed, there are still compelling reasons to use a trust (some of which were highlighted in the section on real property above):

- *Creditor Protection.* Although the trust assets will be available to be used for the beneficiary's benefit as well as for the benefit of his or her children and grandchildren, no creditor of theirs or of any of their children or grandchildren would be able to reach the assets held in an "inheritance" trust. Therefore, the beneficiary would be able to use the trust assets, for example, to buy a vacation home, and know that no claims against them or any member of their family would result in a lien against the home (as long as it is held in the trust.) Since the child (or grandchild, as the case may be) will be the primary beneficiary, holding title to such assets in the trust should be virtually transparent in terms of their use and enjoyment of such assets.
- *Continued Control*. A beneficiary would still be able to revise how the trust remainder would be distributed among family or other beneficiaries upon death (by including a limited testamentary power of appointment). Moreover, as long as the beneficiary is the trustee of the trust (which is permitted under U.S. tax laws), the beneficiary may determine the distributions to family members during his or her lifetime, as well as control investments.

- *Flexibility*. The trust is mobile. In other words, if a beneficiary moves, the trust may move with the beneficiary. Or the beneficiary may relocate it elsewhere if there should be some advantage. Also, the beneficiary may add, and then remove, a co-trustee.

- *U.S. State Estate Tax Exempt*. Even if the federal estate tax is repealed, a trust can be used to protect against state estate taxes. Although each beneficiary would have great access to the assets in the trust, the access is limited to what are known as ascertainable standards, which means that the value of the trust will be excluded from his or her personal estate upon his or her later death for state estate tax purposes. This is true even if the trust were to grow considerably in value. Accordingly, the beneficiary's children and grandchildren would inherit the benefits of this trust without any reduction for any U.S. state estate taxes.

In sum, with the repeal of the US federal estate tax, a large incentive for this type of planning goes away, but many clients may still find it compelling for the reasons discussed above.

D. Table Summarizing State Level Transfer Taxes

State	Exemption	Max Rate
Connecticut	$2,000,000	12%
Delaware	$5,490,000 (estate tax sunsets December 31, 2017)	16%
Washington, D.C.	$2,000,000	16%
Hawaii	Same as federal exemption	15.7%
Illinois	$4,000,000	16%
Iowa	Inheritance tax on transfers to others than descendants and ancestors	Varies depending on recipient (highest 15%)
Kentucky	Inheritance tax	Varies depending on recipient

State	Exemption	Max Rate
		(highest 16%)
Maine	$5,490,000	12%
Maryland	$3,000,000 estate tax and separate inheritance tax	16% estate; 10% inheritance
Massachusetts	$1,000,000	16%
Minnesota	$2,100,000	16%
Nebraska	Inheritance tax imposed at the county level	Varies depending on recipient (highest 18%)
New Jersey	$2,000,000 (estate tax is eliminated effective January 1, 2018) and separate inheritance tax (which will not be eliminated)	16% estate; 16% inheritance
New York	$5,250,000	16%
Oregon	$1,000,000	16%
Pennsylvania	Inheritance tax	Varies (15% highest)
Rhode Island	$1,515,156	16%
Vermont	$2,750,000	16%
Washington	$2,129,000	20%

[1] This paper only tangentially addresses state estate tax considerations. Many U.S. jurisdictions have their own estate or inheritance taxes separate from the federal transfer tax regime.

[2] "Uniform Framework for Fixing our Broken Tax Code," September 27, 2017.

[3] Julia Hirschfeld Davis and Alan Rappeport, "Trump Proposes the Most Sweeping Tax Overhaul in Decades," N.Y. Times, September 27, 2017 (accessed online).

[4] Internal Revenue Code of 1986, as amended (hereinafter "IRC") § 2001(a).

[5] IRC § 2031.

[6] IRC § 2040.

[7] IRC § 2042(1).

[8] IRC § 2309.

[9] IRC § 2041(a).

[10] IRC § 2038.

[11] IRC § 2036.

[12] IRC § 2037.

[13] IRC § 2040(b)(1).

[14] IRC § 2051.

[15] IRC §§ 2053, 2054, 2055, 2056.

[16] An additional 6-month extension is available, but the estate tax must be paid by the original 9-month filing due date.

[17] IRC § 2010(a).

[18] All amounts are in U.S. dollars.

[19] IRC § 2010(e).

[20] IRC § 2522(a); Reg. §25.2522 (a)-1.

[21] IRC § 2056.

[22] IRC § 2056(a)(7).

[23] IRC § 1014.

[24] IRC §§ 2001(b), 2502(a).

[25] IRC § 2503(b)(1), indexed for inflation.

[26] Unless spouses opt to “gift-split.”

[27] IRC § 2503(e)(2)(A) & (B).

[28] IRC § 2523(a).

[29] IRC § 2523(i).

[30] IRC § 2522.

[31] IRC § 1015.

[32] IRC § 2502(c).

[33] IRC § 2601.

[34] IRC §§ 2056(d)(1)(A), 2056(A).

[35] IRC § 2056(a)(1). Because of the requirement of a U.S. Trustee, the QDOT may not qualify as a Canadian resident trust, prohibiting a spousal rollover. However, a competent authority request can be made to treat the QDOT as a resident of Canada. U.S. – Canada Treaty, Article XXIXB, Paragraph 5.

[36] IRC § 2056(a)(1).

[37] IRC § 2056A(b)(3).

[38] IRC § 2056A(b)(1).

[39] IRC § 2040(a).

[40] U.S. – Canada Treaty, Article XXIXB, Paragraph 7.

[41] IRC § 2523(i)(2).

[42] IRC §§ 2101(a), 2103.

[43] IRC § 2104.

[44] There is an exception for "portfolio" debt, for example.

[45] IRC § 2105.

[46] IRC § 2105.

[47] IRC § 2102(b)(1).

[48] Treaty, Article XXIXB, Paragraph 2.

[49] IRC § 2106.

[50] Treaty, Article XXIXB, Paragraph 3.

[51] IRC § 2106(a)(2)(A).

[52] IRC § 2522(b).

[53] Treaty, Article XXIXB, Paragraph 6.

[54] IRC § 2511(a).

[55] In contrast, U.S. corporate stock is taxable as U.S. situs property for estate tax purposes.

[56] IRC § 2522(b).

[57] Reg. § 26.2663-2.

[58] Reg. § 26.2663-2(a).

[59] South Dakota

[60] Wyoming

[61] Allyson Versprille, "Six Burning Questions That Remain on Trump's Estate Tax Plans," Bloomberg BNA, December 28, 2016 (accessed online).

[62] IRC § 1014.

[63] Vidya Kauri, "Gaps In Trump-GOP Tax Plan Hint At Loss Current Benefits," Law 360, October 4, 2017 (accessed online).

[64] This means that if the parties separate or divorce, the beneficiary spouse may continue as a beneficiary and use the property to the exclusion of the grantor spouse. It is possible to avoid this result through proper drafting.

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TAB 11

Life Insurance Update for Trusts and Estates Practitioners

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DAY TWO
October 17, 2017

cpd Continuing Professional Development

Life Insurance Update for Trusts and Estates Practitioners

Florence Marino, B.A., LL.B., TEP, Assistant Vice-President Tax, Retirement & Estate Planning Services, Manulife

Introduction

This paper will focus on a life insurance update specific to estate planning and implementation areas of interest for trusts and estates practitioners – the practical stuff!. However, to start, it will address certain general updates regarding the tax and legal landscape for life insurance and highlight the general trends and developments relating to life insurance.

Update on the tax and legal landscape for life insurance

2017 Life insurance tax changes – The rubber has hit the road but the sky has not fallen

At last year's Trusts and Estates Summit Robin Goodman addressed the significant changes to the taxation of life insurance that took effect on January 1, 2017.[1] These changes are now in effect and her general observations regarding the impact of them have held true. Product modifications have resulted from compliance with the new tax regime, but these changes do not impact the overall viability of life insurance as a tool to provide risk protection, liquidity at death and continued tax benefits – tax-free death benefits and tax-sheltered accumulation.

What has changed is the maximum deposit limits and overall tax-sheltered accumulation limits for exempt policies[2] (generally, permanent life insurance products with cash values).

[1] Bill C-43, "A second Act to implement certain provisions of the budget tabled in Parliament February 11, 2014 and other measures (Economic Action Plan 2014 Act, No. 2)" received Royal assent December 16, 2014 and which contained the changes to the exempt test and life insurance policy tax rules with an effective date for these measures of January 1, 2017.

[2] The rules relating to exempt policies are set out in Regulations 306-310 of the Income Tax Act, R.S.C. 1985, c. 1 (5th Supplement), as amended, hereinafter referred to as the "Act". Unless otherwise stated, statutory references in this paper are to the Act. The income earned on the cash value within an exempt policy is exempt from accrual taxation – section 12.2 of the Act. However, tax may arise upon the disposition of an exempt policy pursuant to section 148 of the Act.

Depositing more into a permanent policy than to merely meet the contractually-specified policy costs can either accumulate with investment growth or purchase additional amounts of paid-up insurance. Where these additional deposits are intended to pay future policy costs and not to increase the death benefit payable under the policy, the new regime has brought about minor reductions in the maximum deposit limits. But where excess funding is intended to make a permanent increase in the death benefit payable, more material reductions in the permitted level of additional deposits have resulted from the new regime. This reduction has less of an impact on policies where premiums or cost of insurance rates run for the lifetime of the policy. On the other hand, policies that have limited-duration premiums or cost of insurance charges (for example, if "paid-up" in 10, 15, or 20 years) do see very material reductions in the ability of the policy to absorb excess funding.

These changes in the maximum accumulation permitted within exempt policies are largely the result of changes in the tax value or "reserve" ascribed to the policy. The new regime increases this tax reserve for most policies. This has the effect of increasing the "accumulating fund"[3] of the policy and generally shrinking the room for additional deposits. Certain policies attract a lower tax reserve than others and thereby have more room for excess funding. For example, products with increasing insurance costs or premiums have much smaller tax reserves under the new regime than products with level-for-life and limited-duration costs or premiums and therefore greater ability to accommodate additional deposits. Depending upon the importance placed on maximizing deposits by a client, different cost of insurance or premium options may be used than may have been the go-to approaches in the past.

This increase in tax reserve also results in smaller "net cost of pure insurance"[4] values in the calculation of the adjusted cost basis (ACB) of a policy and therefore larger ACB's that take longer to fall to a value of zero than under the previous tax regime. Like the changes in the maximum permitted deposits, the impact on ACB's is different for the various premium or cost of insurance options that are offered by insurance policies. Depending on the importance

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[3] Regulation 1401(3).
[4] Regulation 308. "Net cost of pure insurance" reduces the ACB of a policy and for post-2016 policies is based on a more modern mortality table (CIA mortality tables 1986-1992).

placed on minimizing (or maximizing) ACB by a client, different cost of insurance or premium options may be used than may have been the go-to approaches of the past. Generally, one would want to minimize ACB where a policy is corporately-held until death due to the fact that the ACB reduces the credit to the capital dividend account[5] (CDA). On the other hand, where cash value accumulations are intended to be withdrawn or policy loans taken at a later date, a higher ACB is beneficial.

In summary, although all products are affected by the changes brought in by the new regime, the degree of change is not consistent across all products' premium or cost-of-insurance options. Where the rubber will continue to hit the road is how well any given product design serves the needs of the client given their stated objectives. This has not changed!

Private company tax planning - Consultation paper and draft legislation – Insurance observations

On July 18, 2017, the Department of Finance released a discussion paper and draft legislation in relation to "Tax Planning Using Private Corporations"[6]. The proposals provide a consultation period ending on October 2, 2017. On September 25, 2017 the Canadian Tax Foundation (CTF) held a conference in which Department of Finance officials participated. There were no specific comments, positive or negative, from Finance relating to insurance. Any comments relevant to the topics discussed in this paper will be provided. Joan Jung's paper deals with the specifics of the proposals in detail. This paper will only address the potential implications for insurance of the proposals in the three main areas covered by them – income sprinkling, surplus stripping and passive investments. (This paper was written and submitted prior to the October 2, 2017 consultation deadline and therefore discusses the potential implications of the proposals as released.)

Overview

[5] Subsection 89(1) definition of "capital dividend account" of the Act.

[6] "Tax Planning Using Private Corporations", Department of Finance Canada, July 18, 2017, hereinafter referred to as "the proposals". This package contained a discussion paper, draft legislation with explanatory notes and a Technical Briefing slide deck.

Overall, the proposals represent a fundamental change to the taxation of private companies. They are complex and when added to the already complex rules involving recent changes to the taxation of inter-corporate dividends[7] and changes to the small business deduction that expanded the situations where the small business limit must be shared[8], tax compliance for small businesses will become even more tortuous and byzantine. Worse still, the proposals could have the effect of discouraging starting, owning and growing a business and impair business succession in Canada.

In general, from an insurance planning perspective, the proposals, if implemented, will bring about higher tax liabilities arising upon death. Life insurance is an obvious solution to provide needed liquidity at death. The more specific implications for insurance in relation to each of the areas of the proposals will be dealt with in turn.

Income Sprinkling

The proposals significantly expand the application and scope of the "kiddie tax"- tax on split income (TOSI), which taxes the recipient at the highest marginal tax rate on the "split income".[9] The proposals expand who the TOSI will apply to and the type of income the TOSI rules will apply to. "Reasonable" amounts (based on labour and capital contribution, risk assumed and total remuneration) received by adults (over 25, with 18-25 year-olds having to meet an even tougher standard) will be excluded, injecting significant uncertainty. They also address multiplication of the lifetime capital gains exemption (LCGE)[10], eliminating the LCGE on capital gains:

- that accrued before the taxation year in which the individual turns 18;
- if income on the property was subject to TOSI; or

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[7] Subsection 55(2) of the Act amended by 2016 Budget first bill C-15, S.C. 2016, c. 7 Royal assent June 22, 2016 for dividends received after April 20, 2015.
[8] Section 125 of the Act amendments throughout by 2016 Budget second bill C-29 S.C. 2016, c.12 Royal assent December 15, 2016.
[9] Section 120.4 of the Act. Supra note 6 the proposals add numerous definitions to subsection 120.4(1), new subsections (1.1), and replace (4) and (5), to be applicable to the 2018 taxation year. The way this legislation is drafted, the impugned income falls into "split income" first, then is exempted from split income ("excluded amount") if you are an adult, then is reincluded if you meet the definition of "split portion".
[10] Section 110.6.

- that accrued while the property was held by a trust (other than certain trusts).[11]

This would restrict the ability to claim the LCGE in many common tax and estate planning structures - for example, where a family trust holds the new common shares after an estate freeze.

If the proposals are implemented, in the future, if income cannot be efficiently distributed from the corporation, it could mean more funds are reinvested into the business, ultimately growing the value of the business and the capital gains tax liability at death. If use of the LCGE is also restricted, this may result in an even larger capital gains tax liability at death. Life insurance is an effective way to deliver the liquidity needed at death to fund potentially higher liabilities.

Surplus Stripping

In respect of surplus stripping, the proposals make changes to section 84.1 of the Act and introduce a new surplus-stripping anti-avoidance rule[12]. Both are effective as of July 18, 2017. Relevant to insurance and estate planning, the changes to section 84.1 appear to impact post-mortem "pipeline" planning.

In simple terms, pipeline planning addresses the double tax problem that results when a shareholder of a corporation dies and is deemed to have disposed of shares of the company and the assets of the company are later distributed to heirs. Pipeline planning preserves capital gains treatment upon the death of the taxpayer. To avoid double taxation of any future extraction of assets from the company, planning is undertaken to create a "pipeline" where the adjusted cost base of the shares that arose on the deemed disposition on death is converted

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[11] Supra note 6 the proposals add definitions, new subsections and make significant amendments to existing provisions to be applicable to the 2018 taxation year. An "eligible LCGE trust" (proposed new definition in subsection 110.6(1) of the Act) that is not subject to the proposed changes are: spousal or common-law partner trusts; alter-ego trusts or similar trusts settled for the exclusive benefit of the settlor during the settlor's lifetime (i.e. self-benefit trusts); certain employee share ownership trusts where the individual beneficiary is an arm's length employee of the employer sponsor of the arrangement.

[12] Supra note 6, proposed subsection 246.1 of the Act.

into a loan from the corporation that can be repaid without incurring further tax. Given that capital gains attract less tax than dividends, there has been a preference for pipeline planning in recent years. Existing pipeline planning that has not yet been completed (i.e. the promissory note has not yet been repaid) appear to be caught by the proposals resulting in the loan repayment receiving deemed dividend treatment, thus triggering double tax. (The Department of Finance expressed openness to consider transitional rules at the September 25, 2017 CTF conference.)

Another way to address the double tax problem described above is to redeem the shares within the first year of the estate and carry back the capital loss created on the redemption to the year of death to reduce the deceased's capital gain.[13] If available at all,[14] this results in one level of tax at dividend rates. As a result of the proposals, this form of post-mortem planning (if available at all) appears to be the only method of avoiding the double tax problem. Life insurance may be used to fund some or all of such a redemption or may provide funding for the tax liability in respect of dividend tax arising from the redemption[15]. In general, life insurance can improve the tax results of post-mortem planning[16]. However, assuming it is possible to use redemption and loss carry-back planning, it is important to note that the estate must be the "graduated rate estate" (GRE)[17] and the redemption must occur in the first year of the estate otherwise, there could again be, double tax. (At the CTF conference the Department of Finance expressed an openness to consider modifications to subsection 164(6) of the Act to allow more time to carry out the redemption.)

