

**Succession Planning for
Preserving Assets**

Toolbox Seminar

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**Obstacles to Wealth
Preservation**

- Taxes
- Creditors
- Litigation
- “Wrong” executors or attorneys
- Beneficiary Error

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Common Will Myths

- My spouse gets it all anyway
- My spouse owns half of everything anyway
- There are no longer succession duties
- Testamentary trusts no longer “work”

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Common Myths

- A trust can only continue for 21 years
- Insurance and RSP beneficiary designations in Wills are subject to probate
- The \$25 will kit is lawyer approved

Planning Tools

- Multiple wills
- Testamentary trusts
- Spousal trusts
- Carefully considered powers of attorney for property
- Alter ego trusts for those over 65
- Principal residence trusts

Taxation on Death

- Estate administration tax ("EAT")
- Federal tax on capital gain
- U.S. estate tax
- Land transfer tax
- Other foreign tax

Will Planning

- Multiple Wills to avoid 1.5% EAT on certain assets and the risk of a provincial tax audit on private company shares and loans, personal articles
- Utilize spousal rollovers to qualifying spousal trusts
- Avoid rights to purchase real estate by beneficiaries, structuring instead as a share of residue

Will Planning ...cont'd

- Choose sensible executors
- Name more than one executor
- Consider majority rule
- Provide a mechanism for replacing executors/trustees
- Consider special executors for business and other specialized assets

Trust Wills

- Assets gifted outright to a surviving spouse may never find their way to the children
- Trusts can prevent the survivor from giving everything to a second spouse
- Trusts for insurance proceeds, either under the will or separate insurance trusts protect the beneficiary and preserve the capital

Trust Wills ...cont'd

- Trusts continue to be an essential will planning aid
- Income splitting advantages continue to apply if beneficiaries have little or no other income
- Trusts can assist in protecting assets from the beneficiary's spouse on marriage breakdown

Trust Wills ...cont'd

- Protect against the surviving spouse remarrying and leaving the assets to the second spouse
- Ensure children from prior marriages are not cut out by the step parent
- Protect the young or spendthrift beneficiary
- Protect beneficiaries from spousal claims

Trust Wills ...cont'd

- Think ahead to the number of years the trust will continue
- Consider Successor trustees
- Anticipate the 21 year deemed realization of capital property
- Include
 - Power to effect a post mortem estate freeze
 - Power to move trusts offshore



Principal Residence Trust Wills

- Principal Residence Trust for surviving spouse
- Preserves capital interest for residual beneficiaries (typically children)
- Consider how expenses will be paid
- Consider effect of remarriage

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Principal Residence Trust Wills ...cont'd

- Principal Residence trusts for minor children, or until a specified age
- Allows for continuity of stable home environment if both parents die
- Consider how expenses will be paid
- Consider who will have the right to reside in the home

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Power of Attorney

- Take care in who is named
- Preferably name at least 2 attorneys
- Name special attorneys for business interests
- Instructions on management issues
- Power to effect tax minimizing estate planning measures, such as an estate freeze

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Alter Ego Trusts

- Settlor must be 65 and over
- All the income must be paid to the settlor and no one other than the settlor can receive capital
- More comprehensive document than a power of attorney

Alter Ego Trusts ...cont'd

- After death of settlor, all income is taxed in the trust at top marginal rates
- Since the demise of the testamentary income splitting trust, alter ego trusts are much more attractive planning vehicles

Alter Ego Trusts ...cont'd

- Not subject to probate
- Saves estate administration tax
- Privacy – not a public document
- Can protect the settlor from predatory caregivers and others
- Trusts already existing at death are harder to contest

Beyond Wills and Powers of Attorney

- Estate Freeze in favour of a Trust:
- Defer tax on future gain
- Limit tax liability on death to current gain
- Multiplying the \$800,000 capital gains exemption on qualifying small business corporation shares and other income splitting opportunities
- Maintain control through family trust and voting shares

Asset Protection

- Hold "Family" assets in name of non-active spouse
- Separate real estate from Opco
- Designate beneficiaries of Life Insurance and RRSP's
- Joint property ownership
- Principal residence trusts

Asset Protection ...cont'd

- Alter Ego and Joint Partner Trusts
- Hold assets in offshore jurisdictions
- Offshore creditor protection trusts
- Multiple trusts for different family factions to avoid tying up the estate administration in litigation

Asset Protection – Family Law Claims

- Domestic Contracts
- Life Insurance to discourage *Family Law Act* elections on death
- Segregating inherited assets
- Structuring ownership of business assets to qualify as “excluded property”

Gifts to Married Children

- Gifts after marriage are not excluded if used to invest in a matrimonial home or commingled in a joint account with the spouse
- Always have a deed of gift to document it
- Consider loans instead
- Take back security where possible
- Consider a principal residence trust

