# The Private Wealth & Private Client Review

Sixth Edition

**Editor**
John Riches

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# THE PRIVATE WEALTH & PRIVATE CLIENT REVIEW

SIXTH EDITION

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# PREFACE

## I INTRODUCTION

At a macro level, the dominant trend affecting the private wealth arena in the last 12 months continues to be the impact of various supranational initiatives seeking greater transparency with respect to anti-money laundering regimes and tax information exchange. I propose to focus in this year's introduction on the central importance of the concept of 'beneficial ownership' and the theme of convergence in the increasingly interconnected arenas of anti-money laundering policy and tax information exchange.

The clearest examples of this trend can be found in the introduction of centralised beneficial ownership registers, especially in the European Union and the Crown Dependencies and Overseas Territories of the United Kingdom (generally collectively referenced as CDOTs).[1] There are two specific manifestations of this:

*a* corporate beneficial ownership registers; and
*b* trust beneficial ownership registers.

In parallel, 2017 has witnessed the first substantive reporting by the first wave 'adopters' of the Common Reporting Standard (CRS) in the context of the 2016 calendar year.

I would like to first reference the common definitions that connect CRS with beneficial ownership registers and then refer in detail to the UK domestic trust register that was introduced by Regulations adopted in June 2017[2] (2017 MLR) before noting some key developments in the CRS domain.

### i Common use of beneficial ownership concept

The key 'source document' with respect to the concept of beneficial ownership is the Financial Action Task Force (FATF) 2012 Recommendations.[3] These recommendations were introduced as part of the international anti-money laundering policy but have been adopted as an essential element of the international tax information exchange policy implemented by the CRS.

1 These jurisdictions includes Jersey, Isle of Man, Guernsey, Cayman Islands, Bermuda and British Virgin Islands.

2 To give them their full title, 2017 No. 692, The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017.

3 FATF/OECD (2013), International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation, The FATF Recommendations February 2012, FATF/OECD, Paris, available on www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF_Recommendations.pdf.



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This is clearly confirmed in a CRS context by the CRS Commentary on the concept of controlling persons. Paragraph 132 of the interpretive notes to Recommendation 10 on Customer Due Diligence, states:

> *Subparagraph D(6) sets forth the definition of the term 'Controlling Persons'. This term corresponds to the term 'beneficial owner' as described in Recommendation 10 and the Interpretative Note on Recommendation 10 of the Financial Action Task Force Recommendations (as adopted in February 2012), 13 and* ***must be interpreted in a manner consistent with such Recommendations, with the aim of protecting the international financial system from misuse including with respect to tax crimes.***[4]

The FATF recommendations lead to a position where one essentially moves away from a strict legal definition of who might be entitled to enjoyment of an asset as a beneficial owner to an expanded concept. Under these rules, if it is not possible to identify a beneficial owner based on 'ownership interests' it is necessary to identify a beneficial owner based on 'control' even though the person or persons who control a legal entity have no capacity to call for the assets of the entity for their own personal benefit. In addition, as a last resort, if no 'ownership' or 'control' test can be satisfied, the final step is to look to the 'senior managing official' of the entity at the top of the ownership chain. This three-level ordering of who is to be regarded as the 'beneficial owner' is taken from the interpretive notes to Recommendation 10 of the FATF 2012 Recommendations:[5]

> *Identify the beneficial owners of the customer and take reasonable measures to verify the identity of such persons, through the following information:*
>
> *(i) For legal persons:*
> *(i.i) The identity of the natural persons (if any – as ownership interests can be so diversified that there are no natural persons (whether acting alone or together) exercising control of the legal person or arrangement through ownership) who ultimately have a controlling ownership interest in a legal person; and*
> *(i.ii) to the extent that there is doubt under (i.i) as to whether the person(s) with the controlling ownership interest are the beneficial owner(s) or where no natural person exerts control through ownership interests, the identity of the natural persons (if any) exercising control of the legal person or arrangement through other means.*
> *(i.iii) Where no natural person is identified under (i.i) or (i.ii) above, financial institutions should identify and take reasonable measures to verify the identity of the relevant natural person who holds the position of senior managing official.*

The immediately following interpretive notes describe the steps to be taken to identify the beneficial ownership of a trust (or similar legal arrangement such as a foundation). In this case the approach is subtly different. They start with a composite list that blends together

4 Emphasis added.
5 FATF/OECD (2013), International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation, The FATF Recommendations February 2012, FATF/OECD, Paris, available on www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF_Recommendations.pdf at pages 61-62.



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those who might benefit personally with those who are perceived to have some 'control'. They state:

> *For legal arrangements:*
> *(ii.i) Trusts – the identity of the settlor, the trustee(s), the protector (if any), the beneficiaries or class of beneficiaries, and any other natural person exercising ultimate effective control over the trust (including through a chain of control/ownership);*
> *(ii.ii) Other types of legal arrangements – the identity of persons in equivalent or similar positions.*

What is notable here is the introduction of a 'residual' concept of:

> *Any other natural person exercising ultimate effective control over the trust*

I will refer to this as the 'NPEEC' in the rest of this article.

Until recently, there has been a major problem with construing who might be regarded as an NPEEC in a trust context especially because there has been no guidance in a FATF or CRS context that sheds light on what is meant by 'control'. This has created uncertainty as to when a person has 'control' over a trust, for example, will it include someone who has power to remove a trustee, someone who can only exercise powers jointly with someone else or someone who holds only powers of veto rather than positive powers to act.

In the Anti-Money Laundering context, the 2017 MLR includes a definition of 'beneficial owner' and 'control' for the purposes of the Regulations. At Regulation 6 it states:

> *6.—(1) In these Regulations, 'beneficial owner', in relation to a trust, means each of the following—*
> *(a) the settlor;*
> *(b) the trustees;*
> *(c) the beneficiaries*
> *(d) where the individuals (or some of the individuals) benefiting from the trust have not been determined, the class of persons in whose main interest the trust is set up, or operates;*
> *(e) any individual who has control over the trust.*
> *(2) In paragraph (1)(e), 'control' means a power (whether exercisable alone, jointly with another person or with the consent of another person) under the trust instrument or by law to—*
> *(a) dispose of, advance, lend, invest, pay or apply trust property;*
> *(b) vary or terminate the trust;*
> *(c) add or remove a person as a beneficiary or to or from a class of beneficiaries;*
> *(d) appoint or remove trustees or give another individual control over the trust;*
> *(e) direct, withhold consent to or veto the exercise of a power mentioned in sub-paragraphs (a) to (d).*

A critical point to note here is that the mere existence of one of the relevant powers with respect to a trust is sufficient to be regarded as control even in circumstances where that power is not actually exercised. This is substantially different from the idea of a person who exercises effective management of a trust or a company in many tax contexts, The more conventional concept is a facts and circumstances test that requires the actual exercise of powers rather than the mere capacity to exercise them for control to be attributed to a person.

What is striking here is that in Regulation 6(2), both the holding of joint powers and that the withholding of consent or ability to veto the exercise of key powers is to be equated



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with 'control'. I will return to the specific implications for CRS Reporting in the context of trusts later – for now, it is sufficient to note the expansive definition of beneficial ownership which sits behind the various regimes.

A final point to note is that the scope of powers that can be held with respect to a trust that come within this incredibly wide concept of control extend substantially beyond the power to appoint and remove trustees.Thus powers that relate to changing the class of beneficiaries, varying or terminating the trust and powers to invest or deal with trust property are also to be equated with control.