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[13] Subsection 164(6) of the Act.

[14] Some commentators have raised a concern regarding the application of the TOSI rules when layered on top of the existing rules in the Act and question if the TOSI rules operate such that there is no longer a gain in the deceased's terminal return against which the loss can be carried back pursuant to subsection 164(6). See Allan Lanthier, "Taxation of Private Corporations", Canadian Tax Highlights Vol. 25, Number 8, August 2017 at pg. 1 as follows: "Moreover, on a disposition of shares to a non-arm's length party, the entire capital gain is characterized as a taxable dividend if the shares give rise to split income. This provision effectively bars many intergenerational transfers of shares in a private corporation, and it denies access to post mortem planning under subsection 164(4)."

[15] Subsection 84(3) of the Act.

[16] This results from life insurance proceeds giving rise to a CDA credit, supra note 5, which may be paid in respect of the redemption dividend.

[17] Subsection 248(1) of the Act.

Once again, in general, life insurance may be a solution to provide liquidity to pay greater tax liabilities arising upon death – either because double tax cannot be solved or in conjunction with loss carry-back planning, if available.

The new anti-surplus-stripping anti-avoidance rule[18] can be interpreted broadly. It is unclear just how far it will be applied. The explanatory notes state that it is "intended to prevent the distribution of corporate surplus (in general, unrealized corporate value less liabilities) to an individual shareholder resident in Canada, which would otherwise be distributed as a taxable dividend, on a tax-reduced or tax-free basis in a non-arm's length context…"[19] Where this provision applies, it would cause a distribution of a capital dividend to be taxed as a taxable dividend. The proposed section has extremely broad and ambiguous wording and although it does not appear to be targeted at capital dividends arising from life insurance proceeds, this ambiguity causes some concern.

Could the mere payment of a capital dividend be caught? This would seem to be a tortured reading of the draft provision. Firstly, the provision requires that tax be avoided – in respect of a capital dividend itself there would not otherwise be any tax payable.

Also, the provision seems to require two separate and distinct events to occur: (1) an amount received or receivable by an individual, and (2) a different transaction or event than the amount in (1). The transaction or event in (2) must bring about or cause a reduction or disappearance of assets of the corporation so that the amount in (1) is taxed more favourably to the individual than it otherwise would have if the transaction or event in (2) had not occurred. (I'll refer to this as the purpose test.)

It is difficult to see how a capital dividend from life insurance proceeds could meet both tests. The life insurance proceeds would have increased the assets of the corporation. And, the corporation did not dispose of assets to cause a change in the tax result to the individual. Payment of a life insurance death benefit is not a disposition of the policy[20] (other than the

[18] Supra note 12.
[19] Supra note 6, Explanatory Notes at pg. 45.
[20] Subsection 148(9) definition of "disposition" at paragraph (j) of the Act.

payment of the fund value on first death under a multi-life policy in excess of certain limits[21]). It would be quite a stretch to say that dying should be included in "a transaction, event or series" that should be caught by this proposed rule.

However, there may be some insurance strategies that may be intended to be caught. The explanatory notes state, not dealing at arm's length includes "situations where an accommodating third party that purportedly deals at arm's length with the individual is used as an intermediary"[22] to make a payment of an amount. And they further state "the assets that could be reduced or disappear include assets acquired directly or indirectly in the series (e.g. cash received under a loan)".[23] Corporate-owned life insurance that is immediately leveraged by a shareholder of the corporation as collateral security for a personal borrowing where the borrowed funds are invested in shares with high paid-up capital or debt of the corporation and where the shares will be redeemed or the loan will be repaid on death, (particularly in a situation like that in the Golini case[24]), may be contemplated by these comments.

Other areas involving life insurance planning that could be caught by the broad language of subsection 246.1 may include:

- Buy-sell planning involving individual shareholders holding shares of an operating company (Opco) through their respective holding companies (Holdcos) where the sale of Opco shares results in a capital gain in the deceased's Holdco. The provision may deny the capital dividend arising from the CDA credit created on the capital gain, from being distributed tax-free to a shareholder. This may result in favouring a redemption of shares between Opco and Holdco instead of a cross-purchase. (At the CTF conference the Department of Finance expressed their view that section 246.1 is intended to apply to non-arm's length transactions and not to arm's length transactions. It is unclear to me why a non-arm's length buy-sell transaction should be affected

[21] Paragraph 148(2)(e) of the Act.
[22] Supra note 6 at pg. 46.
[23] Ibid. at pg. 47.
[24] Golini v. The Queen (2016) TCC 174.

particularly where there is a *bona fide* business arrangement with a buy-sell agreement for the sale of shares at fair market value?)

- The "50% solution". Insured share redemption may be subject to the stop-loss rules[25] where capital dividends that exceed certain limits are used on the redemption. Where the stop-loss rules apply, this would prevent all or a portion of a capital loss arising on a redemption of shares to be carried back against the deceased's capital gain on death. The 50% solution uses a portion of the CDA to the extent possible on the redemption without triggering stop-loss, resulting in one level of tax at dividend rates but with the use of some of the capital dividends in respect of the redemption. The remaining unused CDA credit remains in the corporation for the benefit of the surviving shareholder(s). In order to accomplish a partial distribution of the available CDA credit, the payment of a capital dividend is sometimes paid in respect of an increase in paid-up capital[26] for the amount of the desired amount of capital dividend to be employed, followed by a redemption of the shares. If the purpose test discussed above is met, the new subsection could cause the capital dividend portion to be taxed as a taxable dividend, essentially neutering this planning strategy.

In summary, provided that we see appropriate technical clarification to address the concern of the availability of this planning at all[27], loss carry-back planning will be the only method of avoiding double tax on death provided the estate is the GRE and does the planning within the first year of the estate (or any other period as may be specified, if made). This will give rise to dividend tax as opposed to capital gains tax, thus increasing the tax liabilities on death, with the potential for double tax if this cannot be accomplished. Therefore, the general outlook for insurance is that again, tax liabilities on death will likely be higher. Insurance to provide liquidity to pay higher liabilities on death is a possible solution. Insured share redemption will likely be the most tax-effective approach to post-mortem and buy-sell planning.

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[25] Subsections 112(3)-(3.2) of the Act.

[26] Subsection 84(1) of the Act deems a dividend to have been received on a PUC increase.

[27] Supra note 14.

One of the main issues in this period of uncertainty resulting from these rules is: should insurance be purchased personally or corporately? Clearly where there is a choice – there are personal funds and corporate funds to pay the costs of insurance - there is no harm in purchasing the insurance personally until the dust settles and we have greater clarity. However, if the need for insurance is corporate and the funds are in the corporation, the current uncertainty should not prevent valid business insurance planning to occur. The medical and financial underwriting process can take time and the health of an individual can change. Where there is a need for insurance, applying for and obtaining it should not be delayed due to the uncertainty around these proposals.

Passive investments

In relation to passive investment income the proposals express the concern that individuals who carry on a business through a corporation can leave their business income (which is very favourably taxed at the small business rate[28] or the general corporate rate[29]) in the corporation to make passive investments. Because of the difference in personal versus corporate tax rates, there is more available to invest from business income earned in a corporation than if that business income were earned by the individual and received as salary. The current system taxes passive investment income in a corporation at a rate approximating personal rates by imposing a refundable tax[30]. However, it does not align the amount available to invest within the corporation to that which would be the case if the business income were earned personally or taken as salary.

No draft legislation was released. Possible approaches discussed[31] would:

- replace the current system of refundable taxes with a non-refundable tax (generally equivalent to the top personal tax rate);
- eliminate the CDA credit on the non-taxable portion of capital gains;

[28] 10.5%-18.5% range across the provinces
[29] 26.5%-31% range across the provinces
[30] Subsection 129(3) of the Act.
[31] Supra note 6 at pg. 32-54.

- treat all dividends distributed as non-eligible dividends[32]; and
- apply on a "go-forward" basis.

Although life insurance is considered a "passive asset" for purposes of the active/passive asset tests relating to qualification for the LCGE[33], it would only produce passive investment income on a disposition of the policy. Dispositions include full or partial surrenders, policy loans, policy dividends and transfers of ownership that are not permitted a rollover.[34] A collateral assignment of a life insurance policy does not constitute a disposition[35] of a policy, nor does the payment of life insurance death benefits[36] in general. To the extent that after-tax profits are retained corporately and not reinvested in active business assets (and this would remain to be seen), corporate-owned life insurance may be an alternative to investments that give rise to passive investment income. However, it would be too speculative to say at this point that an insurance purchase decision should be motivated by these potential changes.

Genetic testing and underwriting – Bill S201

On May 4, 2017 Bill S-210 Genetic Non-Discrimination Act received Royal Assent. This legislation was the result of a private member's bill initiated by now-retired Senator James Cowan. The Bill was unanimously supported in the Senate and received overwhelming support in the House of Commons even though the Justice Minister, the Prime Minister and several provinces expressed the view that the Bill is unconstitutional. On June 8, 2017 the government of Quebec announced that it would launch a challenge at the Quebec Court of Appeal[37] to the constitutionality of the Bill and create a working group to consider the broad issue of the

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[32] Subsection 82(1) of the Act.
[33] Supra note 10. Question 32 at the 1988 Canadian Tax Foundation Roundtable confirmed the CRA view that life insurance would normally be considered a passive asset. See also #9310100 and #9310105.
[34] Supra note 20 paragraphs (a)-(e); paragraph 148(2)(a) of the Act.
[35] Ibid. at paragraph (f).
[36] Supra note 20.
[37] As of September 7, 2017, the BC Attorney General, Attorney General for the Federal Government, the Canadian Life and Health Insurance Association and the Canadian Coalition for Genetic Fairness have all asked for intervenor status.

appropriate privacy protections that should be afforded genetic information. In the interim, the law is in effect[38].

In general, this legislation prohibits any person from requiring that genetic tests be undergone[39] or demanding to see the results of genetic tests that an individual has undergone[40] when providing goods or services, entering into or continuing a contract or agreement or offering specific terms or conditions in a contract or agreement with an individual. Contravention is a criminal offense with significant consequences.[41]

Insurers have modified their applications and processes for claims adjudication to be in compliance with the law. At the same time, insurers themselves and the Canadian Life and Health Insurance Association (CLHIA) continue to engage with the provincial governments and insurance supervisors to educate them on the underwriting process and how insurance companies would, if permitted, gather, maintain and use an applicant's genetic testing information.

Even prior to the federal legislation, insurers did (and will) not require applicants to undergo genetic testing in order to purchase insurance. If an applicant has undergone previous testing, and has access to the results, then the insurer would ask that the applicant provide this information. Some genetic test results could actually be helpful to obtaining insurance (e.g. results that rule out specific genetic illnesses). Under the current law, insurers may accept genetic testing results from applicants if provided on a voluntary basis and with the applicant's written consent.

Access to an applicant's lifestyle and medical information, including genetic testing results, allow life insurance companies to avoid anti-selection (i.e. those who know they are more

[38] In a joint news release on May 5, 2017 from the Office of the Privacy Commissioner of Canada and the Canadian Human Rights Commissioner, Commissioner Therrien said "he expects organizations subject to Canada's federal private sector privacy law to re-examine their practices related to genetic tests and bring them in line with the new law. In light of Parliament's passage of S-201, organizations that require genetic test results as a condition of providing a good or service will also generally be considered in contravention of the Personal Information Protection and Electronic Documents Act (PIPEDA))."
[39] Subsection 3(1) of the Genetic Non-Discrimination Act, SC 2017, c. 3.
[40] Ibid. subsection 4(1).
[41] Supra note 39 section 7 provides fines of up to $1,000,000 and/or imprisonment for 5 years.

susceptible to an illness due to genetic testing requesting insurance without divulging this knowledge to the insurer) and price their products fairly. The ability for insurers to access medical information is permitted under Canadian law[42] and ensures that the market in Canada remains equitable and sustainable.[43] It is expected that the Quebec Court of Appeal will find the current law unconstitutional and that the issue of use of genetic information will be appropriately dealt with at the provincial level with the input of insurers and the CLHIA. The industry has voluntarily adopted a Code on Genetic Testing Information for Insurance Underwriting.[44]

Medical assistance in dying (MAID) – Life insurance contestability not an issue

As a result of the Supreme Court of Canada's unanimous decision in the Carter case[45] amendments to the Criminal Code[46] were made to decriminalize MAID.[47] The legislation sets out the requirements for the provision of MAID and establishes exemptions to various Criminal

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[42] Section 22 Human Rights Code, R.S.O. 1990, c. H.19; Collection, use and disclosure of personal information (including medical information) is governed by the Personal Information Protection and Electronic Documents Act (PIPEDA) S.C. 2000, c. 5. Insurers obtain consent to collect medical and other personal information from applicants for insurance. There are three main principles in PIPEDA that are relevant to insurance underwriting which are set out at Schedule 1 – The Consent Principle (4.3.3) affirms that an organization shall not require an individual to consent to the collection, use or disclosure of personal information beyond that required for an explicitly specified and legitimate purpose. The Limiting Collection Principle (4.4) limits collection to only that personal information which is necessary for purposes identified by the organization. The "reasonable person" provision (subsection 5(3)) limits the collection, use or disclosure of personal information "only for purposes that a reasonable person would consider are appropriate in the circumstances." In respect of genetic testing, the main issue is this reasonable person test. The Office of the Privacy Commissioner of Canada (OPC) issued a Policy statement on the use of genetic test results by life and health insurance companies on July 10, 2014. In this statement, the OPC stated: "Based on our analysis, it is not clear that the collection and use of genetic test results by insurance companies is demonstrably necessary, effective, proportionate or the least intrusive means of achieving the industry's objectives *at this time.*"

[43] Insurance companies rely on medical information, including genetic testing if permitted, to asses each applicant's risk and avoid anti-selection. Prohibiting insurers from accessing known genetic testing results may lead to: higher costs of insurance or premiums for all purchasers; not being able to offer cost of insurance rates or premiums that are fixed and guaranteed for the term of the contract; and, may make it more difficult to access other medical tests that contain genetic information (i.e. not all genetic findings come from genetic testing; routine testing for known familial illnesses such as blood testing and ultrasound can also identify genetic diseases) thus increasing the cost and time it takes to underwrite any given risk.

[44]https://www.clhia.ca/domino/html/clhia/clhia_lp4w_lnd_webstation.nsf/page/E79687482615DFA485257D5D00682400!OpenDocument

[45] Carter v. Canada (Attorney General), [2015] SCR 331.

[46] Criminal Code, R.S.C. 1985, c. C-46.

[47] Bill C-14, "An Act to amend the Criminal Code and to make related amendments to the Acts (medical assistance in dying)", S.C. 2016, c. 3., received Royal Assent June 17, 2016.

Code offences[48] for physicians, nurse practitioners, pharmacists and certain other persons who provide or assist in MAID. As the Carter case was going through the courts, Quebec was involved in a detailed study of end-of-life care which resulted in legislation that legalized MAID.[49] Ontario has passed legislation[50] confirming that assisted death will not adversely affect the status of a policy or the payment of a benefit which would otherwise be provided under a contract.

Generally, the payment of a death benefit will not occur under a life insurance contract in Canada if the insured person commits suicide within two years[51] of the policy being issued. Where an insured person dies as a result of a medically assisted death in accordance with the rules and processes set out by the appropriate government in relevant legislation, insurers will not consider the medically assisted death to be a "suicide" for purposes of life insurance. However, it should be noted that insurers will adjudicate any claim in accordance with other contract provisions that may be applicable. For example, any misrepresentation (innocent or fraudulent as those terms are interpreted under applicable provincial insurance legislation[52]) that may have been made in connection with the coverage, or any exclusions that were specifically included in the policy at the time the coverage was issued.[53]

Life insurance updates regarding estate planning and implementation areas of interest specific to trusts and estates practitioners

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[48] Supra note 46 sections 241(b) and 14.

[49] Bill 52 "An Act Respecting End-of-Life Care", R.S.Q., c S-32.0001, introduced on June 12, 2013 received Royal Assent on June 5, 2014

[50] Medical Assistance in Dying Statute Law Amendment Act, 2017, R.S.O. 2017, c.7 came into force May 10, 2017.

[51] Most policies have a two-year suicide exclusion, others a one-year exclusion or none at all, and a handful may bar suicide during the entire term of the policy. The number of MAID cases falling within the typical two-year exclusion will be few since (unless there is misrepresentation in applying for coverage) there would likely be very few people who will be healthy enough to be medically underwritten and then find themselves within the first two years of coverage to be suffering a "grievous and irremediable condition" as required in the Criminal Code, supra note 48.

[52] Sections 183-184 Insurance Act, R.S.O. 1990, c. I.8, hereinafter referred to as the Insurance Act.

[53] For example, an insurer would determine if the underlying cause of death was an excluded condition and the claim would not have been payable, not by reason of MAID but because the illness from which the person was suffering and led to the person seeking MAID was excluded, or if there was a failure to disclose a pre-existing condition.