In Terrorem Will Clauses

- *In terrorem* clauses typically threaten to disinherit the beneficiary who brings a claim to contest the will
- Must be a gift over to others, not just failure of the gift if a claim is brought
- Consider making the signing a full release, a condition precedent to the gift

Inter Vivos Trusts

- Will challenges are easily made under the *Rules of Civil Procedure*
- *Inter vivos* trust challenges are more difficult
- Trusts are not public record like probated wills
- Off shore trusts in creditor protected jurisdictions may be recommended

Asset Protection Trusts

- Where the family might fight – for example blended families
- Consider multiple *inter vivos* trusts for different family factions
- Separate the children from first marriage and step parent
- Taxpayers under 65 may trigger tax on capital gain

Educate the Beneficiaries

- Net family property under the Family Law Act excludes gifted or inherited property received after the date of marriage, and property traced to the gift or inheritance
- Declaration by donor/testator can also exclude any income or increase in value

Educate the Beneficiaries

...cont'd

- Protection lost if beneficiary puts assets in joint account with spouse or in name of spouse
- Inherited or gifted property put into a matrimonial home will lose its excluded status

Foreign Real Estate

- Immoveable property generally subject to domestic law of the jurisdiction
- Consider whether forced heirship applies, or whether there are domestic taxes payable on death

Foreign Real Estate ...cont'd

- Advisable to have a separate Will prepared by counsel in the foreign jurisdiction in the foreign language
- Advisable to name an Executor who is resident in the jurisdiction to avoid probate problems where there are foreign executors

U.S. Real Estate

- Ownership by Canadians of U.S. real estate continues to be a problem in planning to avoid U.S. estate tax
- Holding through a Canadian resident corporation no longer tax neutral
- Non-spousal Canadian resident trusts are subject to the 21 year deemed realization of capital property

U.S. Real Estate ...cont'd

- Non U.S. citizens resident outside the U.S. subject to U.S. estate tax on U.S. *situs* assets
- U.S. *situs* assets include real property in the U.S.
- 60,000 exemption for non-citizens
- Protocol provides additional relief

U.S. Estate Tax-Treaty Protocol

- Protocol provides for exemption proportionate to value of U.S. assets over value of worldwide estate
- Formula:

$$\frac{\$ \text{ U.S. } 5.45 \text{ m. } \times \text{ value of U.S. } \textit{situs} \text{ assets}}{\text{value of worldwide assets}}$$

U.S. Estate Tax-Treaty Protocol

...cont'd

- No tax if worldwide estate value is less than U.S. \$5.4 m. (for 2016)
- Marital credit enables the pro-rated exemption for Canadian resident non-U.S. citizens to be doubled for transfers to spouse or spouse trust

U.S. Estate Tax-Treaty Protocol

...cont'd

- Modified tax credit relief for U.S. estate tax paid by Canadian residents in respect of assets subject to Canadian tax on capital gain in same year
- Tax credit relief for cross-border charitable donations

U.S. Estate Tax

- Transfers to qualified domestic trust (QDOT) enable deferral of tax to death of second spouse
- QDOT may be established under testator's will or by surviving spouse
- Rules for QDOT must be strictly followed

Holding Title to U.S. Real Estate

- Joint tenancy results in the entire value being considered part of the U.S. estate of the first to die
- Tenants in common preferable
- Each spouse can leave their interest in a testamentary spousal trust
- Where the threshold may be exceeded, recommended structure is to hold U.S. real estate in a Canadian trust

Holding Title to U.S. Real Estate ...cont'd

- Consider having the spouse with the smaller worldwide estate own the U.S. *situs* property; hold the U.S. *situs* property in a spousal trust under the title holder's will
- Consider non-recourse mortgage: some U.S. commercial lenders will lend up to 65% of the value

Holding Title to U.S. Real Estate ...cont'd

- If one spouse is a U.S. citizen, preferable to have the U.S. citizen spouse hold the U.S. real estate as the combined exemption is \$4m.
- Have the U.S. citizen spouse leave the U.S. real estate in a testamentary spousal trust on death

Summary

- Trusts are a critical tool to address:
 - Creditor claims & beneficiary spousal claims
 - Issues of a spendthrift beneficiary
 - Control over assets passing to a surviving spouse who may remarry
 - Second spouse excluding children of the first marriage
 - Avoiding 1.5% EAT by an *inter vivos* trust

Summary

Tools for Preserving Asset Succession:

- Multiple Wills
- Careful choice of executors
- Protective Trusts in Wills
- *Inter Vivos* Principal Residence Trusts
- *Inter Vivos* Trusts to hold U.S. real estate
- *Inter Vivos* Alter Ego Trusts
- Off shore creditor protection trusts
- Educating beneficiaries