### ii UK Trust Register

I now turn to the UK Trust Register in its own terms. The reason I wish to consider this piece of domestic UK legislation in detail is because, as far as I am aware, it represents the first instance where a major 'onshore' jurisdiction with a domestic trust law has introduced a centralised beneficial ownership register for trusts. The 2017 MLR effectively implements the UK's obligations under the EU Fourth Money Laundering Directive ((EU) 2015/849 (4AMLD)) to introduce a UK trust register. The regulations have a wide context with respect to the combating of terrorist financing and the fight against organised crime more generally. It seems likely that they will be widely copied, especially by trusts administered in the CDOTs where the UK has substantial influence.

The Regulations require the UK tax authority (HMRC) to maintain a trust register. The trust register will principally apply to trusts with UK resident trustees. However, trusts with non-UK resident trustees are also within the scope of the register if they hold UK situate assets that generate the obligation to report to UK HMRC with respect to certain taxes, including income and capital gains tax, inheritance tax and stamp duty land tax. The scope of the register requires more extensive information to be reported and maintained than that required to be disclosed under CRS.

In addition to the information which would typically be disclosed for the purposes of CRS (see paragraph 11 above) it also necessary to provide HMRC with the following information:

*a* The trustees must provide information about certain professional advisers to the trust, namely those who provide 'legal, financial or tax advice[6]' to the trust.

*b* There is a requirement to provide 'a statement of accounts for the trust, describing the trust assets and identifying the value of each category of the trust assets'. CRS, in contrast, only requires a composite value for the notional 'account value' of the trust fund of the trust without breaking this value down into categories.

*c* In considering who might be regarded as a beneficiary, Regulation 44(5)(b) states that trustees must report information 'about any other individual referred to as a potential beneficiary in a document from the settlor relating to the trust such as a letter of wishes'. This means that reference has to be made to documents other than the trust deed itself which, in the longer term, is likely to create a significant degree of confusion and uncertainty over reporting given that there is no current requirement to undertake such an exercise that I am aware of in any CRS or other equivalent tax reporting context with regard to persons who are not named as current beneficiaries.

6 See regulation [ ] of 2017 MLR.



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The UK Trust Register will (subject to the caveat noted below) only be accessible by law enforcement agencies in the UK and throughout the rest of the EU/EEA – the issue of what happens to this EU/EEA access post Brexit is presently unclear. The categories of persons with access to the UK Trust Register under 2017 MLR are arguably narrower than those described in Article 14 of 4AMLD. Article 14 states that:

> *persons who are able to demonstrate a legitimate interest with respect to money laundering, terrorist financing, and the associated predicate offences, such as corruption, tax crimes and fraud should also have access to beneficial ownership*

It is, therefore, possible that NGOs and investigative journalists with an anti-corruption profile could seek access to the UK Trust Register on the basis that the UK (as a current EU member) has failed to implement 4AMLD in full.

### iii Trustee obligations under the UK Register

A trustee of a relevant trust[7] is obliged to:

*a* maintain an up-to-date register of the 'beneficial owners' of and advisers to the trust;

*b* provide HMRC with detailed information about the beneficial owners on an annual basis and with respect to the assets of the trust and their capital value;

*c* inform relevant persons[8] of:
- its status as a trustee;
- the beneficial owners of the trust; and
- any change of beneficial owners (within 14 days of the change occurring).

*d* respond to any request for information from any law enforcement agency with respect to the trust within the reasonable period specified in the notice of request.

### iv Information about the trust under the UK Trust Register

With respect to the trust itself, it will be necessary to confirm:

*a* the name of the trust and its date of creation;

*b* a statement of accounts for the trust, describing the trust assets and identifying the value of each category of the trust assets;

*c* the place where the trust is administered;

*d* a contact address for the trustees; and

*e* the full names of any advisers who are being paid to provide legal, financial or tax advice in relation to the trust.

With respect to individuals identified as beneficiaries or NPEECs it will be necessary to provide:

*a* full name and date of birth;

*b* details of the individual's role or roles in relation to the trust; and

*c* unique tax reference number of the individual.

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7 Essentially a trust within scope of reporting.

8 Essentially financial in institutions and other professional persons with reporting regulations under AML rules.



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Where a corporate entity is involved in a trust, one is obliged to 'look through' that entity and identify the individual(s) who control it; they are subject to disclosure in their own right.

### v CRS developments

In a CRS context, I would like to consider two key areas. The first is the issue of local guidance and fragmentation, especially with respect to trust reporting. The second is the vexed issue of reporting protectors and its overlap with the NPEEC concept.

### vi Fragmentation

On fragmentation, it is notable that during 2017, many jurisdictions issued their own local guidance on certain issues. To take a few examples:

*a* Canada: as in the case of the Foreign Account Tax Compliance Act (FATCA), Canada takes the position that other than in certain instances where banks or similar entities are concerned, most trusts with professional trustees are to be regarded as passive non-financial entities (NFE) not reportable financial institutions (RFI).

*b* Singapore: Singapore has issued guidance that permits settlors who are excluded as beneficiaries to report a nil value in terms of the value of their equity interest in the notional account represented by the trust fund.

*c* Bermuda: a trust where the settlor reserves a right to direct investments is not to be regarded as an RFI even though its trustee is a financial institution.

*d* Cayman Islands: all financial institutions are required to file a nil report even though they are non-reporting FIs. This is contemplated in CRS but is likely to create a significant degree of extra reporting in large and complex trust structures.

The concern here is that there will be substantial confusion over what to report where local guidance generates positions that contradict OECD's own commentary or the position taken in other jurisdictions generally. It is also likely that a pattern of jurisdictional arbitrage will emerge.

### vii Protectors

On the issue of reporting protectors, it is well known that there is an inconsistency in the class of persons who are to be identified as the controlling persons of a trust when compared with those who to be identified as holding an equity interest in a trust. The two lists of persons are substantially similar except that the latter makes no express reference to 'protectors'. This has led to a great deal of confusion and divided opinion on when protectors are required to be reported. OECD in an FAQ issued in June 2016 takes the view that protectors must always be reported but a strict reading of the wording of the Model Treaty leads to the conclusion that they should only be disclosed as holders of an equity interest where they satisfy the test as a NPEEC.

What is interesting is that, in the context of the UK Trust Register, 2017 MLR do not make express reference to protectors either. Instead, as noted above, they refer to 'any individual who has control over the trust' and then refer to the powers over the trust that are to be equated with 'control'.

### viii NPEECs and control

I would like to consider the question of who is to be regarded as 'exercising control' and who might be regarded as an NPEEC for CRS purposes if one follows the approach adopted in 2017 MLR.



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It is interesting to note that, in commenting on the issue of control under the Controlling Persons heading in the CRS Handbook at paragraph 227, the OECD states:

> *The account held by a trust will also be reportable if it the trusts has one or more Controlling Persons that are Reportable Persons. The concept of Controlling Person used in the CRS is drawn from the 2012 FATF Recommendations on beneficial ownership. As such, the Controlling Persons of a trust are the settlor(s), trustee(s), beneficiary/ies, protector(s) and any other natural person exercising ultimate effective control over the trust.* ***This definition of Controlling Person excludes the need to inquire as to whether any of these persons can exercise practical control over the trust.***[9]

It is reasonable to conclude that OECD's intention was to follow the FATF expansive definition of beneficial ownership which is not based on a conventional legal analysis of matters such as control but, instead, to ensure that those persons reported under CRS include those with the capacity to exercise substantial influence over how a trust is run.