Insurance trusts as Qualified Disability Trusts

The fundamental changes made to the taxation of testamentary trusts effective January 1, 2016[54] created new tax concepts meant to limit the types of trusts that are permitted to benefit from graduated rate taxation. Only two categories of trusts are permitted this luxury – the GRE[55] and a "qualified disability trust" (QDT)[56]. To meet the requirements, a QDT must:

- at the end of the trust year, be a "testamentary trust"[57] that arose in consequence of a particular individual's death[58];
- be resident in Canada for the trust year[59];
- elect jointly with one or more beneficiaries named in the trust who qualifies for the disability tax credit[60] for the individual's taxation year in which the trust year ends and who does not jointly elect with any other trust[61].

While all of the criteria are relevant in qualifying as a QDT, the aspect relevant to life insurance planning relates to the qualification of so called, "insurance trusts", as testamentary trusts. In the "good old days" where qualification as a testamentary trust brought on graduated rate taxation for all testamentary trusts, the qualification as such was particularly important. It was in this context where the "testamentary trust-ness" of life insurance trusts was established.

An insurance trust is created on and in consequence of an individual's death by virtue of a declaration[62] in favour of a beneficiary[63] for which a trustee is appointed[64]. Such a declaration may be made in a will or any other written instrument (including in the policy contract - the application for insurance forms part of the policy contract - or on the insurer's beneficiary

[54] Supra note 1, with an effective date for testamentary trust measures of 2016 and later taxation years.
[55] Supra note 17.
[56] Subsection 122(3) of the Act.
[57] Subsection 108(1) of the Act.
[58] Supra note 56 at subparagraph (a)(i) of the definition.
[59] Ibid at subparagraph (a)(ii) of the definition.
[60] Subparagraphs 118.3(1)(a) to (b) of the Act.
[61] Supra note 56 at subparagraph (a)(iii) and paragraph (b) of the definition.
[62] Insurance Act section 171 definition of "declaration".
[63] Ibid., definition of "beneficiary".
[64] Subsection 193(1) Insurance Act.

designation form). The instrument must be signed by the policy owner and identify the contract or describe the insurance or insurance fund or part thereof to which the declaration relates. On death, the life insurance proceeds paid pursuant to such a declaration pass outside of and do not form part of the estate creating a separate insurance trust notwithstanding that the trustee of this trust may be the same person as the estate trustee.

The Canada Revenue Agency (CRA) has confirmed that a trust funded from the proceeds of life insurance owned by an individual on that individual's death whose terms were established while the individual is alive, within or separate from a will, is viewed as a testamentary trust.[65] The policy owner is the person legally entitled to name a beneficiary and to direct the payment of the proceeds into the trust, thereby, creating the trust. This trust does not arise from the estate even if its terms are captured in the same instrument. Therefore, there is the possibility of there being two testamentary trusts which qualify for graduated rate taxation, at least for as long as the estate qualifies as the GRE!

Another aspect of QDT qualification of interest is the possibility of life insurance proceeds being paid to an existing testamentary trust which otherwise qualifies as a QDT. The language of the definition of the term "testamentary trust"[66] appears to permit the contribution to an existing testamentary trust from an individual other than the one creating the trust, as long as the contribution was the result of death. The specific language is as follows:

> …a trust that arose on and as a consequence of the death of an individual… other than…
> (b) a trust created after November 12, 1981 if, before the end of the taxation year, property has been contributed to the trust otherwise than by an individual on or after the individual's death and as a consequence thereof….[67]

In prior commentary, the CRA confirmed that an existing testamentary trust created on the first death of a husband (Mr. A) and wife (Mrs. A) retained its testamentary trust status

[65] CRA technical interpretation #9625975, dated October 7, 1996, # 9605575 dated December 17, 1996, and #2009-0350811E5 dated January 6, 2011.
[66] Supra note 57.
[67] Ibid.

notwithstanding that an insurance trust declaration was made in favour of the existing testamentary trust because the insurance proceeds were received on the second death by virtue of the death of last-to-die.[68] In particular, the CRA stated:

> Based on the wording in paragraph (b) of the testamentary trust definition, it appears that the Act contemplates the possibility of certain contributions to an existing testamentary trust by an individual other than the individual on whose death the trust first arose (i.e. as long as the subsequent contribution is as a consequence of the death of the contributor). It is worth noting that the points raised in document 2010-0358654IE5[69], referred to in your question remain valid. However, if,
>
> - immediately before the death of Mrs. A the trust was a testamentary trust,
> - the facts lead to a conclusion that Mrs. A was the sole policyholder[70] after the death of Mr. A, and
> - the contribution occurs as a consequence of death,
>
> then in our view, the receipt of the insurance proceeds on her death would not result in a loss of testamentary status of the trust.[71]

From an insurance perspective, this could mean that an individual (who is both the owner and life insured) can designate a beneficiary causing insurance proceeds to fall into a newly created testamentary insurance trust on their death or into someone else's existing testamentary trust

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[68] #2012-0435701C6 May 2012 CALU CRA Roundtable Question 4.2.

[69] This technical interpretation dealt with spousal trusts set up in dual wills and the designation of life insurance proceeds in favour of the trustees of these trusts. Testamentary trust status could be impacted in this case if "the insured has not appointed the named persons in the insurance designation in their capacity as trustees of the estate or where the policyholder was not the taxpayer." It is clear that a separate insurance trust created pursuant to an insurance declaration cannot qualify as a testamentary spouse trust because such a trust must be created by the will of the taxpayer (paragraph 104(4)(a) of the Act).

[70] Two prior technical interpretations specifically dealt with this question. #2008-0270421C6 May 2012 CALU CRA Roundtable Question 5 and #2008-0278801C6 June 2012 STEP CRA Roundtable Question 2. In both of these responses, the CRA confirmed that: "in the case of a joint-last-to-die life insurance policy where the only amount that is payable to the trust under the policy is paid on the death of the last of the two persons insured under the policy, our position would be the same – that is, a trust created from the receipt of the proceeds of such a policy will not lose its testamentary trust status solely by reason of the receipt of the proceeds of the life insurance policy provided the life insurance policy is owned by the individual who survives the other immediately before his or her death and the policy qualifies as a testamentary instrument of that person at the time."

[71] Supra note 68.

at the time of the insured's death. This could be particularly interesting in the QDT context since only one trust may qualify as such for an electing beneficiary.

A QDT may have been established on the first death of Mom and Dad arising from the will of the first to die of Mom and Dad. Where Mom owns a policy on her own life and Dad predeceases her, she might choose to have the proceeds payable to Dad's existing testamentary trust (qualifying as the QDT) for the benefit of their disabled child. If Dad created a testamentary insurance trust on his death, this trust could be the operative QDT trust and be a trust into which Mom's life insurance proceeds could flow at the time of her death. If this works for insurance, why can't it work for a specific testamentary gift in a will that is made payable to an existing testamentary trust for a disabled person which is the one operative QDT?

Although it was confirmed that a trust settled with the proceeds of a jointly-owned last-to-die life insurance policy on the joint owners' lives, qualifies as a testamentary trust where the beneficiary designation was made by the owners jointly and the surviving owner made no changes to the designation after the death of the first owner and life insured, the CRA differentiated the situation where the fund or cash value is paid on the *first* death under a joint last-to-die policy, to an existing testamentary trust, finding that this would impact the testamentary trust status of the trust.[72] This distinction makes sense because although the fund value would be payable on the death of an individual, it would be paid pursuant to a declaration/designation made by a policy owner who is at the time of the first death, still alive. The ultimate death benefit would be payable on the death of the *last*-to-die and this still would not yet have occurred.

Charitable gifts by direct designation under a life insurance policy

The tax changes applicable to testamentary trusts also brought in changes to the use of charitable donation tax credits at death. In general, under the new estate donation rules where a gift is made by will, by a direct designation under a life insurance policy, RRSP, RRIF or TFSA or by the estate, the gift is deemed to be made by the estate (and no other taxpayer, i.e. not the

[72] Ibid. Question 4.1.

individual) at the time the property is transferred to the charity (and at no other time, e.g. not at death).[73] This establishes for all estates (whether the estate is the GRE or not) who is seen to have given the gift and the timing of that gift.

If a gift is made by the estate and the estate is the GRE at the time, or would otherwise meet the requirements to be a GRE but the 36-month period has been exceeded and the gift is made within 60 months of death, the executor will have the flexibility to claim these donations among and up to:

- 100% of the net income in the deceased's last two taxation years;
- 75% of the net income in the year of the gift or in the 5 years (10 years for ecological gifts) following the year of the gift; or
- 75% of the net income of a prior taxation year of the GRE.[74]

If the gift does not qualify as a gift by a GRE, the executor can only claim donations up to 75% of the net income in the year of the gift or in the 5 years (10 years for ecological gifts) following the year of the gift.[75]

When these measures were first introduced, the period of time to give gifts at death and benefit from the new flexibility only contemplated the maximum 36-month period of the GRE. The extension of the timeline to 60 months[76] was a welcome development. Even with the extended timeframe, there is still a lingering concern that a gift may not be able to be made within the timeframe.

Also of importance is the fact that other tax benefits arising from charitable giving also hinge on the estate qualifying as the GRE. For example, where a gift of publicly listed securities (which include mutual funds and segregated fund contracts) is made by an estate that is a GRE at the time or would otherwise meet the requirements of a GRE but the 36-month period has been

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[73] Subsections 118.1(4.1)-(5.2) of the Act.
[74] Subsection 118.1(1) of the Act definitions of "total charitable gifts", "total cultural gifts" and "total ecological gifts".
[75] Ibid.
[76] Bill C-29 Budget Implementation Act, 2016, No.2, Royal Assent December 15, 2016.

exceeded and the gift is made within 60 months of death, this allows the deceased individual to have a nil inclusion rate for purposes of computing the capital gain on death.[77] So not only is there a credit to offset taxes on death, any capital gain from the disposition of the publicly listed securities is not included in income on the deemed disposition on the death of the individual.[78]

What happens where an estate cannot make the gift in time? If a gift is not made in time, the flexibility described above is lost and for gifts of publicly listed securities, the benefit of a nil inclusion rate would also be lost. Delay in the administration of an estate beyond 60 months could be caused by:

- the probate process;
- dependent's relief claims;
- creditor claims;
- income tax clearance process;
- complex estates;
- illiquid assets;
- challenges to the validity of the will;
- estate litigation.

Since gifts by direct designation qualify as estate gifts, clients may wish to plan to make charitable gifts at death using life insurance by direct beneficiary designation to a charity instead of making specific bequests or gifts of some, or all of, the residue of their estate to enable a speedier gift. In general, life insurance claims are paid promptly upon receipt of all claims documents[79] – normally well within any 36 or, indeed, 60-month period. The requirements for direct designations[80] of life insurance are as follows:

[77] Paragraph 38(a.1) of the Act.
[78] Subsection 70(5) of the Act.
[79] Subsection 203(1) Insurance Act provides for payment within 30 days of receipt of "sufficient evidence".
[80] Subsection 118.1(5.2) of the Act.

- a transfer is made as a consequence of death of an individual, solely because of the obligations under a life insurance policy on the life of the donor;
- the individual's consent would have been required to change the recipient (i.e. the donor owns the policy)[81];
- the charity is neither owner nor assignee of the individual's interest in the policy.

It should be noted that direct designations were not always considered gifts. Prior to the enactment of 118.1 (5.2) of the Act,[82] where a charity was named as beneficiary under a life insurance policy, the death benefit was viewed as being received by operation of contract – i.e. "an obligation on the part of the insurer and not to be considered as a gift on the part of the person who bore the cost of the premiums."[83]

It is important to note that if a direct designation is used in respect of a corporate-owned policy, there would be no gift as the operation of the contract would deliver the death benefit proceeds to the charity. Worse still, there would be no capital dividend account[84] credit for the life insurance proceeds to the private corporation since the corporation would not have been designated as the beneficiary under the policy. A better solution would be for the corporation to receive the death benefit proceeds as beneficiary under the policy and for the corporation to make a gift of the life insurance proceeds.

Estate settlement where a corporate-owned life insurance policy is used as collateral security for a personal (shareholder) borrowing

Life insurance may be used as collateral security for a borrowing. In most cases, the policy owner providing the security would be the borrower. However, there are some situations in which a shareholder may borrow money using an asset of a private corporation that they wholly own or control as security for a personal loan. That asset may be a corporate-owned life

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[81] If the charity is irrevocably designated, this does not cause this requirement not to be met. See CRA technical interpretation # 2004-65451C6 CALU CRA Roundtable Question 7, May 2004 .
[82] Added by Bill C-22 (Part I), Royal Assent June 14,2001 effective in respect of deaths that occur after 1998, and amended by Bill C-33, Royal Assent May 13, 2005.
[83] #2000-0054467 dated December 19, 2000 (unofficial English translation).
[84] Supra note 5.

insurance policy. There have always been many issues to consider when utilizing this approach and the potential issues have been increasing with recent tax changes and developments.[85] One of the more significant issues to consider is whether this structure gives rise to a shareholder benefit.[86] Robin Goodman presented a paper at last year's Summit which, in the Caselaw Update portion, discussed the Golini case[87] which found that the shareholder had to bring into income an immediate shareholder benefit in respect of such a borrowing. This case is currently under appeal.

In addition to the potential for an immediate shareholder benefit, there is the potential that a shareholder benefit could arise on death where the personal borrowing is repaid directly with the corporate-owned life insurance proceeds. There are several cases where a shareholder benefit was found to exist for the amount paid where a corporation had repaid principal or interest in respect of a loan incurred by a shareholder or by a relative of the shareholder.[88]

When a life insurance policy is collaterally assigned to a lender, at death, the insurer will generally confirm the identity of the lending institution and the amount of proceeds to which the lender is entitled and pay this amount directly to the lender with the remainder paid to the beneficiary under the policy. Practices may vary from insurer to insurer. The proceeds (one cheque) may be made payable to both the collateral assignee and the beneficiary. Where a life insurance policy is collaterally assigned by a corporation to secure a shareholder's borrowing, the direct payment of proceeds to the lender may result in a taxable shareholder benefit if steps are not taken by the estate trustee and the corporation to avoid the direct payment of the deceased individual's debt with the life insurance proceeds.

If the borrower's estate repays the loan prior to the life insurance proceeds being paid to the collateral assignee then all of the proceeds would be paid to the corporation (as beneficiary).

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[85] See discussion of proposed subsection 246.1 of the Act and related explanatory notes supra notes 22 and 23; see also "back-to-back loan rules" (subsections 15(2.16-(2.192) of the Act which may also apply to shareholder borrowing structures.
[86] Subsection 15(1) of the Act.
[87] Supra note 24.
[88] See Riddell v. M.N.R., {1986} 1 CTC 2500 (T.C.C.), Kaufman v. M.N.R., [1987] 2 CTC 2028 (T.C.C.), and Davisson v. R, [2000] 3 C.T.C. 2576 (T.C.C.).

The corporation could then pay a capital dividend[89] to the estate to provide the funds to replenish the funds used by the estate to make the repayment. However, the estate trustee may not be in a position to repay the loan. Alternatively, if the estate is able to provide sufficient, liquid, alternative collateral security to the lender, the lender may be willing to release its collateral assignment of the policy, which would allow the life insurance proceeds to be paid to the corporation (as beneficiary) and pay a capital dividend in the manner described above to repay the debt and the lender could then release the alternate security provided. However, the lender may require that the will be probated prior to accepting other security.

Another method would be for the estate to provide a demand promissory note to the corporation for the amount of the personal debt and, in exchange, the corporation agrees to repay the loan to the lender by directing the insurer to pay the proceeds to the lender in the amount of the personal debt. The corporation would then pay a capital dividend to the estate which can be used to repay the promissory note it provided to the estate.

Where corporate life insurance is collaterally assigned to secure a personal debt of a shareholder, at the time of death, it is important for the corporation and the estate of the shareholder to be aware of the potential for a shareholder benefit and to take steps to ensure the amount repaid does not give rise to a shareholder benefit in the estate. Since the claims process is generally quick[90], it is possible that the claim could be paid directly from the life insurance proceeds without intervening steps taking place. It is therefore important to ensure that information relating to the proposed process at death be maintained with the policy so that policy owner corporation and the estate trustee can work together with the lender to take the necessary steps at the time.

Transfer of a life insurance policy on death of the owner – Unexpected tax traps

A disposition of an interest in a life insurance policy generally refers to any transaction in which the interest is transferred to another party. This includes an absolute assignment of the

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[89] Subsection 83(2) of the Act.
[90] Supra note 79.

interest, whether by way of gift or sale. It also includes a transfer of an interest in a policy that occurs on the death of the policyholder where the life insured is someone other than the policyholder. Note that at death, where the policyholder is not the life insured, and where there is no successor owner[91] designated, the policy passes through the estate. Whether the policy is dealt with specifically in the will or forms part of the residue of the estate, there will technically be two transfers: a transfer to the estate at death resulting in a disposition to the deceased, and a second transfer from the estate to the beneficiary. In practical terms, if the person entitled to the policy via the will is a spouse, it is possible that these transfers would occur on a rollover basis.[92]

The Act further defines the term "disposition" as it relates to an interest in a life insurance policy to include, *inter alia,* a disposition of the interest by operation of law only[93]. A disposition by operation of law would generally arise when "a right or liability has been created for a party, irrespective of the intent of that party, because it is dictated by existing legal principles."[94] Operation of law, in respect of a life insurance policy, could bring about the termination, surrender or conveyance of the policy. Examples of dispositions by operation of law of an interest in a life insurance policy would include: voiding a policy, seizure of a policy, transfer of a policy under the laws of intestacy or by right of survivorship under joint tenancy.

