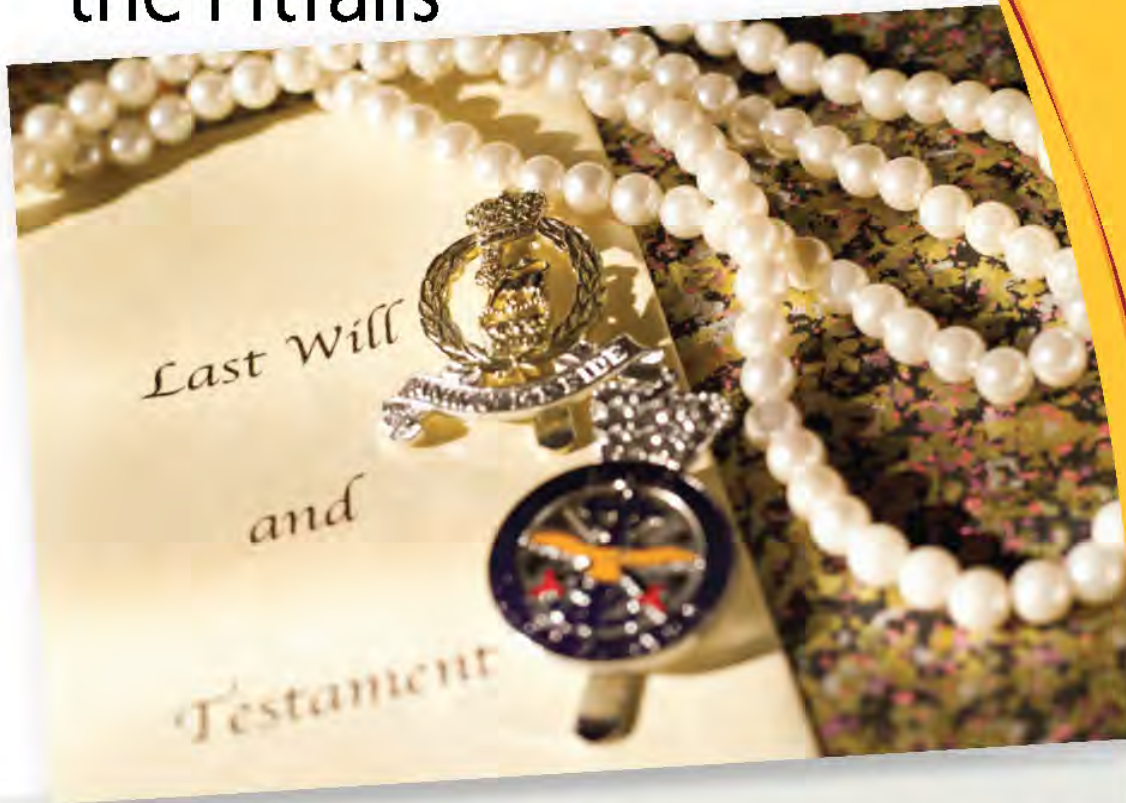




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Estate Planning – Avoiding the Pitfalls



Accessibility and Convenience

Lancaster, Brooks & Welch LLP have offices in both St. Catharines and Welland which are conveniently located in the downtown core.

Regular office hours are Monday to Friday from 8:30am to 5:00pm.

We are happy to make appointments at other times to satisfy our clients' needs.

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You've worked hard and are financially comfortable. You're looking forward to enjoying your retirement, but you're also thinking of the future. Should you rearrange your financial affairs to make things easier for those left behind on your death? Should you give some of your assets to your spouse or children during your lifetime or put them in joint names? Will the Ontario government implement an inheritance tax?

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A lawyer specializing in estate planning can help answer these questions. The first goal should be to ensure there are enough assets available to take care of each other. The second, to make sure bequests are received in a cost-effective way. Proper estate planning requires a strategy designed to fit particular needs. Depending on the amount and type of assets, a plan could range from the simplest of wills to a complicated combination of a will, a trust agreement and a holding company.

Let's work our way through some of the questions that might arise in an estate planning interview.

Joint Tenancy

My spouse and I own our house as joint tenants. What happens if one of us dies?