This approach is echoed in OECD's comments at paragraph 214 of the Handbook with respect to those to be regarded as holding an equity interest in an RFI Trust. This states:

> *The Equity Interests are held by any person treated as a settlor or beneficiary of all or a portion of the trust, or any other natural person exercising ultimate effective control over the trust.* ***The reference to any other natural person exercising ultimate effective control over the trust, at a minimum, will include the trustee as an Equity Interest Holder.***[10]

The fact OECD uses the phrase 'at a minimum' is confirmation of this expansive approach.

My view is that the definition of control from MLR 2017 could well be widely adopted in a CRS context to assist in defining NPEECs with respect to trusts. If this does indeed happen, it will mean that virtually all protectors with significant powers with respect to trusts will be reportable as NPEECs, thus rendering the debate about whether protectors of RFI trusts are reportable as such largely academic.

## II CONCLUSION

The year 2017 has witnessed some important developments in beneficial ownership reporting. The convergence of the expanded concept of who is to be regarded as a beneficial owner or exercising control in the tax reporting and AML arena looks set to be a dominant trend in the years ahead. Advisers should be very conscious of this, not only in advice on existing wealth ownership structures but also in the design of new ownership structures.

**John Riches**
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September 2017

9 Emphasis added.
10 Emphasis added.



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Chapter 12

# CANADA

*Margaret R O'Sullivan, Sara Beheshti and Emma Hamilton*[1]

## I INTRODUCTION

### i The current Canadian wealth situation

On its 150th birthday on 1 July 2017, Canada was hailed as a country that has lived up to its official motto of 'peace, order and good government'. It is looked to increasingly as an oasis of calm and financial and political stability in a world that, in particular, in the last year, has been on a rollercoaster ride of unprecedented change rocked by a number of unexpected political events – the outcome of the US 2016 presidential elections and the election of Donald Trump, Brexit, and heightened tensions and serious conflict in the hotspots of the world.

But Canadians cannot be complacent. Lurking beneath the surface is a variety of undercurrents that spell potential turbulence and trouble ahead. One is the red-hot housing market, particularly in certain urban centres such as Vancouver and Toronto, and now the prospect of a potential housing correction, which, depending on its severity, could create a tidal wave of dislocation throughout the Canadian economy.

Canada has at the same time drawn the world's attention by its move in July 2017 for the first time in seven years since the 2008 economic crisis to finally increase interest rates. The concern is that the harmful effects of an artificially induced low-interest rate environment now outweigh its benefits, and the time has come to move forward on the path to normalcy. But how increased rates will impact other aspects of the Canadian economy remain to be seen. Raising rates will increase the Canadian dollar and put a damper on exports. And that dampening effect, if not sufficiently gradual, could be the instigator of a sharp housing correction.

The government is also now more than just stretched – it is virtually tapped-out in terms of debt level, a topic that should be at the core of public debate, but that is not. And with that reality arises the prospect, and virtual certainty, of only increasing levels of taxation, but at the same time Canadians are also tapped-out and have unprecedented levels of personal debt.

The 2017 Canadian Federal Budget announced that the government intends to target private corporations and their shareholders, often high net worth individuals and professionals, who use tax planning to split income among family members or defer tax using private corporations. A package of tax proposals was released on 18 July 2017 for consultation, which contain the most significant changes to tax policy in over 40 years and have rocked

1 Margaret R O'Sullivan is principal and Sara Beheshti and Emma Hamilton are associate lawyers at O'Sullivan Estate Lawyers LLP.



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the tax planning community as well as spelling significant problems for entrepreneurs and business owners. What the final proposals will be remains to be seen, but what is clear is the government is desperate and has no choice but to try to squeeze even more tax from those who have more ability to pay. The problem it faces is that at combined highest income tax rates of more than 50 per cent, a tipping point has been reached. While south of the border, the Trump tax proposals are to reduce personal tax rates to a maximum of 35 per cent, which would result in a huge gap of almost 20 per cent compared with Canadian rates should the Trump proposals be enacted, which Canadian politicians must keep in their sights.

In the last year, the Canadian banks and investment community has been embroiled in a lot of soul-searching and debate on their retail practices and on the key issues of who is an adviser and who is not, and whether the fiduciary rule should apply to prevent conflicted advice and ensure transparency of fees in providing financial and estate planning advice, following the lead of other jurisdictions that have adopted the rule, including the UK, Australia and proposals in the US to adopt the rule slated for enactment, and now delayed by the Trump administration.

No doubt the financial and estate planning industry is on the verge of modernisation and change to meet the needs of an ageing demographic, who in particular when it comes to financial and estate planning, need the ability to rely on professional, objective advice and transparency of compensation, fees and commissions.

Which is all to say as indicated at the outset, beneath the surface of Canadian calm lie several disruptive undercurrents taking hold that have the potential to achieve progressive change and carry us forward. What the outcome will be of what seems to be an inflection point on a variety of key issues that impact the Canadian private client and wealth management world remains to be seen. Let's hope the hands at the tiller are steady ones as government and the private sector navigate some tricky waters ahead.

### ii Key factors in respect of private clients

Canada's constitutional system is a federal one, with a clear division of powers between different levels of government. Its primary legal heritage for all provinces and territories, with the exception of Quebec, is based on English common law; Quebec's is based on civil law. From the private client perspective, Canada offers the stability of a highly developed legal and court system and charter-based human rights protections. Property law, including succession, is a matter of provincial jurisdiction. Many modern and innovative concepts affecting private clients have been pioneered or progressed ahead of other jurisdictions in Canadian law, including equalisation of property between spouses on marital breakdown and death in several Canadian provinces recognising marriage as an equal economic partnership, recognition of common law spouses' and same-sex spouses' property and support rights, and same-sex marriage. Many Canadian jurisdictions have modern laws governing incapacity and substitute decision-making to take into account the need for a modern infrastructure to deal with an increasingly ageing population. Canada's multiculturalism and relatively 'open-door' immigration policy, which is required to maintain positive population growth and expand the Canadian economy and is increasingly geared to attracting more entrepreneurs and skilled workers, have together created and contributed to a dynamic, sophisticated, diverse and innovative Canadian culture.



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## II TAX

### i Personal taxation

*Federal and provincial income tax*

Canada taxes Canadian residents on their worldwide income from all sources, and non-residents on certain Canadian-source income, subject to international tax treaties. Income for Canadian tax purposes includes income from employment, business, property, 50 per cent of capital gains, and various other income sources, less certain deductions.

Canada is a federal state consisting of 10 provinces and three territories. The provinces and territories also tax income generally on the same basis as the federal government, except for Quebec, and increased federal tax applies to certain income not earned in a province. Canadian tax is levied at graduated rates of up to approximately 54 per cent in combined federal and provincial rates on taxable income, less applicable tax credits.

Canada taxes non-residents on income earned in Canada, notably income from business or employment in Canada and from certain taxable Canadian property, including Canadian real estate. A withholding tax of 25 per cent is deducted from certain income relating to non-residents, subject to international tax treaties that reduce the applicable rates.

*Capital gains regime*

Unlike most jurisdictions, Canada has no gift or inheritance tax. Instead, it levies tax on capital gains. In 2016, 50 per cent of capital gains are included in income upon actual disposition or deemed disposition. There is an exemption for capital gains on a principal residence and a lifetime exemption (C$824,176 in 2016) for capital gains on certain qualified business-use property.