What are the tax consequences on disposition? In general, the "proceeds of the disposition"[95] in excess of the policy's ACB[96] would be reported on a T5 slip and included in the income of the policyholder as ordinary income. If a policyholder disposes of his or her interest in a policy by way of gift (either during life or by way of will), where a transfer occurs by operation of law only

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[91] Subsection 199(1) Insurance Act.
[92] Subsection 148(8.2) of the Act provides that "where in consequence of the death of a policyholder who was resident in Canada immediately before the policyholder's death, an interest of the policyholder in a life insurance policy… is transferred *or distributed* to the policyholder's spouse or common-law partner who was resident in Canada immediately before the death, unless an election is made… to have this subsection not apply, the interest shall be deemed to have been disposed of by the policyholder immediately before the death for proceeds of the disposition equal to the adjusted cost basis to the policyholder of the interest immediately before the transfer and to have been acquired by the spouse or common-law partner at a cost equal to those proceeds."
[93] Supra note 20 at paragraph (d).
[94] https://en.wikipedia.org/Operation_of_law.
[95] Subsection 148(9) of the Act definition of "proceeds of the disposition".
[96] Ibid. definition of "adjusted cost basis".

to any person, or any transfer is made to a person with whom the transferor is not dealing at arm's length, the proceeds of the disposition are deemed to be equal to the greatest of: the ACB; the cash surrender value of the interest in the policy; and, the fair market value of consideration given in respect of the transfer.[97] In general, no consideration would be given in the estates context for the transfer so that there would only be a T5 issued if the greatest of number is the cash surrender value.

In addition, the Act provides for automatic rollovers of an interest in a life insurance policy in limited circumstances. Where a rollover applies the transferor will be deemed to have disposed of the life insurance policy for proceeds of disposition equal to the ACB of the policy. The recipient will be deemed to have acquired the interest in the policy at a cost equal to those proceeds.

Relevant to the estates context, a tax-free rollover is permitted on a transfer to a spouse or common-law partner at death[98]. Another rollover provision involving a transfer to a child, grandchild or great grandchild ("the child rollover")[99] in certain limited circumstances may also apply. In the estates context, the main limitation of the child rollover is that it does not contemplate a transfer other than directly by the policyholder to a child such that it cannot pass via the owner's will and qualify for the rollover.[100] However, where a successor owner designation[101] is made in respect of a policy which otherwise meets the child rollover requirements, it will qualify for the rollover.[102]

Where a policy has cash value, there are some unexpected tax traps that can cause an income inclusion to the deceased/estate[103] upon the transfer of a policy on death. These would include the following:

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[97] Subsection 148(7) of the Act.
[98] Supra note 92.
[99] Subsection 148(8) of the Act. This subsection has numerous requirements that may not be satisfied resulting in the application of subsection 148(7) of the Act instead of rollover treatment.
[100] See CRA technical interpretation #9433865, dated February 15, 1995.
[101] Supra note 91.
[102] See CRA technical interpretation #9618075, dated September 3, 1996.
[103] Practice varies among insurers whether a T5 is issued in the name of the deceased or to the estate of the deceased.

- a transfer on death via successor owner designation or via a will to a former spouse (often the former spouse may be the life insured under the policy);
- a policy held by siblings as joint tenants on the life of their parent (for example, to pay tax liabilities arising on the death of the parent for a cottage property) where one (or more) of the siblings predeceases the parent;
- the transfer of a joint last-to-die policy that is jointly owned by spouses who are no longer residents of Canada at the time of the first death;
- as noted above, a transfer of a policy on a child, grandchild or great-grandchild on death of the parent, grandparent or great-grandparent to a child, grandchild or great-grandchild that is not pursuant to a successor owner designation.

Life insurance claims and payments into court – Practical items and reminders

The Insurance Act entitles an insurer to be discharged in respect of the amount paid where a payment is made into court.[104] It provides the circumstances under which the insurer can pay amounts into court.[105] Where two or more people have advanced claims for the insurance proceeds and it is not obvious on its face that the claims have no merit, insurers will not act as a judge and adjudicate the merits of competing claims. Insurers are not authorized to adjudicate, as a judge is. Information presented to an insurer by claimants is not tested by cross-examination or examination for discovery and may not be complete.

Payment into court also occurs if a beneficiary entitled to proceeds can't be located or if there is no person entitled to proceeds. If there is no one capable of giving and authorized to give a valid discharge, for example the beneficiary is not mentally competent and there is no one appointed to act on the person's behalf, a payment into court can be expected. In the latter

[104] Subsection 214(3) Insurance Act.
[105] Ibid. Subsection 214 (1) provides: "Where an insurer admits liability for insurance money and it appears to the insurer that, (a) there are adverse claimants; (b) the whereabouts of a person entitled is unknown; (c) there is no persona capable of giving a valid discharge therefor, who is willing to do so; (d) there is no person entitled to the insurance money; or (e) the person to whom the insurance money is payable would be disentitled on public policy or other grounds, the insurer may, at any time, after thirty days from the date of the happening of the event upon which the insurance money becomes payable, apply to the court without notice for an order for payment of the money into court…"

context it should be noted that the Insurance Act also provides the insurer with the ability to pay into court if money is payable to a minor[106]. Notwithstanding the pleas from parents or even lawyers (who sometimes ask to circumvent this legislative framework if an indemnity is provided) if no guardian of property for the minor has been appointed by a court, insurers will pay into court to the credit of the minor and the Public Guardian and Trustee would be responsible for managing the funds. Finally, payment into court will be made if the person who is entitled to receive the proceeds is disentitled on public policy or other grounds, for example, the beneficiary has murdered the life insured.

As noted earlier, the claims process can be speedy. This is due to the fact that it is incumbent upon insurers to pay death claims as soon as there is "sufficient evidence" to make a claim payment.[107] Therefore, where there is any question or concern of an adverse claim or any of the other circumstances under which an insurer is permitted to make a payment into court, the tendency will be for insurers to pay amounts into court as soon as these circumstances become evident so that there is no delay.

Conclusion

This paper was intended to provide mix of information – larger legislative trends impacting life insurance and related planning and practical matters of interest to estates and trusts practitioners in the trenches.

[106] Subsections 220 (1)-(4) Insurance Act.
[107] Supra note 79.

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TAB 12

20TH ANNUAL Estates and Trusts Summit

Disclosure of Wills, File Storage, What to Include In the File, Etc. PANEL MATERIALS

Jordan Atin, C.S., TEP
Atin Professional Corporation

Sean Lawler
Shibley Righton LLP

Susan Sack
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DAY TWO
October 17, 2017

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http://www.practicepro.ca/wp-content/uploads/2017/08/Landmines4Lawyers.pdf

Landmines for lawyers when drafting wills

When it comes to mistakes and claims, the Achilles heel for lawyers in the wills and estates area is drafting wills: Making will-drafting errors – either because of poor communication, inadequate discovery or errors in law – is the single most common issue in claims reported in this area of law. In many cases, the mistake which led to the claim could have been prevented.

Communication

Communication – or lack thereof – remains the number one reason for claims reported in the wills and estates area. Most communication errors arise from a failure to follow a client's instructions, a failure to obtain consent, or a failure to inform the client.

In the area of will-drafting, commonly reported errors which originate from communication or lack thereof can include:

- failure to compare the lawyer's will instruction notes with the will;
- failure to confirm the assets and debts of the testator, and;
- failure to confirm the marital status of the testator.

Many of these errors can be easily avoided: For example, have someone else review the will to avoid a problem arising out of a failure to follow client instructions. Use checklists or reporting letters that confirm drafting instructions to avoid an error arising from a failure to inquire about assets or the marital status of the testator.

A good way to avoid communication errors in will-drafting: Document the will drafting instructions, review and confirm the instructions with the testator when the will is drafted, and do a final review of the instructions when the will drafting is completed.

Inadequate investigation

Inadequate investigation is a broad category; typical errors include those arising from a failure to properly inquire about the testamentary capacity of the testator and the failure to properly inquire as to the personal circumstances of the testator.

It is your responsibility, as the lawyer preparing the will, to ensure that the testator has the requisite testamentary capacity. The solicitor should ask the testator open-ended questions to determine testamentary capacity. As well, inquiries should be made about any medical conditions to assess if there is any mental or physical impairment.

If you are concerned about capacity, consider obtaining an expert opinion from an assessor or, at a minimum, speak to the family doctor and obtain a medical report. Along with preparing the will, prepare a memo on your observations of the physical and mental state of the testator.

As part of your initial will interview, obtain a list of assets and liabilities of the testator. You should also, where possible, verify ownership and registration of assets as well as any

designated beneficiary of those assets. Special attention should be paid to life insurance, pension plans, RRSP and RRIFs.

Finally, the solicitor should inquire and confirm marital status of the testator and any obligations to dependents. If possible, the lawyer should obtain and review a copy of any separation agreement or marriage contract which may give rise to those obligations.

Know the law

Legal errors arising from lack of knowledge of the law are more prevalent in the wills and estates field than in many other areas of the law. Errors range from the mundane (e.g., failure to properly execute a will) to the more complex (e.g., errors in estate planning).

Some of the most expensive claims for LAWPRO in the wills and estates field arise from errors in estate planning. These errors often occur because the lawyer preparing the estate plan does not understand or have the expertise to properly execute it.

Complex estate planning requires a thorough understanding of corporate and tax law. If you don't have the expertise in these areas, please refer the matter to a lawyer who does. If an accountant asks you to draft certain documents and you don't understand the implications of the documents being prepared, send the matter elsewhere. Asserting that you were merely a scribe is no defence to a negligence claim.

When undertaking any type of estate planning it is imperative that the lawyer confirm how assets are held. Do not rely on the testator to properly describe corporate assets or the title to a piece of land. For example, the lawyer has an obligation where practicable to confirm that real property forms part of the testator's estate and is not registered in the name of a corporation. Similarly, the solicitor should confirm ownership registration of shares and other assets (see *Willhelm v. Hickson* (1999),183 D.L.R. (4th) 45 (Sask. C.A.).

Finally, in light of the decision in *Pecore v. Pecore* (2005), 19 E.T.T. (3d) 162, (Ont.C.A.), [2007] 1 S.C.R. 795, it is crucial that you discuss the implication of joint ownership.

Standard of care
Developments in the current law of solicitor's negligence can be traced to the decision of the House of Lords in *White v. Jones*, [1995] 2 A.C. 207. In *White v. Jones,* the court created a remedy for the benefit of disappointed beneficiaries. The new remedy was necessary because there is no privity of contract between a beneficiary and the lawyer drafting the will who makes an error depriving the beneficiary of his or her inheritance.

In W*hite v. Jones* the court created a duty of care owed by the solicitor to the disappointed beneficiary to fill a "lacuna in the law." The rationale for the duty of care is that it is reasonably foreseeable to the solicitor that the beneficiaries will suffer a loss if the will is not prepared properly or in a timely manner. The solicitor's liability arises from the solicitor's assumption of responsibility to implement the testator's wishes by preparing the will properly and the absence

of a basis, for the disappointed beneficiary who has suffered the loss, to frame a cause of action unless the court provides a remedy.

Common mistakes in will drafting which can give rise to disappointed beneficiary claims include:

i) unreasonable delay in preparation of a will;
ii) preparation of a will for a testator lacking competence; and
iii) clerical errors in drafting a will.

Unreasonable delay
Unreasonable delay in preparing a will is a question of fact. (*Rosenberg Estate v. Black*, 2001 O.J. No. 5051).

The age and health of the testator are of prime importance. In urgent cases the lawyer should consider preparing a holographic will while the lawyer attends to drafting a more formal will.

LAWPRO was recently called upon to assist an insured in a claim where the disappointed beneficiary alleged that the insured was negligent in not preparing a will in a timely manner.

Justice Mulligan in his decision in *McCullough v. Riffert,* 2010 ONSC 3891, reviewed the standard of care for a solicitor drafting a will. Justice Mulligan referred to Brian Schnurr's text, *Estate Litigation*, 2nd ed. (Carwswell; 1994- (looseleaf)) where Mr. Schnurr, when addressing how long is too long, states:

> "If the testator is elderly and it is known to the lawyer (or ought to have been apparent to the lawyer) that the testator is in poor health, there is a higher obligation upon the solicitor to take all reasonable steps to give priority to completing the will quickly."

In these circumstances, Mr. Schnurr suggests that a temporary or holograph will should be prepared immediately while the solicitor attends to the drafting and revision of the formal will. In the case at bar, the judge found that the lawyer met the reasonable standard of care in will preparation. Even though the testator died 10 days after consulting with the lawyer, the judge concluded that the facts did not support a finding that the lawyer should have known that the preparation of the will was necessary immediately, because there was no clear evidence that the testator was in poor health or that his death was imminent.

Incompetent testator
The flipside to the failure to prepare a will are the claims which are reported when the lawyer allegedly prepares a will or a power of attorney for an individual who lacks capacity.

This allegation usually arises in the context of a will challenge. The challenger will allege that the testator lacked mental capacity or was unduly influenced when the will was prepared. The lawyer will usually be added as a party to the proceedings by the challenger who is seeking damages for his lost legacy or costs.

A LAWPRO matter is one of the leading cases in this area. In *Hall v. Estate of Bruce Bennett*, 2003 Can LII 7157 (ON C.A.), the Court of Appeal found that the solicitor properly declined to prepare a will where the testator lacked capacity. The evidence in this case was that the testator did not remember the full extent of his estate and was not alert enough to sign. In coming to this decision, the Court of Appeal found that there was no retainer to prepare a will and, as such, there was no duty owed to the disappointed beneficiary.

However, in cases where a solicitor has improperly refused to prepare a will where there is a retainer, damages have been awarded. In situations involving a potential issue of capacity and a near-death situation, the problem for the lawyer is that he or she is in an impossible situation. If a will is prepared and the testator is found to lack testamentary capacity, the lawyer may be liable for costs to set aside the will. On the other hand, if the lawyer doesn't prepare a will for the testator, there may be liability to disappointed beneficiaries for not completing the retainer.

In these circumstances, where possible, a medical opinion or a capacity assessment should be obtained. Regardless of whether a will is prepared or not in these circumstances, it is imperative to document all advice given to the testator. As well, copious notes should be taken on all aspects of the will preparation, including extensive notes on issues relating to capacity.

In determining capacity, you should ask sufficient relevant questions to satisfy yourself that the testator meets the capacity tests in the legislation. Numerous checklists with lists of relevant questions are available.

Usually where there is a will challenge on the basis of lack of capacity, there is often also an allegation of undue influence.

It is important when drafting a will to ensure that the testator is instructing you and not being directed by an interested party. Be aware of red flags that may suggest undue influence. Examples include a refusal by a "friend" or relative to allow the testator to meet with the lawyer privately or a testator who brings in notes setting forth the terms of the will.

Another red flag would be a radical change in the beneficiaries from a previous will. In these cases, the lawyer should ask the testator the reason for the change and confirm and document the change requested. If you are not satisfied with the answers given for the change, probe further.

Finally, once the will has been drafted, highlight in your reporting letter the changes in the will and the explanation given by the testator for the changes.

Clerical errors

Clerical errors are a continual source of claims at LAWPRO. Common errors include spelling errors in the names of charitable organizations, typographical errors in bequests, errors in the number of parts in the division of a residue and missing dispositive provisions in the document.

Most of these errors can be avoided by reading the will or having someone else proofread the will.

Another "avoidance tip" is to check the math: The division of the residue should total 100 per cent.

Errors in names of charities can result in a charity not receiving its bequest. The solicitor owes a duty to the intended beneficiaries and can be found negligent for misnaming the charity.

When drafting a will with a charitable beneficiary, the lawyer can take steps by reviewing the Canada Donor's Guide or the Canada Revenue Agency website to confirm the existence of the charity and the proper spelling of its name. It is best practice to include both the name and address of the charity because if there is an error, the court has a better chance of identifying the intended beneficiary.

Recently LAWPRO was successful in a rectification application with respect to a typographical error.

In *Earle Nugent, Estate Trustee under the will of Viola Binkley v Susan Lang et al.*, 2009 CanLII 26604 (ON S.C.), the solicitor had made a typographic error in the preparation of a new will. As a result, the new will left the sum of $25,000 to each of three beneficiaries rather than the intended $2,500. The court granted the request for rectification. The beneficiaries sought leave to appeal but it was denied on the basis that there was no good reason to doubt the correctness of the decision. Although this precedent has been extremely helpful in resolving other similar claims, it was an expensive process which could have been avoided by simply proofreading the will.

Failure to include clauses in the will for disposition of assets and the residue often result in an intestacy. If the matter cannot be rectified or resolved, a claim for negligence will be advanced against the drafting solicitor. Even if it is resolved, a claim for costs will be advanced by the various parties against the lawyer, which can be difficult and costly to resolve.

If the testator has life insurance, RRSP or pension plans where there is a separate designation of a beneficiary, this needs to be discussed and considered when drafting the will. Finally, it is imperative that you inquire and confirm a testator's marital status. Common-law spouses are often referred to as husband or a wife by a testator. If the testator is separated or divorced, the lawyer should review any agreement to determine any support obligations and discuss the implications of the appropriate family law provisions.

Conflict of interest

Another source of claims in the estates field is conflicts of interest. Often conflicts arise where a lawyer accepting a retainer from both husband and wife or common-law partners to prepare mirror or mutual wills.