The surviving joint tenant legally becomes sole owner of the house. This is generally true of any jointly owned asset, such as a bank account or Guaranteed Investment Certificate. Recent case law suggests if one of the joint tenants was really a trustee (for example, a son being a joint tenant of a bank account so banking could be done by the son for the parent), then this presumption of law can be rebutted. For this reason, we advise our clients to insert in their wills that all their joint tenancies are true joint tenancies and the surviving tenant is the true owner of the asset, unless the reverse is clearly specified. With respect to real estate, it is prudent to make an application to change the parcel register so that title rests in the survivor's name.

Spouse as Sole Beneficiary

I have a Will. Everything goes to my spouse if I die first. We own everything as joint tenants. What happens when I die?

On your death, your spouse automatically becomes legal sole owner of all your assets. If they are not jointly owned, it is likely that probate will be needed.

Probate

What does it mean to probate a Will?

Technically, one no longer probates a will. Rather, an application for a Certificate of Appointment of Estate Trustee with a Will is made. The result is identical to the process of probating a Will that was followed for hundreds of years. For most Wills, this is fairly simple. A judge reviews the application and if the process has been properly followed, they will confirm the Will is indeed the deceased's Last Will and Testament and provide a Certificate of Appointment of Estate Trustee with a Will. No one

then needs to be concerned about whether there is a more recent Will or whether the probated Will is valid. Once the judge grants this certificate, your executor can then deal with any estate assets.

Executors

What does an executor do, and how do I choose one?

The terms "estate trustee" and "executor" are synonymous. That person is in charge of administering your estate and obligated to fulfil the terms of your will and account to your beneficiaries and, if necessary, the court. The executor's responsibility is to pay debts, including taxes, from the estate before distributing the assets. They may seek professional advice (for example, in legal or accounting matters), but ultimately the executor must approve all actions of those professionals. The executor should be someone in whom you have confidence, not someone who is older than you but perhaps younger. They may be a family member, close friend, professional advisor or trust company.

Child as a Joint Tenant

My spouse predeceased me. My daughter will inherit my house when I die. Should I make her a joint tenant with me in order to avoid probating my will?

That takes us back to my first question. Your care and support are the most important matters. By making your daughter a joint tenant, you're opening the door to negative possibilities. The selling, mortgaging or any other dealing in the ownership of the house is no longer within your control. If your daughter were injured and unconscious, you would be unable to sell your home without either dealing with the person who holds your daughter's power of attorney or a court-appointed person. If your daughter is ever sued successfully, that creditor could complicate any transfer of ownership of your home.



Also, if you should fall out with your daughter you would have a problem, as she is co-owner with you.

Non-Spousal Considerations

If you do hold an asset jointly with someone other than your spouse and it is your intention that this person receive title to that asset upon your death, you should ensure that your intentions are clearly noted in writing.

Family Law Act

How does the Family Law Act affect making a Will?

This act places the surviving spouse in a position no worse than had they separated during each others' lifetime. If the deceased's Will would produce a worse result, the surviving spouse may elect, within six months of the date of death, to take the provisions of the act rather than those under the Will.

Taxes

That's an easy question if all of the deceased's assets are given to the surviving spouse. Currently, there are no taxes to be paid (either federal or provincial) when an individual leaves their estate to his or her spouse.

What happens if the asset is left to someone other than a spouse?

Generally, an individual is deemed to have sold everything he or she owns at the time of death at the fair market value of that asset. This could result in a deemed capital gain if the asset is worth more at the time of death than its initial cost. For example, if Joe bought stock in 1995 valued at \$10,000 and when he died in 2006 it was worth \$15,000, he would have a capital gain of \$5,000, which would be taxed on the same basis as if he had on the date of his death sold those shares for \$15,000.

Why does this not happen between spouses?

Between spouses there is a roll-over. The surviving spouse acquires the asset at the deceased spouse's cost base, but when they sell the asset, the built-in capital gain surfaces and the government gets its piece of flesh. Back to Joe. If his spouse inherits the stock, there would have been no immediate capital gain. If his spouse later sold the stock for \$20,000, she would have a \$10,000 capital gain. Her cost base is Joe's original cost base, \$10,000, and her gain is calculated from that point. The roll-over postpones or defers the tax, but it does not eliminate it.