The basic tax unit is the individual. Limited opportunities exist for income splitting, including by the use of trusts. Tax on capital gains may be deferred on certain transfers of property, for example, between spouses.

### ii Developments relating to personal taxation

*Provincial tax brackets for high earners*

The combined provincial and federal tax rates for high earners in 2017 range from 47.7 per cent in British Columbia to 54 per cent in Nova Scotia. The highest tax rate in 2017 in Ontario is 53.53 per cent. In 2015, Alberta introduced graduated tax rates for taxpayers. Prior to the new rates, all Albertans paid tax based on a flat provincial tax rate of 10 per cent. As of 1 October 2015, the new highest combined provincial and federal tax rate for Albertans will be 48 per cent.

*Tax proposals for planning with private corporations*

The consultation paper 'Tax Planning Using Private Corporations' and draft legislation released in July 2017 focuses on three main issues that the government says can result in 'high income individuals gaining tax advantages that are not available to most Canadians': sprinkling income using private corporations to lower tax-rate family members; holding passive investments inside a private corporation to gain the advantage of lower rates than personal rates facilitating the accumulation of earnings; and converting a private corporation's regular income into capital gains to take advantage of the lower rate on capital gains. If the government's proposals are ultimately enacted, they would profoundly change tax planning for business owners as practised over the last several decades, and restrict or eliminate many



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planning strategies, and in certain cases, result in double taxation and other anomalies. No doubt, these measures have introduced great uncertainty, but they have also raised concerns about government support for entrepreneurs and those who take risk, and how tax policy should foster it, as opposed to undermining it.

***Revised federal legislation on the taxation of trusts***

Certain estates and testamentary trusts have generally calculated federal tax using the graduated rates applicable to individuals, while trusts established during lifetime have been subject to the top federal marginal rate applicable to individuals. In 2016, graduated rates for certain estates and testamentary trusts were eliminated by the federal government. Now, the top federal marginal rate is applied to testamentary trusts and to certain estates. However, graduated rates will continue to be available to 'graduated rate estates' for 36 months and to certain testamentary trusts having disabled beneficiaries who are eligible for the Federal Disability Tax Credit. In addition, the taxation year end for testamentary trusts is now 31 December and testamentary trusts are now required to make instalment payments of income tax.

***Residence of trusts for tax purposes***

The Supreme Court of Canada in 2012 clarified the law on the tax residence of a trust in *Fundy Settlement v. Canada*,[2] also known as Garron Family Trust and St Michael's Trust Corp. The Supreme Court of Canada held that the residence of a trust is where the central management and control of the trust occurs, a significant change from the former focus on a trustee's residence. *Discovery Trust v. Canada*[3] was the first decision to apply the test that was articulated in *Fundy Settlement*. In that case, the court held that the beneficiaries' involvement in the administration of the trust did not result in the trust being resident in the province in which the beneficiaries resided as the trustee still made all decisions with respect to the administration of the trust. Instead, the court held that the trust was resident in the province in which the trustee resided.

***New principal residence rules***

In the Canadian system, capital gains are subject to taxation, and arise on the disposition of capital property. The capital gain is the difference between the property's adjusted cost base plus costs of disposal, and the proceeds of disposition. The adjusted cost is the actual cost of the property, subject to certain adjustments. Proceeds of disposition are, generally, the actual proceeds, but are subject to certain deeming provisions that will deem the proceeds to be equal to the fair market value of the property in respect of dispositions which are not at arm's length. A property is exempt from taxation on capital gains in the years that it is designated a principal residence.

Effective 3 October 2016, both individuals and trusts must report the disposition of a principal residence and make a principal residence designation in the prescribed form and manner. The period in which the CRA can reassess beyond the normal reassessment period is indefinitely extended if the disposition of a property is not reported and a penalty applies for

2 *Fundy Settlement v. Canada*, 2012 SCC 14, [2012] 1 SCR 520.

3 *Discovery Trust v. Canada*, 2015 NLTD(G)86.



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late filing. For dispositions on or after 3 October 2016, an individual who is a non-resident in the year of acquisition of a principal residence may not include the year that the property was acquired when calculating the exempt years for the principal residence exemption.

As of 2016, only certain eligible trusts may designate a property as a principal residence for any year of ownership after 2016. An eligible trust includes qualified disability trusts, an alter ego trust, spousal or common-law partner trust, joint spousal and joint common-law partner trust, and certain trusts for the exclusive benefit of the settlor during the settlor's lifetime. An eligible trust also includes 'orphan' trusts where: (1) the settlor died before the start of the year; (2) the eligible beneficiary is a minor child whose parents died before the start of the year and is a minor child of the settlor; and (3) at least one beneficiary of the trust is a resident of Canada during the year and is a specified beneficiary of the trust for the year. In order to benefit from the principal residence exemption, if a trust acquires a property on or after 3 October 2016, the terms of the trust must also provide the eligible beneficiary with a right to the use and enjoyment of the property as a residence throughout the period in the year in which the trust owns the property.

***Non-Resident Speculation Tax***

Effective 21 April 2017, the Ontario government introduced a 15 per cent tax on the value of the consideration when a residential property in the Greater Golden Horseshoe area is purchased or acquired by individuals who are not citizens or permanent residents of Canada, by a foreign corporation or by a taxable trustee, which include both foreign entities holding title in trust for beneficiaries and Canadian individuals or corporations holding title in trust for foreign entity beneficiaries. The new Non-Resident Speculation Tax (NRST) is in addition to the Ontario and Toronto land transfer taxes. Although the NRST is subject to the approval of the legislature, it is currently in effect and applies to any agreements of purchase and sale entered into after 20 April 2017. Effective 2 August 2016, British Columbia enacted a similar 15 per cent property transfer tax payable by foreign entities or taxable trustees in addition to the general property transfer tax on transfers of residential property located in the Greater Vancouver Regional District (also known as the Metro Vancouver Regional District).

***General anti-avoidance rule in respect of income tax***

There is increasing concern over the application of the general anti-avoidance rule (GAAR) in the Income Tax Act (Canada), which may apply to deny the tax benefit of provisions of the Income Tax Act (Canada) where certain conditions are met. In considering whether the GAAR applies, a court will generally consider whether there was a tax benefit, whether the transaction (or series of transactions) giving rise to the tax benefit was an 'avoidance transaction' and whether the avoidance transaction giving rise to the tax benefit was abusive.

***Whistle-blower rules, audit initiatives and compliance measures***

The CRA has launched the Offshore Tax Informant Program, under which the CRA will enter a contract to provide financial compensation to individuals who provide information that leads to the assessment or reassessment and collection of additional federal taxes in excess of C$100,000, and where the non-compliant activity involves property located outside Canada or certain other foreign elements. Banks and other financial intermediaries are required to report international electronic funds transfers of C$10,000 and over, to the CRA. Such transfers are currently reported to Canada's Financial Transactions and Reports Analysis Centre of Canada (FINTRAC). The CRA's Related Party Initiative is ongoing, under which



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individuals, including high net worth individuals (generally over C$50 million) or those with complex planning using many related entities, have been asked to provide detailed information and supporting documents about Canadian and foreign interests. Thresholds relating to value and complexity have been relaxed, and individuals not under audit are also being asked for such information. An aggressive tax planning reporting regime generally requires advisers to report to the CRA information concerning certain transactions on Form RC312 by 30 June of the following year. Reportable transactions or a reportable series of transactions will generally include an avoidance transaction or series of transactions for the purposes of GAAR if they feature two of the following: contingent fees, confidentiality protection or contractual protection. Where the form is not filed, denial of tax benefits and possible penalties may result.