If you obtain instructions from spouses or common-law partners to prepare wills, treat the matter as one of a joint retainer. The commentary in the Rules of Professional Conduct under Rule 2.04 states:

> A lawyer who receives instructions from spouses or partners as defined in the *Substitute Decisions Act, 1992*, S.O. 1992, c.30 to prepare one or more wills for them based on their shared understanding of what is to be in each will, should treat the matter as a joint retainer and comply with subrule (6).
>
> Further, …if only one of them were to communicate new instructions…
>
> a) the subsequent communication would be treated as a request for a new retainer and not part of the joint retainer…
> b) in accordance with rule 2.03 the lawyer would be obligated to hold the communication in strict confidence…;
> c) the lawyer would have a duty to decline the new retainer, unless:
>   i) the spouses had annulled their marriage, divorced, permanently ended their conjugal relationship, or permanently ended their close relationship…;
>   ii) the other spouse or partner had died; or
>   iii) the other spouse or partner was informed of the subsequent communication and agreed to the lawyer acting on the new instructions.
>
> After advising the spouses or partners in the manner described above, the lawyer should obtain their consent to act in accordance with subrule (8).

Although the sub-rule does not require it, if there is a power imbalance between the two spouses consider recommending that the “weaker” client obtain independent legal advice to ensure that the client’s consent is informed and not coerced.

Notwithstanding that the rules do allow a lawyer, in certain circumstances, to act on a subsequent retainer, this is an area fraught with danger and a practice that should be avoided. For example, although it appears to be permitted under the Rules, a problem can arise when one of the partners dies and the surviving partner returns to the lawyer seeking to change his or her will.

An example of the type of situation which can arise was discussed in the case of *Hall v. McLaughlin Estate,* 2006 CanLII 23932 (On. S.C.), 2006 O.J. No. 2848.

In the *Hall* case, the couple had made mutual wills. This was a second marriage for both spouses and both spouses had grown children from previous relationships.

The initial wills were mirror wills which provided that on the death of the first spouse the estate would go to the other. On the death of the last spouse, the estate was to be split equally with one half going to the husband’s children and the other half going to the wife’s children.

The wife died first and her estate went to the husband. Contrary to the agreement, the husband changed his will and left the entire estate to his children only. The court imposed a constructive trust on the net value of the husband's estate for the wife's children. The court did so because it found there was a binding agreement that the survivor of them would divide his or her estate into two halves between the two families.

There is no mention in the judgment whether or not the same lawyer prepared the 1992 will and the husband's subsequent will. If it was the same lawyer and the estate had been depleted, it is likely that a claim would have been advanced by the disappointed beneficiaries.

Avoiding negligence claims

1. Promptly report to LAWPRO

Preventing claims is in both your best interests and those of all lawyers insured under the LAWPRO program. Claim prevention helps to reduce the cost of the program and ultimately the cost to the profession for the primary insurance program.

To trigger LAWPRO's involvement, the matter must be reported by the lawyer or the named insured in a timely fashion. Failure to report could result in a denial of coverage if LAWPRO is prejudiced by the late report.

Many claims are reported late because the lawyer does not realize that there is a potential claim. This is particularly true in the wills and estates field. The following events should trigger a report by the insured lawyer to LAWPRO:

1. a request for the will file after the testator's death;
2. a request that the lawyer be examined or provide an affidavit in a will dispute.

If the lawyer reports the matter to LAWPRO as soon as a request is made for his or her file, or the lawyer is asked to provide an affidavit, his or her interests can be best protected. LAWPRO will, in many cases, provide counsel to respond to a request to review a file or to examine the lawyer on a claim prevention basis.

We have in our portfolio numerous claims in which an insured has provided an inaccurate statement or affidavit, and in a subsequent lawsuit this becomes the basis for a negligence claim against the lawyer.

If you are asked for your file after the testator has died, or are asked by a lawyer for a beneficiary or executor to provide a statement, it is possible that a will challenge is being contemplated and the potential exists that you may be sued. As well, in the event of a challenge to the will, the appointment of the executor may also be in doubt and the lawyer may be releasing a file to a party who is not entitled to receive it. The best practice in these circumstances is not to give the file to any party without a court order.

2. Document your file

Once you have reported the claim or potential claim to LAWPRO , defence counsel will request a copy of your file. The contents of the file will often determine the strategy defence counsel will

employ to respond to a claim/potential claim. Well-documented files will often provide a viable defence to the claim. The reverse is true with respect to poorly documented files.

3. Use retainer agreements

Consider using retainer agreements in your practice. Through the use of retainer agreements, you specify the terms and conditions of your employment. If there are conflicts of interest, or any issue of privilege, this can be canvassed in the retainer agreement.

4. Write reporting letters

Where possible, confirm will instructions in writing, document telephone calls and e-mails, and prepare comprehensive reporting letters. Reporting letters are extremely important and can be easily created through the use of templates. In some cases, a reporting letter confirming instructions for a new will and the reason for the drafting instructions may provide a defence to a claim from a disappointed beneficiary.

5. Use checklists

Using a checklist will help prevent many of the clerical errors that are reported. Checklists also help ensure that you've asked about all relevant issues including marital status, family history and testamentary capacity.

6. Develop office routines

All personnel involved in will preparation should be aware of the proper steps to be taken for the execution of wills.

Proofreading wills, comparing the lawyer's notes to the drafted document and checking the math for any fractional legacy should be part of the routine before a will is sent to the testator for review. Consider using a tickler system to follow up and ensure that wills are executed in a timely manner.

Conclusion

In summary, reducing the risk of malpractice claims in the wills and estate field is possible through the use of good practices and procedures. The tools to implement these practices are readily available to the profession. While you cannot totally eliminate the risk of a malpractice claim, you can improve the odds of avoiding a claim by integrating risk management strategies into your practice.

Pauline R. Sheps is a claims counsel specialist in LAWPRO's Primary Professional Liability Claims Department.

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Wills & estates claims

Malpractice fact sheet

lawpro.ca

Quick stats

Average **173 claims** per year

Average cost: **$6 million** per year

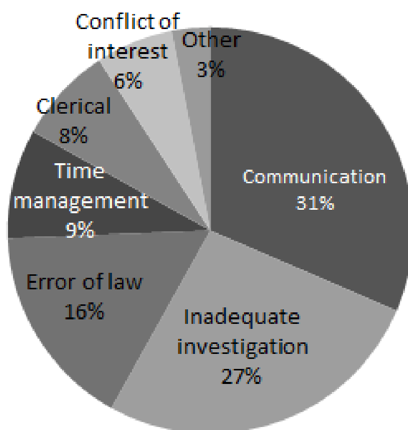
Average cost per claim: $34,400

#4 claims area by cost

#5 claims area by count

Average of 4 years before claim reported

Common errors



Malpractice claims in wills and estates practice have increased steadily over the last decade, nearly doubling in frequency.

Communications issues (often at the time the will is drafted) are the biggest source of these claims. Too many lawyers are not truly listening to the client's instructions and not probing and questioning the client to uncover facts that may cause problems later. It's important to read between the lines instead of simply filling in the elements of a will template or precedent.

Wills and estates is an extraordinarily complex area. Lawyers who practice in this area must maintain a working familiarity with wide range of statutes and must apply complex provisions of the *Income Tax Act*. Law-related errors are more than twice as likely to occur in the wills and estates area as compared to other areas of practice.

Ensuring you understand the client's needs, knowing the relevant law and avoiding shortcuts can help prevent claims. Detailed documentation of your conversations with, and instructions from, the client can support a lawyer's defence should a claim be made.

See reverse page for the most common wills and estates errors and more steps that can be taken to reduce exposure to a malpractice claim.

Speakers and resource materials

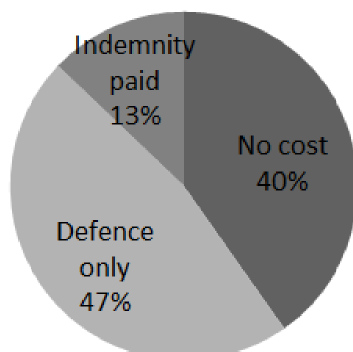
We can provide knowledgeable speakers who can address claims prevention topics. Email practicePRO@lawpro.ca

Visit practicePRO.ca for resources including LAWPRO Magazine articles, checklists, precedents, practice aids and more.

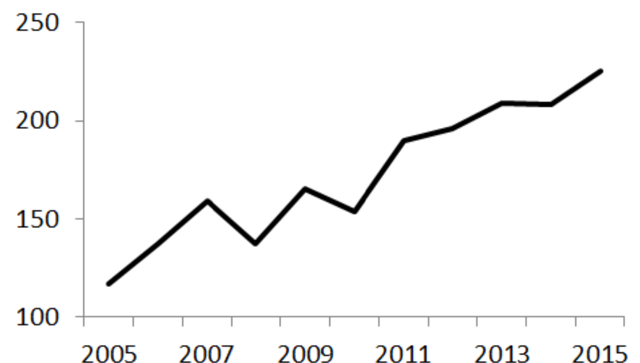
Hot topics in wills & estates law claims

- Proper investigation requires that you ask yourself the question: "what does my client really want?"
- Ask your client what their assets are (and insist on an answer).
- Law-related errors are twice as likely to occur in this area of practice than in others. Make sure you know statute and case law.

Resolution of claims



Count of wills & estates claims



All claim figures from 2005-2015. All cost figures are incurred costs (April 2016)

Risk management tips

Ask more probing questions when meeting with a client to prepare a will

Too many lawyers are not asking the questions that could uncover facts that could cause problems later, or making clear to the client what information they need to provide. Was there a prior will? Are all the beneficiaries identified correctly? What about gift-overs? Were all assets identified, and how are they registered? Was there a previous marriage? Ask, ask, ask. And then do a reporting letter to confirm everything that was discussed.

Take time to compare the drafted will with your notes

It sounds like obvious advice, but we see claims where the will did not adequately reflect the client's instructions, or overlooked some important contingencies. Many of these errors could have been spotted by simply reviewing the notes from the meeting with the client. It can help to have another lawyer proofread the will, or set it aside for a few days and re-read it with fresh eyes. When you review it, consider the will from the position of the beneficiaries or disappointed would-be beneficiaries. Ask yourself if you were going to challenge this will, on what basis would you do so?

Confirm as best you can the capacity of the testator and watch for undue influence

With greater numbers of elderly clients, lawyers need to be vigilant about these issues. Meet with the client separately from those benefiting from a will change, and have written proof that the client understands what they are asking and the advice you've given. And while it is difficult to be completely certain of capacity, be sure to document what steps you've taken to satisfy yourself that the client's capacity has been verified.

Don't act for family members or friends

We see claims where lawyers didn't make proper enquiries or take proper documentation because they assumed they had good knowledge of their family or friends' personal circumstances. It's best not to act for them, but if you must, treat them as if they were strangers. And remember if a claim arises it will likely not be from the friend or family member, but from a disappointed beneficiary with no personal relationship with you.

Most common malpractice errors

Lawyer/client communication errors (31%)

- Failure to compare the draft will with the instructions notes to ensure consistency
- Failing to ensure that the client understands what you are telling him and that you understand what he is telling you, particularly if there is a language barrier
- In estate litigation: failing to communicate and document settlement options

Inadequate investigation of fact or inadequate discovery (27%)

- Failure to ask the testator what their assets are
- Failure to ask about the existence of a prior will
- Not digging into more detail about the status of past marital relationships, other children or stepchildren, or whether a spouse is a married spouse or common law spouse

Failure to know or properly apply the law (16%)

- Not being aware of key provisions of the *Income Tax Act* (and not obtaining the appropriate tax advice)
- Drafting a complex will involving sophisticated estate planning when you do not have the necessary expertise;
- Failing to properly execute documents

Time Management and procrastination (9%)

- Missing the six-month deadline for making an election and issuing the necessary application under Section 6 of the *Family Law Act*
- Delay in preparing a will
- Delay in converting assets into cash in an estate administration

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Sean Lawler: " 'One Less Witness': Getting Evidence From Lawyers in Estate Disputes", (2014) 34 E.T.P.J. 54-78.
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"ONE LESS WITNESS": GETTING EVIDENCE FROM LAWYERS IN ESTATE DISPUTES

Sean Lawler[*]

1. Introduction

Noted New York criminal defence lawyer Murray Richman has boasted in more than one interview: "I love murder — always one less witness to worry about."[1] The "one less witness" problem[2] is also a feature common to those disputes that turn on what a deceased or incapable person intended to do, or whether he was capable of doing it. The person who is best-placed to say whether his intentions were foiled by, among other things, a lack of capacity, another person's undue influence, or a drafting error, is unavailable. However, unlike in murder cases, the deceased's evidence of "what happened" will, in many cases, not be lost; his lawyer will have written it down or otherwise recorded it.

Getting the lawyer's evidence of her client's intention can be complicated by the parties' competing interests: for instance, the person propounding a will may be reluctant to give the will-challenger ammunition to use against the estate. The deceased's lawyer may have her own reasons to not reveal what the deceased said to her. She is unlikely to be properly compensated for her time answering such requests, and may also face the prospect of having allegations of professional negligence made against her. Lastly, the lawyer who received information from a client must be careful to maintain solicitor-client privilege and respect the client's confidentiality.

The purpose of this article is to discuss the circumstances in which a lawyer must reveal the details of her communications with her client for the purpose of an estate dispute (whether or not it is in the form of a law suit), and consider what protection she receives from the courts. The article is divided in four parts: responding to requests from a client's representative, court-ordered production to

* Shibley Righton LLP. With thanks to Isabelle Eckler, student-at-law at Shibley Righton.

1. Philip Gourevitch, "The Crime Lover", *The New Yorker* (February 19, 2001), p. 160; Joyce Wadler, "Public Lives; In Court, an Expert in Packaging Rappers", *The New York Times* (January 26, 2000).
2. A problem for the prosecution, at any rate.

non-clients, oral examinations of the lawyer, and what protection there is for the lawyer in these circumstances.

The theme of this article is that relevance is paramount. In each case, the courts balance the rights of the parties, the deceased, and the lawyer. However, the purpose of the civil litigation process is to "permit a judge to find the facts necessary to resolve the dispute and to apply the relevant legal principles to the facts as found."[3] Other considerations are secondary: the courts will order production of information where it is necessary to get to the "truth" of what happened.

2. Requests from the Client's Representative

This article assumes that the lawyer's client cannot ask for his file because he is dead or incapable. In Ontario, a request from the "client" will come from the personal representative such as an estate trustee under a will or pursuant to the *Estates Act*[4] (if the client is deceased), or the attorney for property,[5] or the statutory[6] or court-appointed[7] guardian of property (if the client is incapable). The attorney for property,[8] the guardian of the property,[9] and the estate trustee of the client's estate[10] have the same power as the client to ask for the lawyer's file.

Aggio v. Rosenberg

The 1981 decision of Master Sandler in *Aggio* v. *Rosenberg,*[11] a case that has been cited with approval several times in Ontario,[12]

3. *Hryniak v. Mauldin*, 2014 SCC 7 (S.C.C.), at para. 28.
4. R.S.O. 1990, c. E.21, as amended, s. 7.
5. *Substitute Decisions Act, 1992*, S.O. 1992, c. 30, as amended ("SDA"), s. 7.
6. SDA, s. 15.
7. SDA, s. 22.
8. SDA, s.7(2), although the attorney for property may be subject to the restrictions set out in the power of attorney: SDA, s. 7(6).
9. SDA, s. 31(1), though the court may impose restrictions on the guardian of property SDA, s. 31(3).
10. *Re Bion Estate; Hope v. Martin*, 2011 ONSC 5447 (Ont. S.C.J.).
11. *Aggio v. Rosenberg* (1981), 24 C.P.C. 7, [1981] O.J. No. 2229 (Ont. Master).
12. *Spencer v. Crowe* (1986), 180 A.P.R. 9, [1986] N.S.J. No. 218 (N.S. T.D.); *Bowman v. Rainy River (Town)* (2007), 156 A.C.W.S. (3d) 563, [2007] O.J. No. 1235 (Ont. S.C.J.), additional reasons 2007 CarswellOnt 2991 (Ont. S.C.J.); *Price v. Lambrinos* (2012), 222 A.C.W.S. (3d) 886, [2012] O.J. No. 4000 (Ont. Master); *Grillo v. D'Angela* (2009), 306 D.L.R. (4th) 370, [2009] O.J. No. 7 (Ont. S.C.J.), additional reasons (2009), 174 A.C.W.S. (3d) 968 (Ont. S.C.J.); *Wadsworth v. Elkin Injury Law, Barristers, Professional Corp.* (2008), 167 A.C.W.S. (3d) 475, [2008] O.J. No. 1846 (Ont. S.C.J.).

sets out the rules governing who owns which parts of a lawyer's file, and therefore, what must be produced to a client on request. In *Aggio*, the client was a defendant in a law suit. She changed lawyers. The client had paid her first lawyer's accounts and the lawyer gave her his entire file except for his notes and correspondence. The client brought an application to compel the lawyer to turn those documents over as well.