Wait a moment! What about my house?

Not to worry. One of the few exemptions from the capital gains regime is a principal residence. If you have always used the house as your principal residence, there is no tax payable on its transfer, no matter who acquires it.



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Trusts

What is an inter vivos trust and what use does it have?

An inter vivos trust is a trust created during one's life and has many different uses. A trust would allow Joe to give something to his children during his lifetime without giving up control of that asset. For example, the shares Joe gave to his children could have been placed in a trust that he controls. If the company had excess income that he desired to give to his children, the trust could allow him to sprinkle the money among them at his discretion. This could be done as often as he wished and in each case it could be on a different basis.

If an inter vivos trust is established during my lifetime, what happens on my death?

On the death of the settlor (the person who started or "settled" the trust) the terms of the trust simply are followed. Often the settlor is the initial trustee. A trustee is the person charged with administering the terms of the trust and their role is similar to that of a Will executor. The trust agreement will normally appoint successor trustees or describe a method of appointing them. The trust agreement will provide for a time of distribution of the capital of the trust. Often this is either the date of death of the settlor or a specific point of time following their death.

What is a testamentary trust?

A testamentary trust is a trust created through an individual's Last Will and Testament. For example, a portion of the estate you wish your child to inherit could be placed in trust under certain terms. The child, for instance, may not be entitled to the income from the trust until a certain age and then might receive a portion of the capital at another age and the balance at a later age.

What are the other advantages of a testamentary trust?

In addition to the beneficiary not receiving access to the capital until the terms of the trust have been satisfied, there are also income tax advantages. It is sometimes prudent to create a spousal trust even when your spouse is receiving the entire estate. In those circumstances, part of the estate would go directly to your spouse and part would go to a spousal trust. The net result of this is that both your spouse and the trust will pay less income tax on the income derived from the estate than would be the case had they received the entire estate and therefore generated all of the income in their hands.

Last Word

As you can see, the variations are endless. The core goal remains the same, however. Husband and wife must first provide for each other. Secondly, they should be concerned about other beneficiaries. Advice on an estate plan can be as varied as the different circumstances in which people find themselves.

One word of caution: Any plan must be as flexible as possible. The unforeseen constantly happens. In the 1950s and 60s it was not uncommon for one spouse to leave a monthly stipend to the other in an amount that at the time seemed generous. The inflationary period following turned it into a miserly amount. Flexibility and simplicity should be the target.

The information provided in this brochure is designed to provide topical information of a general nature only. You may wish to discuss any specific matter with your lawyer and you should feel free to do so at any time. This material is provided for information purposes only, not as legal advice, and is not intended to be exhaustive of your rights under the relevant legislation.

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Holding Companies

Earlier you referred to a holding company. What's that all about?

Holding companies are used when an estate freeze is undertaken. I previously explained that a person is taxed on death by way of a deemed capital disposition. That means if Joe owns an asset, such as a business that is increasing in value, the amount of tax that will be incurred upon his death is constantly increasing as the value of that asset increases. We can transfer this asset into a company on a roll-over (tax-deferred) basis. Joe would receive shares in the company. Those shares will not increase in value, but he has sufficient voting rights attached to them to control the company. The value of Joe's shares has been frozen at the current level, hence the name estate freeze. Other shares are often issued in the company to the children. These shares are created so that they increase in value as the asset increases. In this way, the tax on the increase in the value of the asset from the date of the freeze to the date of Joe's death is deferred until his child dies or transfers the shares.

Deferral of Tax

Can I avoid that tax?

Generally tax cannot be avoided in the sense that it will never be paid. Often a deferral is the best that can be achieved. In my example, the tax that otherwise would be payable on Joe's death is not paid until his child dies or transfers the shares. The deferral of taxes is a major benefit. By retaining the stock for 20 years, his child will have had the benefits of those tax dollars for that entire period.

Are there no total exemptions from tax?

Yes, there are a few exceptions to the general rule of taxation. In those cases, although tax would normally be paid, a specific section of the Income Tax Act exempts the situation so that no tax is payable. The sale of a home that has always been occupied as the owner's principal residence is one example. There is also an exemption up to a certain maximum value on the sale of a family-held active business. Your accountant and lawyer can give you more details.