### iii Cross-border structuring

***Immigration to Canada***

Canada relies heavily on immigration and offers certain tax concessions to immigrants. These same concessions along with the lack of gift and inheritance tax make Canada an attractive destination. Upon immigration to Canada, an individual receives a 'step up' in the tax cost of his or her capital property (excluding taxable Canadian property), which eliminates Canadian tax liability for capital gains accrued to that point.

***Non-resident trusts and immigration trusts***

Certain non-resident trusts established by non-resident settlors provided various conditions are met are exempt from tax and can distribute trust capital to specified beneficiaries tax-free, which provides tax planning opportunities where a non-resident trust situated in a low-tax jurisdiction has Canadian resident beneficiaries. However, the opportunities for trust planning with non-resident trusts have been significantly curtailed by the revised Section 94 of the Income Tax Act (Canada), which prevents the avoidance of Canadian taxes by certain non-resident trusts with Canadian connections where there is a Canadian resident contributor or Canadian resident beneficiary by deeming these trusts to be Canadian resident and taxable on their worldwide income. Where a trust is deemed Canadian resident, Canadian resident beneficiaries can be liable for tax along with the trust.

Previously, an immigration trust could be set up to benefit an immigrant to Canada and his or her family, and the income and capital gains in the immigration trust could accrue tax-free for up to 60 months. If the trust was settled in a foreign jurisdiction (including a low-tax offshore jurisdiction) with foreign trustees who held the foreign investment assets, there could be significant tax savings depending on comparative tax rates. However, this planning opportunity was unexpectedly eliminated as a result of the 2014 federal budget. An immigration trust, including those established prior to the legislative changes, is now subject to tax on its worldwide income, and the 60-month exemption from the deemed residence rule is eliminated.

***Emigration from Canada***

A taxpayer emigrating from Canada must pay a departure tax, which taxes gains on his or her property that accrued during his or her Canadian residency, subject to exceptions including for certain Canadian situs property and retirement plans. Payment of the departure tax may be deferred upon providing security to the CRA in like amount.



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***Tax treaties***

Canada is a party to many favourable tax treaties, which in part aim to prevent double taxation of income. Due, however, to variations in the internal taxation law of treaty nations, there can be mismatches in tax credits and timing that are not addressed in the treaties. Among other benefits, Canada's tax treaties include tiebreaker rules relating to tax residency for treaty purposes, and reduce the amount of withholding tax required from income relating to non-residents (often to 15 per cent from 25 per cent and in certain cases to zero per cent). In 2014, Canada ratified an intergovernmental agreement (IGA) relating to the US Foreign Account Tax Compliance Act (FATCA), a US law that imposes strict reporting requirements to the US taxing authority, including on financial institutions located in Canada. Canada has also agreed to implement the Organisation for Economic Co-operation and Development's Common Reporting Standard (CRS), which is based on FATCA. As of 1 July 2017, financial institutions located in Canada will be subject to the CRS and will be required to provide the CRA with certain information pertaining to accounts and account holders.

***Foreign investment entity and foreign trust rules***

Foreign trust rules designed to more effectively tax Canadian residents' passive investment, including in non-resident trusts, have been enacted, following numerous amendments to draft legislation over a protracted period. The non-resident trust rules deem a trust Canadian resident based on the presence of a Canadian-resident contributor, broadly defined, or a Canadian-resident beneficiary, and require tax to be withheld on distributions from trusts deemed Canadian resident, subject to exceptions. An election may be made to treat a portion of the trust as non-resident that will not generally be taxable in Canada. New provisions for taxing offshore investment funds have also been enacted, along with transitional provisions for those who filed under proposed foreign investment entity rules that were never enacted.

Canadian taxpayers holding specified foreign property outside Canada with a cost amount of C$100,000 or more, are required to provide more detailed information about such property on a revised Form T1135, Foreign Income Verification Statement, including names of the countries and institutions where assets are held, foreign income earned on the assets, and a maximum cost amount of the assets in the year. If Form T1135 is filed late or contains certain errors or omissions, the normal reassessment period is extended for three years, and severe penalties apply for failure to file.

### iv Regulatory issues

***Regulation of banking and related industries***

A significant portion of Canada's private wealth services are highly concentrated in the hands of six major Canadian national banks. In 2017, *Bloomberg Markets* magazine ranked four Canadian banks among the world's top 10 strongest banks with US$100 billion or more of assets. No other country dominated the list as Canada did. Banking is federally regulated by the Office of the Superintendent of Financial Institutions Canada, while the related investment industry, trust companies and insurance firms are regulated both federally and provincially. Canada's major banks are strongly capitalised, and tend to have conservative lending policies relative to other banking institutions.

In 1986, the federal government began to eliminate the four pillars of Canadian finance: Canada's traditional regulatory separation between banks, trust companies, insurance companies and investment companies. Numerous acquisitions of investment firms and trust



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companies by the six largest Canadian banks followed. In 1998, the proposed merger of two of the largest major Canadian banks was rejected by the federal government. In the past decade, Canada's major banks have expanded significantly into the United States. Canada's major banks offer an increasing array of services, including daily banking, investment services, financial planning and insurance, and wealth management, which tend to be fairly uniform among the banks.

For Canada, deregulation resulted in a flurry of mergers and acquisitions in the 1990s leading to consolidation and the three largest insurance companies controlling about two-thirds of the domestic market.

### v Issues affecting holders of active business interests

***Corporate taxation***

Canada's favourable business environment includes low corporate taxes levied at flat rates, which have been reduced aggressively between 2007 and 2012. For active businesses, combined net federal and provincial corporate tax rates range between 26 and up to 31 per cent, and a similar rate applies to income not earned in a province.

Preferential tax treatment is offered to a 'small business corporation', a defined term, which receives typical combined federal rates between 10.5 per cent and 18.5 per cent in the provinces on the first C$450,000 to C$500,000 of active business income. A small business corporation includes a Canadian-controlled private corporation carrying on active businesses in Canada (depending on the province, there may also be a requirement that the taxable capital of the corporation be less than C$15 million). Shares of a small business corporation are eligible for a lifetime capital gains exemption of C$800,000 in total indexed for inflation from 2014 (C$834,714 in 2017), as are certain qualified farm and fishing properties.

Investment income earned in a corporation is taxed at approximately the highest personal income tax rate (approximately 48 to 54 per cent in the various provinces). A gross-up and dividend tax credit mechanism is designed to avoid double taxation of dividends earned in a corporation that are subsequently paid to an individual. In 2017, dividends paid by a small business corporation (in respect of income taxed at the small business tax rate) will be grossed up by 17 per cent and the dividend tax credit will be equal to 21/29 multiplied by the amount of the dividend that was grossed up.

A tax-deferred transfer or rollover of certain eligible property to a taxable Canadian corporation for consideration, which must include shares of the corporation, is available subject to conditions. The property may retain its tax cost or receive a higher tax cost within limits. Among other results, the corporation assumes tax liability relating to gains in the property, payment of which is deferred to a later date.

***Goods and services tax or harmonised sales tax***

Canada levies a 5 per cent supply-side tax on most services and goods, including those made in Canada and imported, and certain property. The goods and services tax applies at all stages of production, subject to an input tax credit for tax paid at an earlier stage, and businesses are responsible for collecting and remitting the tax. In five provinces, the tax has been harmonised with the provincial sales tax and is known as harmonised sales tax, with combined rates between 13 and 15 per cent.