Master Sandler set out the following with respect to what the lawyer must deliver to the client:[13]

> As to what the law in Ontario is, I adopt the law as set out in *Corderley*, *supra*, as follows:
>
> > "D. AUTHORITY OVER DOCUMENTS ON TERMINATION OF RETAINER
> >
> > Documents in existence before the retainer commences and sent to the solicitor by the client or by a third party during the currency of the retainer present no difficulty since their ownership must be readily apparent. The solicitor holds them as agent for and on behalf of the client or third party, and on the termination of the retainer must dispose of them (subject to any lien he may have for unpaid costs – see pp. 416 *et seq*., *post*) as the client or third party may direct.
> >
> > Documents which only come into existence during the currency of the retainer and for the purpose of business transacted by the solicitor pursuant to the retainer, fall into four broad categories:
> >
> > (i) Documents prepared by the solicitor for the benefit of the client and which may be said to have been paid for the client, belong to the client.
> >
> > (ii) Documents prepared by the solicitor for his own benefit or protection, the preparation of which is not regarded as an item chargeable against the client, belong to the solicitor.
> >
> > (iii) Documents sent by the client to the solicitor during the course of the retainer, the property in which was intended at the date of despatch to pass from the client to the solicitor, e.g., letters, belong to the solicitor.
> >
> > (iv) Documents prepared by a third party during the course of the retainer and sent to the solicitor (other than at the solicitor's expense), e.g., letters, belong to the client."
>
> From these broad categories, specific propositions are then laid down at p. 119 as follows:

13. *Aggio v. Rosenberg*, *supra*, footnote 11, at paras. 15 and 16, quoting Arthur Cordery, Graham J. Graham-Green and Duncan S. Gordon, *Cordery's Law Relating To Solicitors*, 6th ed. (London, Butterworths, 1968).

> "Cases, instructions and briefs prepared by the solicitor and delivered to counsel" belong to the client within category (i).
>
> "Drafts and copies made by the solicitor of deeds or other documents in non-contentious business" belong to the client within category (i).
>
> "Copies made by the solicitor of letters received by him, if paid for by the client" belong to the client under category (i).
>
> "Copies made by the solicitor of letters received by him, if not paid for by the client" belong to the solicitor under category (ii).
>
> "Copies made by the solicitor of letters written by him to third parties, if contained in the client's case file and used for the purpose of the client's business" belong to the client under category (i).
>
> "Copies made by the solicitor of letters written by him to third parties, if contained only in a filing system of all letters written in the solicitor's office" belong to the solicitor, under category (ii).
>
> "Entries of attendance, tape recordings of conversations, etc., inter-office memoranda partner to partner, partner to staff, entries in diaries, office journals and books of account" belong to the solicitor under category (ii).
>
> "Letters and authorities and 'instructions written or given' by the client to his solicitors" belong to the solicitor under category (iii).
>
> "Letters received by the solicitor from third parties" belong to the client under category (iv).
>
> "Vouchers for disbursements made by the solicitor on behalf of his client" belong to the client under category (iv).

The lawyer's file will contain several types of documents relevant to an estate dispute. Some documents, such as correspondence from a capacity assessor to the lawyer about the client's testamentary capacity, fall under category (iv), belong to the client, and are therefore producible at the client's request. However, many of the types of documents that will most often be relevant to an estates dispute will, pursuant to *Aggio*, belong to the lawyer and therefore not be producible. For instance:

(a) The lawyer's interview notes and internal memoranda fall into category (ii). In *Bowman*,[14] a contemporary case, D.C. Shaw J. held that this category of documents also includes "lawyers' . . . internal emails, and the firm's computer-generated billing records"; and

(b) The client's letter of instruction to the lawyer or his written memo expressing his wishes appear to fall into category (iii).

14. *Supra*, footnote 12.

This seems to suggest that the wary estates lawyer can avoid involvement in a looming estate dispute by refusing to produce key parts of her file to the personal representative who requests it.

Beyond *Aggio*

Subsequent Ontario case law about the types of evidence to be admitted in estate disputes suggest that it is risky to rely, unquestioningly, on the rigid categorization in *Aggio*. The portions of *Cordery* quoted in *Aggio* presume that the lawyer's notes and memos, as well as the correspondence from the client, were made for the lawyer's benefit. This is not necessarily so in estate cases. For example, in *Hall v Bennett Estate*, the Court of Appeal held that:[15]

> . . . it is settled that a solicitor who undertakes to prepare a will has the duty to use reasonable skill, care and competence in carrying out the testator's intentions. This duty includes the obligation to inquire into *and substantiate the testator's capacity to make a will*. This first obligation is of fundamental importance. After all, if the testator does not have the requisite testamentary capacity, the preparation of a will in accordance with his expressed wishes at the time may only serve to defeat his true intentions. [emphasis added]

The lawyer's notes may also be relevant to a dispute over the interpretation of a will. In *Rondel v. Robinson Estate*,[16] the Court of Appeal held that a court may consider:[17]

> When a will takes effect and is being interpreted, the testator is no longer available to clarify her intentions. Extrinsic evidence is admissible to aid the construction of the will. The trend in Canadian jurisprudence is that *extrinsic evidence of the testator's circumstances and those surrounding the making of the will may be considered*, even if the language of the will appears clear and unambiguous on first reading. Indeed, it may be that the existence of an ambiguity is only apparent in the light of the surrounding circumstances. [emphasis added]

The implication of both *Hall* and *Rondel* is that the estates lawyer should consider, when interviewing and taking will instructions from a client, that her file may be subsequently used in court as evidence about the validity or interpretation of the will. In light of

15. *Hall v. Bennett Estate* (2003), 227 D.L.R. (4th) 263, 64 O.R. (3d) 191 (Ont. C.A.), at para. 48.
16. *Rondel v. Robinson Estate; Robinson Estate v. Robinson*, 2011 ONCA 493 (Ont. C.A.), leave to appeal refused (2012), 295 O.A.C. 400 (note) (S.C.C.).
17. *Rondel*, *supra*, footnote 16, at para. 24.

these cases it is difficult to conclude that documents in Cordery's categories (ii) or (iii) must always belong to the lawyer: the courts do not presume those documents to be solely for the lawyer's benefit.

In addition to setting out the "four categories" of documents, *Cordery* also prescribes what the lawyer and client must prove when arguing over what parts of the lawyer's file should be turned over to the client. It says:[18]

> The solicitor seeking to retain documents must show that:
>
> (a) He was under no duty to prepare them;
> (b) They were not in fact prepared for the benefit of the client; and
> (c) The client cannot be regarded as being liable to pay for them either specifically or under any general item in the bill of costs.
>
> Conversely the client must show that:
>
> (a) The documents were a necessary part of the business transacted, eg a draft lease submitted to the lessee for agreement; and
> (b) He has in fact paid (or is liable to pay) in one form or another for their preparation.

Applying these criteria, it would appear that an estate trustee is entitled to, for instance, the lawyer's will-notes: the lawyer is under a duty to prepare the notes; they are, at least in part, prepared for the benefit of the client; and they are therefore part of the business transacted, in that they are the evidence the lawyer is expected to generate if the will is challenged. The "liable to pay" criteria is related to the other criteria: presumably the client is "liable to pay" for the notes because they are ultimately for his benefit.

The general criteria set out in *Cordery* are consistent with the approach used in the English Court of Appeal's decision in *Leicestershire County Council v. Michael Faraday & Partners Ltd.*[19] In that case a surveyor left the company he worked for and opened his own surveying business. The former employer wanted to prevent the surveyor from keeping the extensive notes he had made during the five years he had worked for the company. The employment contract was of no help to determine what the surveyor could keep. The Court of Appeal held that the surveyor's notes were his own, and did not belong to the employer.

The editorial note to the case summarizes the court's conclusion:[20]

18. Cordery *et al.*, *supra*, footnote 13, at p. 120.
19. [1941] 2 All E.R. 483 (Eng. C.A.).
20. *Leicestershire*, *supra*, footnote 19, at p. 484.

> Where an agent in the course of his employment brings into existence certain documents, those documents are in the principal's documents and the principal is entitled to possession of them. Where, however, a professional man is retained on behalf of a client, apart from a special term in the retainer, documents coming into existence in the course of the carrying out of his duties by that professional man are not the client's documents, unless they are specially prepared for the client.

Leicestershire is not about lawyers' files, but Canadian courts have cited the case as governing production of the files of "professionals",[21] and "attorneys or accountants."[22] If the lawyer's notes, and correspondence to the lawyer are solely for the purpose of preparing the will or giving estate advice, then those documents come "into existence in the course of carrying out his duties." Where, however, the lawyer should expect that those notes may be necessary to substantiate the client's capacity or determine his intentions, a court could conclude that the notes were "specially prepared for the client."

The lawyer who does not want to produce a portion of her file to a client's personal representative must carefully review the documents. It may not be enough to assert that internal notes and correspondence from the client are exempt from such production because of the decision in *Aggio*. The more prudent approach is to also consider the purpose for which those documents were created and whether the documents were intended for the benefit of the lawyer or of the client.

3. Court-Ordered Production

The previous section considered the lawyer's obligation to someone standing in the shoes of her client. The purpose of this section is to discuss what the lawyer is to do when the demand for the file comes from someone who appears to have no, or in fact has no, authority to obtain the lawyer's file. This is most common in will challenges, where the family member who has been excluded from the will, or the person named as estate trustee under a previous will, seeks the lawyer's file. However, such a request may also come in any dispute where an unchallenged estate trustee refuses to consent to the release of the lawyer's file.

21. *Nova Scotia (Attorney General) v. Royal & SunAlliance Insurance Co. of Canada*, 2005 NSCA 34, [2005] N.S.J. No. 77 (N.S. C.A.), *per* Cromwell J.A., at para. 20.
22. *BCE inc. v. BCE Acquisition inc.*, 2010 QCCS 7132, [2010] Q.J. No. 31934 (C.S. Que.), at paras. 18-19.

Confidentiality

The issue is not only one of knowing who has the property interest in the file. The estates lawyer must also be concerned with complying with her duty of confidentiality to her client. Rule 3.3-1 of the *Rules of Professional Conduct* of the Law Society of Upper Canada says:

> *Confidential information*
>
> 3.3-1 A lawyer at all times shall hold in strict confidence all information concerning the business and affairs of the client acquired in the course of the professional relationship and shall not divulge any such information unless
>
> (a) expressly or impliedly authorized by the client;
> (b) required by law or by order of a tribunal of competent jurisdiction to do so;
> (c) required to provide the information to the Law Society; or
> (d) otherwise permitted by rules 3.3-2 to 3.3-6.
>
> *Justified or Permitted Disclosure*
>
> (2) When required by law or by order of a tribunal of competent jurisdiction, a lawyer shall disclose confidential information, but the lawyer shall not disclose more information than is required.

The commentary to Rule 3.3-1 says, in part:

> A lawyer cannot render effective professional service to the client unless there is full and unreserved communication between them. At the same time, the client must feel completely secure and entitled to proceed on the basis that, without any express request or stipulation on the client's part, matters disclosed to or discussed with the lawyer will be held in strict confidence.

In general, the lawyer who releases her file to someone without authorization or an order of the court runs the risk of violating the *Rules of Professional Conduct*.[23]

Action or Application

Someone who does not have the authority to require the lawyer to produce her file may, (i) commence a law suit against the lawyer,

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23. There is at least one exception to this: where all the beneficiaries agree, a lawyer may produce, without court order, the original will to the one beneficiary who will apply for the issuance of a certificate appointment of estate trustee where the named estate trustee renounced her right to apply for probate. *Re Bion Estate; Hope v. Martin*, *supra*, footnote 10.

and seek production of her file pursuant to the *Rules of Civil Procedure*[24] (the "Rules") governing documentary production, or (ii) seek production the lawyer's file pursuant to the Rules governing production from non-parties.[25]

In certain circumstances, the courts in Ontario will allow one party to sue another solely for the purpose of obtaining discovery. However, such "*Norwich Pharmacal*"[26] orders are limited to circumstances where the defendant "has information that the claimant alleges would allow it to identify a wrongdoer, so as to enable the claimant to bring an action against the wrongdoer where the claimant would not otherwise be able to do so", and so are not common in estate disputes.[27] Where the party sues the lawyer because of, for instance, an allegation of professional negligence, the lawyer would likely be required to list, and produce, the contents of her file in an affidavit of document pursuant to the Rules.[28] However a discussion of the lawyer's obligations in that circumstance is outside the scope of this article, which is intended to discuss the lawyer as witness, not as a party.

The rule that a party to litigation must follow in order to obtain production of the lawyer's file depends on whether the proceeding is an "application" or an "action". "Actions" are the default method of bringing a dispute to court: Rule 14.02 says that "Every proceeding in the court shall be by action, except where a statute or these rules provide otherwise." Actions are generally argued on the basis of live evidence given before the trial judge[29] and the issues are framed by pleadings, including a statement of claim and a statement of defence.[30]

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24. R.R.O. 1990, Reg. 194.
25. A lawyer who is examined for discovery as a non-party, or who is examined as a witness on a pending motion or application may be required to bring her file to the examination. Rule 34.10(2) and (3). This is discussed further below.
26. *Norwich Pharmacal Co. v. Customs & Excise Commissioners* (1973), [1974] A.C. 133 (U.K. H.L.).
27. *GEA Group AG v. Ventra Group Co.* (2009), 312 D.L.R. (4th) 160, [2009] O.J. No. 3457 (Ont. C.A.) at para. 41, additional reasons 2009 ONCA 878 (Ont. C.A.); *1654776 Ontario Ltd. v. Stewart*, 2013 ONCA 184 (Ont. C.A.) at para. 2, leave to appeal refused 2013 CarswellOnt 13049 (S.C.C.). The author was unable to find an Ontario case where a *Norwich Pharmacal* order was made in an estates dispute. They are more common in disputes relating to intellectual property, internet defamation, and securities.
28. Rule 30.03.
29. Rule 53.01.
30. Rule 25.01. The pleadings may also include replies, cross-claims, counter-claims, and third-party claims.

Parties may prefer to proceed by way of application because the procedure governing an application is generally simpler than that in an action. Applications are argued on the basis of an application record[31] consisting of witnesses' affidavits, and the transcript of cross-examinations of affiants[32] and examinations of witnesses who have not sworn affidavits.[33] For some estate disputes, such as applications for support under the *Succession Law Reform Act*,[34] the governing statute prescribes that they be commenced by application.[35] The Rules authorize other types of estate disputes, such as will challenges[36] and will interpretation disputes,[37] to be commenced by application. The court has the discretion to convert certain types of application into an action.[38]

Whatever the form of the proceeding, the parties must obtain a court order for production of the file. In an action, this is prescribed by Rule 30.10. When, as is common, the estate proceeding is commenced as an application the usual first step is for the parties to obtain an order for directions pursuant to Rule 75.06. Such orders are:[39]

> . . . designed to provide the parties with a procedural framework in which to prepare the proceeding for final adjudication. Rule 75.06 provides the court with considerable discretion and flexibility to put in place a process that will ensure the just, expeditious and least expensive determination of a proceeding on its merits. Parties are expected to take time and care in preparing proposed orders giving directions for consideration by the court.

Rule 75.06 says that an order for directions may direct, among other things, "such . . . procedures as are just". The *Practice Direction* specifically provides that orders for directions may include direction respecting "any other prehearing steps to be

31. Rule 38.09.
32. Rule 39.02.
33. Rule 39.03
34. R.S.O. 1990, c. S. 26, as amended ("SLRA").
35. SLRA s. 58.
36. Rule 14.05(1)(a).
37. Rule 14.05(1)(d).
38. Rule 38.10(1)(b). However, this does not apply to applications brought under Rules 74 and 75, which govern several types of estate disputes.
39. Mme. Justice Heather J. Smith, Chief Justice Superior Court of Justice (Ontario) and Mr. Justice Geoffrey B. Morawetz, Regional Senior Judge, Superior Court of Justice (Ontario), Toronto Region, *Consolidated Practice Direction Concerning the Estates List in the Toronto Region*, April 11, 2014 (hereinafter the "*Practice Direction*") at Part VII A, para. 44.

undertaken, including documentary disclosure [and] obtaining . . . legal records."[40]

Neither Rule 75.06 nor the *Practice Direction* (which applies to Toronto proceedings) specify the test for production of the lawyer's file. The test generally for the production of documents from someone who is not a party to an action is set out in Rule 30.10. It says:

> 30.10(1) The court may, on motion by a party, order production for inspection of a document that is in the possession, control or power of a person not a party and is not privileged where the court is satisfied that,
>
> (a) the document is relevant to a material issue in the action; and
> (b) it would be unfair to require the moving party to proceed to trial without having discovery of the document.

Rule 30.10 applies to all actions, so it governs estate disputes not commenced by way of an application. Moreover, Rules and the *Practice Direction* provide that the court may, in an order for directions, in effect convert an application into an action, with the exchange of pleadings,[41] examinations for discovery,[42] and a pretrial and trial.[43] Where an estate application has been converted to an action, Rule 30.10 should apply.

Solicitor-Client Privilege

As is set out below, the bulk of the cases in which a party has resisted production of the estate lawyer's file have the following in common, whether or not they are Ontario decisions, and whether or not they refer to Rule 30.10:

(a) The objecting party does so on the basis that the file is solicitor-client privileged;
(b) The court authorizes the release of the file if:
  (i) it is "relevant" to the dispute pursuant to the Supreme Court of Canada's 1991 decision in *Geffen v. Goodman Estate*;[44] or
  (ii) the estate is found to have "waived" privilege.