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## III SUCCESSION

### i Overview of succession in Canada

***Provincial and territorial jurisdiction***

In Canada, succession to property on death is generally a matter within the jurisdiction of the provinces and territories. Of Canada's 10 provinces and three territories, 12 are governed under common law, and one – the province of Quebec – under civil law. With respect to aboriginal Canadians who are subject to the Indian Act, succession to property on death falls within the jurisdiction of the federal government. Certain First Nations, however, have entered into self-government agreements that permit enactment of individualised laws, including those that relate to succession. These two latter scenarios are beyond the scope of this chapter.

***Conflicts of laws***

With regard to determining the applicable law, the law governing succession to moveables is generally that of the testator's domicile and the law governing succession to immoveables typically the jurisdiction where the property is located. Formal validity, which includes such matters as execution requirements for a will, is determined by conflicts of law principles (and in respect of succession to moveables is also generally that of the testator's domicile at date of death and in respect of succession to immoveables is typically the jurisdiction where the property is located), and in several provinces has been expanded by statute.

For clients with certain connections to both Canada and a participating EU Member State, it is important to consider the impact of the EU Succession Regulation (Regulation (EU) No. 650/2012), which is, in effect, for deaths post 17 August 2015, including as it relates to a client's ability to choose the law of his or her nationality to govern certain succession issues.

***Probate or equivalent court process***

The common law principle of testamentary freedom is the general rule in Canadian succession law, as modified by contract or legislation. After the testator's death, a will is typically submitted to probate or equivalent court process, whereby it is validated and the executors' appointment as legal representatives confirmed. In this process, the will and supporting documents, which may include a detailed asset listing, become public. Probate fees are typically levied in the form of a flat fee, or tax based on a percentage of estate assets (e.g., approximately 1.5 per cent in Ontario). In some provinces, in particular those with a high rate structure to probate a will, the option of creating a second, non-probate will that governs private company shares and other assets that do not require a court grant of probate to administer is often used to minimise probate fees and tax. A Quebec notarial will need not be submitted to probate in that province.

Once probate has been granted, the resulting certificate, grant or other like document is used by the personal representative to deal with third-party institutions and entities in the process of transferring title to the personal representative and gathering in the assets.

***Legislative provisions for succession on intestacy***

In an event of intestacy, each province and territory provides for a scheme of property division: typically between the testator's surviving spouse and children – if any – failing which to other relatives as specified. Some provinces allocate the spouse a preferential share prior to



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dividing the estate between spouse and children. In this context, spouses are married spouses, including same-sex married spouses and, in some provinces and two territories, *de facto* spouses, providing certain conditions are met. A court process for letters of administration or equivalent provides for the appointment of estate trustees on intestacy.

As of 1 January 2017, under Part III of the Succession Law Reform Act[4] in Ontario, Section 47(1) was amended to state that for the purposes of determining the beneficiaries on intestacy, the deceased's descendants and relatives conceived and born alive after the deceased's date of death shall inherit as if they were born during the deceased's lifetime and survived, provided specific statutory conditions are met.[5]

### *Legislative provisions for dependants' support*

In all provinces, a dependant can claim support from the deceased's estate, provided he or she stands in a certain relationship with the deceased (typically including a spouse, *de facto* spouse or minor child) and the deceased was providing him or her with support or had a support obligation at the time of death. The quantum of support is determined circumstantially and with judicial discretion, usually taking into account needs and means,[6] and in some cases, the dependant's accustomed standard of living.[7] Some provinces recognise a moral entitlement to share in a deceased's estate and will vary the distribution in a will or award support on this basis.[8] Recent decisions have also shown that support may be awarded to a dependant in spite of an existing domestic contract if its terms have become unfair with the passage of time.[9]

Within Canada, it appears that cases involving entitlement to support in modern 'non-traditional' relationships (usually involving *de facto* spouses) are on the rise, including recent decisions in Alberta[10] and British Columbia.[11]

### *Legislative provisions for matrimonial property rights on death*

Property law in Canada falls under the jurisdiction of the provinces and territories; thus the availability and scheme of statutory property division claims by surviving spouses upon death of a spouse vary throughout Canada. The matrimonial property regimes of most provinces and territories provide a surviving spouse with property rights on a first spouse's death. For example, in Ontario, a surviving spouse has a right to elect to claim against the deceased spouse's estate to notionally equalise the property acquired during marriage as between the two of them. If such an equalisation claim is made, he or she thereby loses entitlements, if any, under the deceased spouse's will and to certain other benefits. In New Brunswick, Newfoundland and Labrador, Ontario and Quebec, claims for division of property on death of a spouse are available to legally married spouses only as well as, in the case of Quebec, the survivor of a couple who have entered into a civil union. Currently, in British Columbia, Alberta, Prince Edward Island and the Yukon, death does not trigger a statutory property

4 RSO 1990, c S26.
5 Ibid, see s 1.1(1).
6 See, for example, *Bath v. Bath Estate*, 2016 BCSC 1239.
7 See, for example, *McKenna Estate (Re)*, 2015 ABQB 37; *Morassut v. Jaczynski*, 2015 ONSC 502.
8 See, for example *Tippett v. Tippett Estate*, 2015 BCSC 291; *Philp v. Philp Estate*, 2017 BCSC 625.
9 See, for example, *McKenna Estate (Re)*, 2015 ABQB 37.
10 *Riley Estate (Re)*, 2014 ABQB 725; *Umbach v. Lang Estate*, 2016 ABQB 16, 2016.
11 *Coombes Estate (Re)*, 2015 BCSC 2050; *Re Richardson Estate*, 2014 BCSC 2162; *Kish v. Sobchak Estate*, 2016 BCCA 65.



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claim for the surviving spouse. All other provinces and territories provide a statutory claim to division of property on death and extend its availability to surviving *de facto* spouses provided the specific requirements of the governing legislation have been met.

### ii Key legislative or case law changes affecting succession

***Increased Ontario compliance to probate a will***

In Ontario in 2011, legislative measures were enacted under the Estate Administration Tax Act permitting the Minister of Finance to assess estates for payment of additional Estate Administration Tax. No practical means or process for determining which estates to assess was put in place until 1 January 2015 when with little forewarning, a new regulation under the Act came into effect. The changes usher in a new reporting regime that is triggered by applying for and receiving a certificate of appointment of estate trustee. Estate representatives must now, in addition to the paperwork relating to the certificate, provide an estate information return to the Ministry of Finance within 90 calendar days of the court issuing the certificate of appointment. Most significantly, the return (an approved form of which is available from the Ministry) requires detailed information about each estate asset and its fair market date of death value. The estate representative must be able to corroborate the reported asset values. Penalties include fines and even imprisonment for failing to file a return or where the information filed was false or misleading. Amending returns must be filed within 30 days of discovering a prior return was incorrect or incomplete, except where the value previously provided for an estate asset has been determined to be incorrect and more than four years have passed since the issuance of the certificate of appointment. The Ministry has broad audit powers in conducting its review of the returns, including assessment of further tax if the estate date of death value is determined to be higher than originally reported.

***Gifts in wills altered for public policy reasons***

Recent Canadian lower court decisions (one decision from New Brunswick and another from an Ontario court) had limited testamentary freedom by altering gifts in wills for public policy reasons. The New Brunswick decision of *McCorkill v. Streed* [12] had the effect of striking an unconditional bequest to a racist corporation on the basis of public policy. This decision was upheld on appeal and an application for leave to appeal to the Supreme Court of Canada was dismissed.[13] In the Ontario decision of *Spence v. BMO Trust Co*,[14] a court struck the entire will of a testator who was survived by two adult daughters (neither of whom qualified as dependants) where one daughter was entirely left out of the distribution of the estate. The will stated the testator had excluded the daughter because she had not communicated with him for years. Based on affidavit evidence, however, the court concluded that the real reason for the daughter's exclusion was that she had had a child with a man of a different race. Again the doctrine of public policy was employed and the entire will was struck down with the result that both daughters shared in the estate equally on intestacy. The Ontario Court of

12 *McCorkill v. Streed*, 2014 NBQB 148.

13 *Canadian Association for Free Expression v. Streed et al*, (2015), 9 ETR ( 4th) 203 (NBCA); CanLII 34017 (SCC).

14 *Spence v. BMO Trust C*o, 2015 ONSC 615.



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Appeal reversed the decision, thereby confirming in this instance that testators do not have any obligation to benefit persons who they have no legal obligation to support or otherwise benefit (e.g., non-dependent adult children).[15]

***Mutual wills***

In a recent Ontario lower court decision, two spouses executed wills simultaneously leaving everything to the survivor of them, followed by an identical gift over to their four children (each spouse having two children from a prior marriage). After the husband's death, the wife made a new will and gifted her estate to her two adult children and she subsequently died. On an application commenced by the husband's two adult children, the court found that while there was not a direct written or oral agreement that the spouses' original wills were mutual wills, as a result of the extrinsic evidence presented – including with respect to the family context – an oral contract had existed between the spouses and by virtue of it, neither spouse was entitled to vary his or her will without the consent of the other spouse. The court held that the estate of the surviving spouse was to be divided among all four children.[16] In a similar case, the testator and his wife executed wills without receiving legal advice. The testator left his entire estate to his wife and if she predeceased him, the estate went to his two stepchildren. The wife died and two days later, the testator executed a will leaving his entire estate to his biological children. The testator's stepchildren brought an application regarding validity of the second will, questioning the capacity of the testator. However, the Court found no evidence or agreement to support the argument that mutual wills existed between the couple. The second will was valid.[17]

### iii Cross-border developments

***Changes to US transfer tax***

Canada is home to many dual citizens, including US-Canadian citizens and many Canadians own holiday property in the United States or other US real or personal property, or spend significant time in the United States. A number of Canadians are, as a result, subject to the US transfer tax regime and attentive to any changes in it. Following the American Taxpayer Relief Act of 2012, which became law on 2 January 2013, the US exemption from estate tax remains US$5 million indexed for inflation from 2011 (US$5.49 million for 2017) and the maximum rate of US estate tax increased from 35 per cent to 40 per cent, both permanently subject to future legislation. Where applicable, the US estate and gift tax exemption remains unified. The Trump administration has proposed to eliminate US estate tax, but there is great uncertainty with regard to these proposals at the time of writing.

***Income tax-related reporting requirements***

FATCA, introduced to combat offshore tax evasion, will affect Canadians with US connections and Canadian financial institutions. Final regulations under FATCA set out detailed reporting and withholding requirements for non-US financial institutions with respect to accounts with certain US connections, including those beneficially owned by US citizens.

15 *Spence Estate (Re)* 2016 ONCA 196, application to the Supreme Court of Canada for leave to appeal dismissed 2016 CanLII 34005.

16 *Rammage v. Estate of Roussel*, 2016 ONSC 1857.

17 *Lavoie v. Trudel*, 2016 ONSC 4141.



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The requirements under FATCA will be phased in generally, ending in 2017. Information to be reported includes identifying information, information about the values of the accounts, and transaction amounts. Other non-US entities (and it is expected certain Canadian trusts) will also be required to report the ownership or beneficial interests of US citizens.

Under FATCA, such information is generally required to be provided directly to the US Internal Revenue Service (IRS) by non-US financial institutions and entities. Canada has ratified a Model 1 type IGA with the United States and passed legislation that aims to implement the IGA. Designed to ease compliance with FATCA, the IGA modifies FATCA's provisions in respect of Canadian financial institutions and other Canadian entities, and expands the tax information exchange provisions between Canada and the United States. Pursuant to the IGA, Canadian financial institutions will generally report information to the Canada Revenue Agency rather than directly to the IRS, although they are generally required to register with the IRS to obtain an identification number. It is intended that by complying with the IGA, Canadian financial institutions will avoid a 30 per cent withholding requirement under FATCA on certain payments to them. Also, certain Canadian-registered plans are exempt from reporting under the IGA, and local financial institutions may be entitled to additional relief.

A self-reporting scheme applies to US persons (including US citizens, green card holders and certain persons who spend a substantial amount of time in the United States) in Canada and elsewhere that may require reporting of non-US bank and financial accounts on a Report of Foreign Bank and Financial Accounts. Under FATCA, US persons must generally also report certain non-US financial assets exceeding threshold values on a Statement of Specified Foreign Financial Assets (Form 8938), filed with their tax returns.

In June 2015, Canada signed the Multilateral Competent Authority Agreement (MCAA), which provides for a coordinated arrangement for the automatic exchange of financial account information among various countries. As of June 2017, over 93 countries have signed the MCAA, with Bahrain being the most recent.

Under the MCAA, Canada agreed to implement the Organisation for Economic Co-operation and Development's CRS. As of 1 July 2017, financial institutions located in Canada will be subject to the CRS and will be required to provide the CRA with certain information pertaining to accounts and account holders. The first information exchanges are set to take place in 2018. The CRS is based on FATCA and is similar in effect.

***United States income tax penalties for Canadian residents***

The Canadian government has expressed its concern to the US authorities and certain concessions have been granted to Canadian residents who are dual citizens of Canada and the United States. The US Internal Revenue Service has provided measures to assist such persons to fulfil their filing and reporting obligations. In June 2014, the IRS announced streamlined filing compliance procedures for certain US taxpayers who non-wilfully failed to disclose offshore assets, eliminating former requirements that taxpayers owe US$1,500 or less per taxation year and a former risk questionnaire, and requiring a certification regarding the taxpayer's non-wilful conduct. Certain penalties or enforcement actions may be avoided, and taxpayers may claim retroactive deferral of income earned in Canadian retirement plans. The IRS also announced its intention in June 2014 to modify the 2012 offshore voluntary disclosure programme.



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### *Uniform Substitute Decision-Making legislation*

The Uniform Law Conference of Canada (ULCC) adopted the Uniform Interjurisdictional Recognition of Substitute Decision-Making Documents Act (Uniform Act) in August 2016. The Uniform Act is a joint project of the ULCC and the Uniform Law Commission of the United States (ULC), which was undertaken to promote cross-border portability and utility of substitute decision-making documents for property and personal care. The ULC adopted its version of the Uniform Act in July 2014 and US states may now consider enacting it internally. To date, Idaho and Connecticut have enacted it and it has been introduced in Alaska and Colorado. It is up to each Canadian province and territory to consider adopting and implementing the Uniform Act. This new uniform legislation in each jurisdiction marks a significant step forward in promoting cross-border effectiveness of powers of attorney.