Some documents in the lawyer's file, such as communications with third parties and documents that exist independently of the

40. *Practice Direction* Part VII A, para. 46(i).
41. Rules 75.06(3)(e) and 75.07; *Practice Direction* Part VII A, para. 46(f).
42. Part VII A, para. 46(i).
43. *Practice Direction* Part VII A, paras. 46(k) and (l).
44. [1991] 2 S.C.R. 353 (S.C.C.).

lawyer-client relationship (such as bank statements) are not privileged.[45] In contrast, solicitor-client communications are privileged. That privilege "belongs" to the client, not to the lawyer.[46] Solicitor-client privilege survives the death of the client and "enures to his or her next of kin, heir, or successors in title."[47]

Geffen v. Goodman Estate

The Supreme Court of Canada has held that the courts may order production of privileged documents in a lawyer's file in disputes where the central issue is the intention or capacity of the deceased or incapable person. In these situations "the nature of the case precludes the issue [of privilege] from arising". Quoting from a 1903 decision of the Ontario Court of Appeal, Wilson J. held that:[48]

> The reason on which the rule [of solicitor-client privilege] is founded is the safeguarding of the interests of the client, or those claiming under him when they are in conflict with the claims of third persons not claiming, or assuming to claim, under him. And that is not this case, where the question is as to what testamentary dispositions, if any, were made by the client. As said by Sir George Turner . . . "the disclosure in such cases can affect no right or interest of the client. The apprehension of it can present no impediment to the full statement of his case to his solicitor . . . and the disclosure when made can exposure the Court to no greater difficulty than presents itself in all cases where the courts have to ascertain the views and intentions of parties, or the objects and purposes for which dispositions have been made." It has been the constant practice to apply the rule here stated in cases of contested wills where the evidence of the solicitors by whom the wills were prepared, as to the instructions they received, is always received. And the application of a different rule in this action would deprive the plaintiff of a considerable part of the proof of his case.

Quoting from another case, Wilson J. said: "In the interests of justice, it is more important to find out the true intention of the testator" than to protect solicitor client privilege.[49]

This approach does not apply only to will challenges. In *Geffen*,

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45. Alan W. Bryant, Sidney N. Lederman, and Michelle K. Fuerst, *The Law of Evidence in Canada*, 3rd ed. (Markham, Ontario, LexisNexis, 2009), at p. 931; *R v. Murray*, (2000), 144 C.C.C. (3d) 289, [2000] O.J. No. 2182 (Ont. S.C.J.).
46. *Geffen*, *supra*, footnote 44, at para. 56.
47. *Geffen*, *supra*, footnote 44, at para 57.
48. *Geffen*, *supra*, footnote 44, at para. 61.
49. *Geffen*, *supra*, footnote 44, at para. 62, quoting from *Re Ott*, [1972] 2 O.R. 5 (Ont. Surr. Ct.), at p. 11.

the moving party alleged that an *inter vivos* trust was procured by undue influence. The party resisting production argued that the cases permitting will-drafting lawyers to give evidence in will challenges was a narrow "exception" to the usual rule that communications between lawyer and client must not be disclosed. There was no basis for extending that "exception" to other types of disputes.

The Supreme Court disagreed. Mme. Justice Wilson rejected such a "pigeon-hole" approach and held that:[50]

> In my view, the considerations which support the admissibility of communications between solicitor and client in the wills context apply with equal force to the present case. The general policy which supports privileging such communications is not violated. The interests of the now deceased client are furthered in the sense that the purpose of allowing the evidence to be admitted is precisely to ascertain what her true intentions were. And the principle of extending the privilege to the heirs or successors in title of the deceased is promoted by focusing the inquiry on who those heirs or successors properly are. In summary, it is, . . . "in the interests of justice" to admit such evidence.

In subsequent cases that considered *Geffen*, the courts have ordered production of the lawyer's will file when the contents were "relevant" to a will-challenge.[51] The courts have also ordered the production of the lawyer's file in disputes over: who should be appointed a "committee of the estate" of an incapable person;[52] and whether someone was incapable at the time he entered into a, seemingly, improvident real estate transaction.[53] In each case, the court found that the file would contain evidence of the incapable person's intention or capacity.

Conversely, when the courts have refused to order the

50. *Geffen*, *supra*, footnote 44, at para. 64.
51. *MacPherson v. Mulcahy* (1993), 332 A.P.R. 374, [1993] N.S.J. No. 600 (N.S. T.D.); *Re McKean Estate* (1998), 501 A.P.R. 125, [1998] N.B.J. No. 36 (N.B. Prob. Ct.); *Verch v. Weckwerth* (2010), 55 E.T.R. (3d) 278, [2010] O.J. No. 907 (Ont. S.C.J.), additional reasons 2010 ONSC 1988 (Ont. S.C.J.). Also, it is implicit in the Court of Appeal's decision in *Hall* (*supra*, footnote 15) that the lawyer's will file would be produced; Lastly, see *Hicks Estate v. Hicks* (1987), 25 E.T.R. 271 (Ont. Dist. Ct.), which was decided before *Geffen*, but which applies the same reasoning.
52. *Re Palamarek* (2010), 196 A.C.W.S. (3d) 410, [2010] B.C.J. No. 2666 (B.C. S.C. [In Chambers]). The application was for production of an audio recording of a conversation between the lawyer and the subject of the litigation about, among her things, where she wanted to live and from whom she wanted to receive care.
53. *Wayne v. Wayne* (2012), 82 Alta. L.R. (5th) 21, [2012] A.J. No. 1306 (Alta. Q.B.).

production of lawyers' files, it has been because they were irrelevant to the dispute. For example:

(a) Where certain property conveyances were challenged on the basis that the transferor had been unduly influenced, the court refused to order the production of the file of the lawyer who drafted the transferor's will. The court found that the will file was irrelevant to whether the property conveyances were the result of undue influence;[54]

(b) Where a deceased's last will was being challenged on the basis of lack of capacity and undue influence, the files relating to the deceased's prior wills were irrelevant, and therefore should not be produced;[55]

(c) In a British Columbia proceeding for support under the *Wills Variation Act*,[56] the deceased's will excluded his children. The deceased said in the will this was because they received gifts of money from him during his lifetime "quite sufficient in my view to satisfy any obligation" to them that he may have had. The court refused production of the will file because it was not needed to enable the court to learn the deceased's intentions, which were evident on the face of the will.[57]

The effect of the *Geffen* decision is that the courts conflate privilege and relevance when considering whether to order the production of an estate lawyer's file. The court sees production of "relevant" legal files as consistent with the purpose of the doctrine of solicitor-client privilege, and therefore in the public interest.

Waiver

The court may also order the production of lawyers' files when privilege has been "waived". Waiver may be "voluntary" where the holder of the privilege knows of the existence of the privilege being waived, clearly intends to waive it, and completely understands the consequences of doing so.[58] In *Schwartz Estate v. Kwinter*,[59] the

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54. *Fawcett Estate v. Steiner* (1998), 21 E.T.R. (2d) 271, [1998] B.C.J. No. 629 (B.C. S.C. [In Chambers]).
55. *Wood v. Wilkie* (2012), 80 E.T.R. (3d) 34, [2012] B.C.J. No. 1580 (B.C. S.C.).
56. R.S.B.C. 1996, Ch. 490 (since repealed).
57. *Gordon v. Gilroy* (1994), 5 E.T.R. (2d) 289, [1994] B.C.J. No. 1927 (B.C. Master). See also the Manitoba decision of *Daily v. Daily Estate* (1996), [1997] 2 W.W.R. 712, [1996] M.J. No. 589 (Man. Q.B.).
58. Bryant *et al.*, *supra*, footnote 45, at p. 957.

deceased executed a will that left everything to daughter Elaine, and excluded daughter Shelley. Elaine alleged that the parents, who were divorced, had agreed that the deceased would leave his estate to Elaine, and the ex-wife would leave her estate to Shelley (the "Agreement").

Shelley and her mother (*i.e.*, the deceased's ex-wife) challenged the will and denied that there was an agreement between the deceased and the mother. The court accepted that the alleged agreement was relevant to whether the deceased's will was valid. In support of her position that there was no Agreement, the mother produced several wills that she had executed over the years. Elaine wanted production of the files of the lawyer who prepared those wills.

The court ordered the will files produced. They were relevant to the dispute. Moreover, the court held that the mother had waived privilege over the will files. Her Honour held that the wills themselves were privileged until the mother died. She had a lawyer but produced them anyway. On the unusual facts of this case, the court found that this was a "voluntary" waiver of privilege.

4. Examination of the Lawyer

It is common for one or more of the parties to want to examine the lawyer, even after receiving the lawyer's file. The diligent lawyer reasonably hopes that thorough note-taking will provide a complete answer to questions about the client's capacity and intentions. However, it can be difficult for the lawyer to anticipate every dispute that may arise in a client's family. Even the most detailed of notes and records may leave certain, relevant, questions unanswered.

(a) Circumstances in Which the Lawyer will be Examined

An examination of a witness on a pending application is governed by Rule 39.03. That rule simply says that "a person may be examined as a witness before the hearing of a pending . . . application for the purpose of having a transcript of his or her evidence available for use at the hearing."[60] It does not require a party to seek leave to examine. Despite this, Strathy J. has held that it is reasonable for a lawyer to insist on the protection of a court order as a condition of attending an examination.[61]

59. (2008), 86 Alta. L.R. (4th) 287, [2008] A.J. No. 183 (Alta. Q.B.).
60. Rule 39.03(1).

A party to an action must seek leave of the court to compel someone who is not a party to the litigation to attend an examination for discovery. Rule 31.10(1) and (2) says:

> (1) The court may grant leave, on such terms respecting costs and other matters as are just, to examine for discovery any person who there is reason to believe has information relevant to a material issue in the action, other than an expert engaged by or on behalf of a party in preparation for contemplated or pending litigation.
>
> *Test for Granting Leave*
>
> (2) An order under subrule (1) shall not be made unless the court is satisfied that,
>
> (a) the moving party has been unable to obtain the information from other persons whom the moving party is entitled to examine for discovery, or from the person he or she seeks to examine;
> (b) it would be unfair to require the moving party to proceed to trial without having the opportunity of examining the person; and
> (c) the examination will not,
> (i) unduly delay the commencement of the trial of the action,
> (ii) entail unreasonable expense for the other parties, or
> (iii) result in unfairness to the person the moving party seeks to examine.

There is a dearth of cases related specifically to the criteria for determining when a lawyer may be compelled to attend an examination as a witness in an estate proceeding. The principal dispute is usually over whether to produce the lawyer's file; the lawyer's examination is an adjunct to that issue.[62] This is probably because relevance, the primary consideration governing the production of the lawyer's file, also drives the Ontario Rules governing non-party examinations for discovery generally. Once the file is ordered to be produced courts do not hesitate to order an examination.[63]

Generally, the courts have interpreted Rule 31.10(2) to mean that the moving party must be prohibited by considerable difficulty,

61. *Re Nieweglowski Estate* (2009), 175 A.C.W.S. (3d) 987, [2009] O.J. No. 1241 (Ont. S.C.J.).
62. See, for example, *Bailey v. Bailey* (2007), 157 A.C.W.S. (3d) 501, [2007] O.J. No. 1842 (Ont. S.C.J.), and *Verch v. Weckwerth*, *supra*, footnote 51.
63. Another reason for the few decisions may be that the rules of civil procedure in other provinces differ from Ontario's Rules on this topic. Garry D. Watson and Derek McKay, *Holmested and Watson: Ontario Civil Procedure* (Toronto, Thomson Reuters Canada Limited, 1993) (looseleaf), vol. 4, at para. 31.28. Cases from other provinces are therefore of little assistance so the pool of possible disputes is relatively small.

delay or expense from getting the sought-after information from the people it may examine. The people whom the moving party may examine must actually or constructively refuse to provide the requested information.[64] There are no reported cases involving the examination of lawyers in Ontario estate disputes where these grounds have been argued basis for the refusal to attend an examination. Presumably this is because of the "one less witness" problem described at the outset of this article. It is assumed that, if the lawyer's evidence is relevant, then it is also necessary because the lawyer is likely the only dispassionate professional person to whom the deceased or incapable person expressed his intention.

An order to examine a lawyer is commonly made in conjunction with an order that she produce her file. The same order requiring the lawyer to be examined will usually also contain a paragraph that specifically releases the lawyer from her obligation of confidentiality and her obligation to protect privileged communications:[65]

> In giving directions with respect to the examination of a solicitor, the court frequently orders that the solicitor may give evidence concerning what would otherwise be privileged communications made by the former client and orders that any claim for solicitor client privilege or confidentiality is waived. It was reasonable for [the lawyer] to insist upon a court order directing him to attend the examination before disclosing privileged information.

(b) Conditions of the Examination

From the lawyer's perspective, little good is likely to come from an examination for discovery. She will likely feel, correctly or not, that a claim for professional negligence looms. Moreover, she must give up time to prepare for, and attend, the examination. Lastly, she may reasonably want to have counsel attend with her at the examination, at some cost.[66]

Rule 31.10(1) may impose "search terms respecting costs and other matters as are just" on the parties seeking to examine the lawyer. This can be used to give the lawyer some relief by requiring that the examining parties, or the estate pay the legal costs associated with, and compensate the lawyer for, preparation and

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64. *Keuhl v. Beachburg (Village)* (1990), 75 D.L.R. (4th) 193, [1990] O.J. No. 2127 (Ont. C.A.).
65. *Re Nieweglowski Estate*, *supra*, footnote 61, at para. 8.
66. Her insurer may insist on it.

attendance at the examination. Both these forms of compensation are discretionary.

(c) Costs of the Examination

There is little case law on point. Potts J. in the 1985 case of *Weiszman v. 491 Lawrence Avenue West Ltd.*[67] awarded no costs to the non-party being examined for discovery. His Honour held:

> Counsel for the plaintiff has suggested that it should be a term of my order that the defendants [who sought the examination] should be required to pay the costs of counsel for the non-parties at the examinations for discovery. I am not sure whether I would have authority to make such a condition but, even if I did, I would not do so. The non-parties are involved in the system of justice and they will have the right to retain counsel if they so wish or they can represent themselves.

Justice Potts does not explain what he meant by "involved in the system of justice". It appears (though the decision does not say) that the non-parties were witnesses to a slip-and-fall, not lawyers or police officers.

In *Lana International Ltd. v. Menasco Aerospace Ltd.*,[68] the court ordered the examining party to pay up to $5,000 towards the witness's legal costs of the examination. Master MacLeod concluded that the examination could cause unfairness to the witness. Not only did the witness complain of being harassed by counsel for the parties, he was worried about making statements that could expose himself to liability. To alleviate this potential unfairness, the witness should have a lawyer at the examination, paid for by the examining party.

In *Lafarge Canada Inc. v. Khan*,[69] a party to a Nova Scotia lawsuit sought letters rogatory against an Ontario resident. The Ontario court's consideration of the costs issue is also relevant to Rule 31.10 examinations:

> [77] Witnesses at trial are not normally afforded the right to counsel. They come to court pursuant to a summons to witness and they are required to give evidence before the court in spite of the inconvenience

67. (1985), 5 C.P.C. (2d) 160 (Ont. H.C.). Note that the case was decided under the "new" Rules, and not the "old" Rules of Practice.
68. (2000), 195 D.L.R. (4th) 497, [2000] O.J. No. 4798 (Ont. Div. Ct.). Justice O'Driscoll held that "The order under review was legal and thoughtful and arose out of a commonsense solution to the problem that the Master faced."
69. (2008), 89 O.R. (3d) 619 (Ont. S.C.J.), additional reasons (2008), 165 A.C.W.S. (3d) 993 (Ont. S.C.J.).

> and even potential embarrassment or upset. As Potts J. said in *Weiszman v. 491 Lawrence Ave West*, compliance with the legal process is a responsibility of Ontario residents.
>
> [78] That being said, a witness at trial is subject to the over-riding protection of the trial judge who can ensure that the witness is treated fairly and that his or her rights are protected. A non-party being discovered, sometimes in an unfamiliar and hostile environment, has no such protection.
>
> [79] In my view, a witness examined pursuant to letters of request should be entitled to legal representation at the examination.
>
> [80] As a general rule, the cost of retaining counsel, if desired, should be an expense of the witness and not the examining party. . .

Justice Strathy then explained why, on the facts of this case, the examining party should bear the cost of the lawyer for the witness despite the "general rule" to the contrary. There was evidence that: (i) the examining party would challenge the witness's credibility; (ii) the witness was impecunious; (iii) there was "history" between the witness and the examining party and so the witness was concerned that the examination could stray into irrelevant matters; and (iv) Nova Scotia's Rules permitted broad examinations, which, in Strathy J.'s opinion, "make it desirable that [the witness] be fully informed . . . concerning her responsibilities."

There is no case law specifically on whether a lawyer's legal costs should be paid where the non-party witness is the estates lawyer. Courts may take the view that lawyers, as "officers of the court" and people who are "involved in the system of justice" (Potts J.'s expression), should be prepared to "stand behind" the advice they gave to their clients. Conversely, a court may be more sympathetic to the lawyer's position where it has doubts about the relevance of the lawyer's evidence, or the extent to which an oral examination will add to what is set out in the paper file.

Compensation

There is recent case law that suggests that lawyers should be compensated for time preparing for, and attending, an examination. In *Primo Poloniato Grandchildren's Trust (Trustee of) v. Browne*,[70] the parties sought the court's direction on how to

70. (2011), 71 E.T.R. (3d) 185, [2011] O.J. No. 3787 (Ont. S.C.J.), Pattillo J. This citation is the decision respecting costs. The decision on the merits is at *Primo Poloniato Grandchildren's Trust (Trustee of) v. Browne* (2011), 65 E.T.R. (3d) 113, [2011] O.J. No. 59 (Ont. S.C.J.), additional reasons 2011

interpret the terms of a trust. The trust consisted of the original trust document, and two subsequent court-approved variations of the trust. The second variation was made in 1997. The beneficiaries of the trust sought directions because of the consequences to the trust of the significant downturn in the stock market in 2001-2002. There was no suggestion in the decision that the trust or the two variations had been negligently prepared.

The lawyer for the second trust variation was examined as a witness on the pending application pursuant to Rule 39.03 and, after the hearing, sought compensation for his time for preparing for and attending the examination. He sought compensation of $19,300 for his time. It appears that the hearing was substantial: the aggregate of the costs sought by all the parties totalled approximately $1.4 million.

One set of beneficiaries complained that the lawyer was examined as a "fact witness" and not as an expert and accordingly was only entitled to witness fees (*i.e*, conduct money). Justice Pattillo concluded that the lawyer should be paid for his time:[71]

> [The lawyer] was summoned to give evidence concerning his services as the lawyer who acted on behalf of the Trust and, in particular, as the lawyer who drafted the 1997 Variation. Although [the lawyer] was testifying primarily as a fact witness, his evidence was in relation to his work as a lawyer. In such circumstances, it is unreasonable to assume that because he was examined in his capacity as a lawyer in respect of legal work he did that he is only entitled to standard witness fees. As a professional being examined in respect of his work, [the lawyer] is entitled to be paid his normal hourly rate for both his reasonable preparation time and for his attendance at the examination.

This case was cited with approval in two recent commercial cases where accountants were witnesses on a motion and an application, respectively.[72] In all three cases, however, the amounts at issue and the professional fees related to the dispute were substantial. The court may take a different view when the estate, or the amount at issue, is modest.

ONSC 4400 (Ont. S.C.J.), affirmed 2012 ONCA 862 (Ont. C.A.), leave to appeal refused 2013 CarswellOnt 6495 (S.C.C.).

71. *Primo Poloniato Grandchildren's Trust (Trustee of) v. Browne*, *supra*, footnote 70, at para. 54.

72. *Guttman v. Dubé* (2013), 234 A.C.W.S. (3d) 285, [2013] O.J. No. 5634 (Ont. S.C.J. [Commercial List]); *DeGroote v. DC Entertainment Corp.* (2014), 236 A.C.W.S. (3d) 310, [2014] O.J. No. 19 (Ont. S.C.J. [Commercial List]), leave to appeal refused 2014 ONSC 1548 (Ont. Div. Ct.).

5. Protection for the Lawyer: The Deemed Undertaking Rule[73]

The estate lawyer who produces her file or submits to an examination for discovery will be concerned that the parties not use that evidence to start professional negligence claim against her that alleges that she did not properly record the deceased's intentions or accurately evaluate his capacity. The lawyer may also face a claim that would have otherwise gone undiscovered if she had not given evidence. For instance, a lawyer's will notes produced in a will challenge may reveal that the testator instructed the lawyer to make a specific bequest, which the lawyer omitted from the will. Rule 30.1, the "deemed undertaking" rule, gives the lawyer some protection from this risk.

(a) Description of the Deemed Undertaking Rule

Rule 30.1.01(1)(a) provides that evidence obtained under Rules 30 (*i.e.*, production of the lawyer's file) or 31 (examination for discovery of the lawyer) is subject to the deemed undertaking. Rule 30.1.01(3) says that:

> All parties and their lawyers are deemed to undertake not to use evidence or information to which this Rule applies for any purposes other than those of the proceeding in which the evidence was obtained.

Taken without qualification, this means that evidence produced pursuant to Rules 30 and 31 may not be used in a subsequent lawsuit against the lawyer.

The Ontario Court of Appeal has set out the rationale for the deemed undertaking rule:[74]

> The primary rationale for the imposition of the implied undertaking is the protection of privacy. Discovery is an invasion of the right of the individual to keep his own documents to himself. It is a matter of public interest to safeguard that right. The purpose of the undertaking is to protect, so far as is consistent with the proper conduct of the action, the confidentiality of the party's documents. It is in general wrong that one who is compelled by law to produce documents for the purpose of particular proceedings should be in peril of having those documents used

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73. An earlier version of this section appears as: Sean Lawler, "An Order for Directions is Not the Place to Exclude the Application of the Deemed Undertaking Rule", *Deadbeat*, April 2013 (Ontario Bar Association).
74. *Kitchenham v. AXA Insurance (Canada)* (2008), 94 O.R. (3d) 276 (Ont. C.A.), at para. 31.

> by the other party for some purpose other than the purpose of the particular legal proceedings.

The Supreme Court of Canada has said:[75]

> The public interest in getting at the truth in a civil action outweighs the examinee's privacy interest, but the latter is nevertheless entitled to a measure of protection. The answers and documents are compelled by statute solely for the purpose of the civil action and the law thus requires that the invasion of privacy should generally be limited to the level of disclosure necessary to satisfy that purpose and that purpose alone . . . The general idea, metaphorically speaking is that whatever is disclosed in the discovery room stays in the discovery room unless eventually revealed in the courtroom or disclosed by the judicial order.

There can be consequences for the party who contravenes the deemed undertaking rule. In 2008, Richard Swan surveyed the relevant cases and said that:[76]

> Breach of the deemed undertaking may attract a variety of remedies, including a sanction for contempt, stay or dismissal of a proceeding, or an order refusing to permit amendments to pleadings. The remedy imposed by the court tends to be specific to the facts of the case and to be tailored to fit the particular circumstance of the breach in question.

Giammanco v. Zahoruk[77] is a rare example of a case where the court was asked to impose sanctions on an applicant to an estate dispute who breached the deemed undertaking rule. In that case, a will-challenger examined the lawyer who drafted the will, and then sued him on the basis of the evidence he gave during his examination. The lawyer sought a stay of the negligence action. Mme. Justice Mossip did not grant the stay, but as a consequence of the breach of the deemed undertaking: (i) rejected the will-challenger's request to consolidate the will challenge with the lawyer's negligence action; (ii) awarded the lawyer his costs of the motion; and (iii) invited the lawyer to bring a separate motion to stay the negligence action.

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75. *Doucette (Litigation Guardian of) v. Wee Watch Day Care Systems Inc.; Juman v. Doucette* (2008), 290 D.L.R. (4th) 193, [2008] S.C.J. No. 8 (S.C.C.), at paras. 25-26. The Supreme Court of Canada continued that a secondary rationale for the deemed undertaking rule is that a third party who is security in his privacy will be more inclined to candidly produce documents when requested.
76. R.B. Swan, "The Deemed Undertaking: A Fixture of Civil Litigation in Ontario" (2008), 28 Advocates' Soc. J. 16, at pp. 16-22.
77. (April 2, 1998), Mossip J., Ont. Ct. (Gen. Div.). Described in I.M. Hull, "The Deemed Undertaking Rule and Estate Litigation" (1998), 18 E.T.P.J. 253.

How the Parties can Avoid the Effect of the Deemed Undertaking Rule

Rule 30.1.01 does not:

(a) apply:
  (i) if the person who disclosed the evidence consents to the further use of the evidence;[78]
  (ii) to evidence that is:
    (A) filed with the court;[79] or
    (B) that is given or referred to during a hearing; or
    (C) to information obtained from evidence obtained through (A) or (B);[80]

(b) prohibit the use of evidence obtained to impeach the testimony of a witness in a separate proceeding.[81]

An applicant may obtain relief from the deemed undertaking rule. Rule 30.1.01(8) provides that:

> If satisfied that the interest of justice outweighs any prejudice that would result to a party who disclosed evidence, the Court may order [that the deemed undertaking rule] does not apply to the evidence or to information obtained from it, and may impose such terms and give such directions as are just.

How the courts have exercised their discretion to relieve a party from the deemed undertaking rule depends on the circumstances of the case. In *Juman*, the Supreme Court of Canada held that, "where discovery material in one action is sought to be used in another action with the same or similar parties, and the same or similar issues, the prejudice to the examinee is virtually non-existent and leave will generally be granted."[82]

However, where the produced evidence is sought for an "extraneous purpose, or for an action wholly unrelated to the purposes of the proceeding in which discovery was obtained" then the courts generally do not authorize production "in the absence of some compelling public interest."[83] The courts have found there to

78. Rule 30.1.01(4).
79. See *Moore v. Bertuzzi* (2007), 88 O.R. (3d) 519, [2007] O.J. No. 5113 (Ont. Master).
80. Rule 30.1.01(5).
81. Rule 30.1.01(6).
82. *Juman*, *supra*, footnote 75, at para. 35. See also *Bluewater Health v. Kaila* (2012), 37 C.P.C. (7th) 15, [2012] O.J. No. 4387 (Ont. C.A.), at para. 11.
83. *Juman*, *supra*, footnote 75, at para. 36.

be a strong "public interest" in cases where a doctor obtained a plaintiff's health records and sought to use them in a related professional disciplinary proceeding.[84] More recently, the court gave relief from the deemed undertaking where the sought-after documents would be used to facilitate the possible settlement of claims involving losses suffered by "hundreds of individuals and corporations."[85] In those cases, the public interest outweighed the privacy interest of the entities from whom production was sought.

The time to bring a motion, under Rule 30.1.01(8) for relief from the deemed undertaking rule, is after the documents have been produced, and not at the time the order for directions is made (*i.e.*, at the outset of the litigation). It will be difficult for an applicant to persuade the court of the public interest in waiving the deemed undertaking rule before the applicant even knows what will be learned from the third-party evidence: which documents or statements does the applicant want to use? For what purpose? What conditions, if any, should be put on the use of those documents? These issues can only be answered after production.

The deemed undertaking rule helps "level the playing field" for the lawyer who has produced his file or who has been examined. In most types of litigation, the plaintiff usually does not see the defendant's documents before the commencement of the litigation. Generally the plaintiff must first start the law suit, and take the risk that the defendant's documents or oral evidence will undermine his case and that he will face an adverse cost consequence. Without the deemed undertaking rule, orders for direction that: (i) are obtained at the outset of the litigation; and (ii) require the estates lawyer to provide evidence, deprive lawyers of this procedural protection: the potential plaintiff can get the lawyer's file, decide whether to sue the lawyer for in relation to the existing dispute, and even scour the lawyer's file for unrelated claims. That would be an unjustified exception to the "private right to be left alone with [one's] thoughts and papers, however embarrassing, defamatory and scandalous". A prospective plaintiff to a lawyer's negligence claim arising out of a will challenge should face the same risk as a plaintiff in any other type of litigation.

The deemed undertaking rule is not an absolute protection for lawyers who give evidence in estate litigation cases. However, it

84. *K. (S.) v. Lee* (2000), 2 C.P.C. (5th) 325 (Ont. S.C.J.), additional reasons 2000 CarswellOnt 3853 (Ont. S.C.J.). See also Swan, *supra*, footnote 76, at para. 19.
85. *Ontario (Securities Commission) v. Norshield Asset Management (Canada) Ltd.* (2010), 100 O.R. (3d) 419 (Ont. S.C.J. [Commercial List]).

does require the potential professional negligence claimants to review the evidence carefully and weigh the costs and benefits of a lawsuit against the lawyer.

6. Conclusion

The estates lawyer may think of her file, and in particular her notes, as private to everyone except her and her client. But the lawyer's estate file may contain evidence of central importance to determining what a deceased or incapable person intended or whether they lacked capacity. Where the file contains "relevant" evidence, that evidence will be produced. The doctrine of solicitor-client privilege is sufficiently flexible to accommodate this.

The lawyer's principal concern will be her exposure to a malpractice claim. The deemed undertaking rule provides a measure of protection. However, the lawyer's best protection is thorough and comprehensive notes. When the lawyer receives a request for the production of an estates file, it is prudent to review it carefully to determine whether, and to what extent documents should be produced. Lastly the lawyer should contact her insurer, which may want to provide guidance on how to respond to the request.

Will Plan Meetings – a Model

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Picture your last will planning meeting.

Your clients sat across the table from you. You talked. They talked. Everyone hoped that the other understood what they were saying.

Will planning can be a very complex exercise. There are a lot of moving parts, lots of "What ifs?". For clients, making a will is often an anxious experience. The multitude of decisions and options can be overwhelming, the legal concepts and terminology, intimidating.

Will challenges are more common now than ever. They almost always focus on "Did she really understand the Will?" And the lawyer is the primary witness in most of those cases.

Is there a better way of ensuring that your client understood what was really in the Will and why it was there?

Perhaps a more systematic, structured process is better for both the client and the lawyer. Better for the client because it is clear and easy to understand. Better for the lawyer because it is easier to defend against claims that "Mom didn't *really* understand what she was doing".

Here is a model that has two components: simplification and visualization.

Simplification

Despite all the complexities that lawyers have to consider, the options for the client's consideration can be easily simplified.

From the client's point of view, there are only two ways of giving a gift in a Will – what the Model refers to as "Absolute" and "Trust". Explaining those two

concepts can also be very straightforward with the proper warnings attached such as:

> "Absolute gifts are the simplest kind. The recipient can do anything with the inherited asset including spending it all or giving it away when the recipient dies to whomever he or she wants."

A nifty way to explain if the client wants to use a trust is:

> "If you (the client) use the word "BUT" in describing the gift, you know you don't want an absolute gift. You have indicated that you need a trust for that gift."

Breaking it down into just two options makes it less overwhelming for the client and easier to focus on decisions.

The second component of the simplification process is creating a logical flow for the decisions. Almost all will plans can be divided into no more than 3 fixed scenarios-

1. Your spouse survives you.
2. Your spouse predeceases you, but you have descendants.
3. You have no descendants.

Some plans may not even have all three scenarios. Going through each scenario, one at a time, keeps the client focussed and avoids drifting off to innumerable other issues.

If your spouse is alive, do you want to give everything to your spouse? Absolute or in a trust? Perhaps some assets are held in trust while others are absolute. Maybe the client wants to leave initial gifts for the children. Absolute or trust?

Like the simplicity of "Absolute vs. Trust", developing a trust can also be broken down into a few simple concepts. When discussing a monetary trust in simple terms, it can be broken down into 6 questions:

1. Beneficiaries?

2. “Duration“? When does the trust end?
3. “Mandatory Payments“? (e.g. staged distributions at certain ages or an required minimum annual payment)
4. “Discretionary Payments“? Are they permitted or are there any limits on those payments?
5. Trustee(s)? Who are the primary and alternates?
6. “Gift-Over“? What happens to any balance when the trust ends?

For trusts for specific property, the lawyer can add other decisions, such as payment of expenses, right to purchase, ability to buy a replacement property and other specific issues.

Visualization

Despite the complexities, most of us simply keep our own notes to track the conversation, advice, discussion and instructions.

Isn’t *seeing* better than hearing?

Visualization of important concepts and decisions encourages the client to reflect and consider their ramifications. It also increases the likelihood that all important issues are canvassed and accurately recorded.

The benefit of visualization is it keeps the client and the lawyer focussed on the same issues and decisions. It avoids miscommunication. It serves as a reminder of where we are in the overall plan and where we are going.

It can be as simple as using a whiteboard or using specialized software that visualizes the instructions, tracks values of assets, income tax effects of certain distributions, probate tax, and automatic cues the lawyer on issues to be considered.

Here is an example of the Model:

ABSOLUTE
vs.
TRUST

House
Cottage
RRSP
TFSA
Non-Reg Investments
Life Insurance - $1M
Life Insurance - $500K
Personal Effects
Bank Accounts
Florida Property
Corp Shares

SPOUSE IS ALIVE

Everything absolute to spouse except:
Life insurance $500K equally among kids – Trusts as below

SPOUSE IS NOT ALIVE

$10,000 to the World Fund
Balance = to kids – TRUST
Duration age 30
Mandatory Payments ¼ at age 25
Discretion Unlimited
Gift-over to other children
Trustee(s) John and Frank, jointly

IF NO ONE IS ALIVE

50% - to Jim's siblings
50% to Susan's siblings

(c) Jordan Atin 2016

Surviving Spouse

Available Assets

- Home
- Cottage
- Bank Accounts
- Registered Plans
- TFSA
- Non-Registered Investments
- Personal Effects
- Life Insurance
- Corporate Shares

▸ Appointment

▾ Joint Assets And Designated Assets

Assets Received Absolutely Outside of Estate

Add Person

Spouse: Suzanne Sample
Assigned Assets
Drag an asset here
Total: $0

Other Person: Enter Name
Assigned Assets
Drag an asset here
Total: $0

▾ Initial Gifts

Absolute Legacy | Trust Legacy

Absolute Legacy - Controller
Double click to open dialogue
Assigned Assets
No Assets available

Assigned Gifts

Add All Gifts to No Spouse Page

▾ Balance Of The Estate

Estate Summary - Drag and drop assets from Available Assets list

Added Assets

Gross Total:	Probate Tax:	Total Cash Legacies:
$ 0	$ 43,275	$ 0
Total Debts:	Income Tax:	Net Total:
$ 350,000	$245,000	$ -638,275

When broken down visually, the client can start to process the decisions that have to be made and their impact. They can also highlight those questions that still need answers.

Once each scenario is drawn out, the display itself contains the will plan. This ensures that client and the lawyer understand one another and that they are all on the same page.

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