Under the ULCC Uniform Act, which differs from the ULC one, a 'substitute decision-making document' will be formally valid if it complies with any of the following: (1) the law indicated in the document, or if none; (2) the law of the jurisdiction in which it was executed; (3) the jurisdiction in which the individual was habitually resident; or (4) the law of the place it is to be used. In the Canadian Uniform Act, the application of the governing law can only be refused if its application would be manifestly contrary to the public policy of the enacting province or territory, which the notes to the Uniform Act indicate in matters relating to personal care, including specific medical procedures. The Uniform Acts provide for the ability of a third party to rely on a document as well as, subject to certain exceptions, the obligation of third parties within a reasonable time to accept a substitute decision-making document and not require an additional or different form of authority. It also provides for a court order mandating acceptance and liability for legal costs for refusal to accept a substitute decision-making document in violation of each Uniform Act.

## iv Applicable changes affecting personal property

### *Same-sex marriage and Quebec civil unions*

In 2005, Canada legalised same-sex marriage and, as a result, a broad array of statutory and common law rights have been available to same-sex married spouses for over a decade, including rights to share in an estate upon intestacy and any rights to property division under provincial family law statutes. Quebec also solemnises a civil union for same-sex or opposite-sex couples, which confers similar rights to marriage.

### *Rights of de facto spouses*

For unmarried *de facto* spouses Canada recognises a limited subset of legal rights. *De facto* spouses are treated similarly to married spouses for various purposes, including taxation and certain government benefits, but significant gaps remain in respect of property rights on relationship breakdown and death, although this varies by province and territory.

### *Spousal support provisions for de facto spouses in Quebec*

In early 2013, the Supreme Court of Canada delivered its decision in *Quebec (Attorney General) v. A*,[18] also known as *Lola v. Eric.* Lola (not her real name) claimed spousal support and property rights from her billionaire *de facto* spouse Eric. The province of Quebec has a greater percentage of *de facto* spouses than any other province (approximately 32 per cent in

18 *Ford v. Quebec (Attorney General)* [1988] 2 SCR 712.



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2011, with the national average being 16.7 per cent) and there are few legal rights provided to these spouses on relationship breakdown.[19] While a majority of the Supreme Court agreed with the Quebec Court of Appeal in finding that Article 585 of the Quebec Civil Code, which does not provide spousal support for *de facto* spouses although it provides for support among married or civil union spouses, discriminates against *de facto* spouses on equality grounds, the discrimination is justified on the principle of respecting individual couples' choice and autonomy.

***Common law property division for de facto spouses***

In *Kerr v. Baranow and Vanasse v. Seguin*,[20] the Supreme Court reviewed the principles of unjust enrichment and resulting trust applicable to *de facto* spouses on relationship breakdown. After a relationship of over 25 years, Ms Kerr claimed property and support entitlements. Both parties had worked and Mr Baranow had cared for Ms Kerr after she had suffered a stroke. The court reviewed the law of unjust enrichment applicable to *de facto* spouses not included in most provincial statutory property division schemes. The elements of the claim are enrichment of one spouse, the corresponding deprivation of another and absence of juristic reason (such as a contract), and remedies have included a constructive trust and monetary amounts, including amounts relating to value received. Where appropriate, the claimant should be treated as a co-venturer in a joint family venture and should share the couple's mutual gains. Indicia of a joint family venture include mutual effort, economic integration, intention and priority to the family, and there must also be a link between the contribution and wealth accumulated. A new trial was ordered in *Kerr* regarding unjust enrichment. A monetary remedy is not limited to a value-received approach, and in *Vanasse*, the Supreme Court upheld a monetary award granted at trial to a partner who had cared for a young family and given up career opportunities during a 12-year relationship.

***Discretionary trust interests as matrimonial property***

British Columbia's Family Law Act is the first Canadian family law statute to expressly address discretionary trust interests in the division of family property by categorising certain beneficial interests in property held in discretionary trusts as excluded property. Problems with the original wording of the Act have been rectified by amendments that came into force on 26 May 2014, thereby clarifying that only the increase in value of the spouse's beneficial interest in a discretionary trust will be subject to division on separation (rather than the increase in value of all of the property in the trust, as originally drafted). Valuation of these interests on separation will continue to remain a live and litigious issue in this province and throughout Canada, as evidenced by recent reported decisions in Saskatchewan,[21] Alberta[22] and Ontario[23] with relatively little valuation analyses having been reported to date.

19 *Statistics Canada*, 'Portrait of Families and Living Arrangements in Canada: Families, households and marital status, 2011 Census of Population', September 2012, p. 6.

20 [2011] SCJ No. 10.

21 *Grosse v. Grosse*, 2015 SKCA 68.

22 *Shopik v. Shopik*, 2014 ABQB 41 (CanLII).

23 *Mudronja v. Mudronja,* 2014 ONSC 6217; *Tremblay v. Tremblay*, 2016 ONSC 588.



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### ***Legal presumptions relating to jointly held personal property clarified and effect of transfer examined***

In two companion cases, *Pecore v. Pecore*[24] and *Madsen Estate v. Saylor*,[25] the Supreme Court of Canada clarified the common-law presumptions of resulting trust and advancement, which are legal presumptions subject to being rebutted on the civil standard of proof. The Court clarified that a recipient of gratuitously transferred personal property is generally presumed to hold it on resulting trust for the donor. The presumption that the property so transferred is advanced to the donee that has historically applied to certain family relationships, now applies only to transfers between a parent and minor child (not from husband to wife or from parent to adult child). The Court also canvassed issues of evidence. In *Pecore*, the Court found that a father who had placed financial accounts into joint names with his daughter had an actual intention to gift these, whereas in *Madsen* the opposite result prevailed. In *Bradford v. Lyell*,[26] a Saskatchewan court held that if an *inter vivos* transfer of a condo property into joint ownership by a grandmother to her granddaughter was found to be intended as a gift of the right of survivorship at the time of the transfer, both the legal and equitable title vested when the joint title was created such that the gift was complete at that time and the grandmother could not later change her mind in her will, thereby entitling the granddaughter to the beneficial ownership of the property upon the grandmother's death.

Joint ownership continues to be a legal minefield in the context of estates and estate planning. Two subsequent Ontario Court of Appeal decisions have added further outcomes to gratuitous transfers of property into joint ownership. In *Sawdon Estate v. Sawdon*, the court found that evidence of intention regarding the transfer may not only show that the presumption of resulting trust has been rebutted, but also that a transfer of personal property into joint names created a trust of the beneficial right of survivorship for certain beneficiaries in addition to the surviving joint owners (two of the deceased's children) such that the property passed outside the deceased's estate and was divided equally among all five of the deceased's children.[27] In *Mroz (Litigation guardian of) v. Mroz*,[28] the Ontario Court of Appeal reviewed a mother's transfer of her home into joint ownership with her daughter where the mother's will directed that the proceeds of sale from the home be used to fund two legacies to her grandchildren. In this instance and based on the findings of the trial judge regarding the mother's intentions at the time of the transfer, the Court held that the daughter had not rebutted the presumption of resulting trust, held the property as trustee and the property was to be dealt with in accordance with her mother's will. *Mroz* was distinguished from *Sawdon* given that the trust obligation in *Sawdon* arose at the time of the transfer (it was *inter vivos*) and in *Mroz* the trust obligation was not to arise until after the mother's death. In other words, it would appear from these two decisions that trust obligations must take effect prior to a joint owner's death for the result in *Sawdon* to occur.

Even more recently in Ontario, the Court of Appeal in *Andrade v. Andrade,*[29] found that the presumption of resulting trust applied where a mother purchased a property using funds provided to her by her children who lived in the home with her, which were applied to

24 *Pecore v. Pecore*, 2007 SCC 17, [2007] 1 SCR 795.

25 *Saylor v. Madsen Estate*, 2007 SCC 18, [2007] 1 SCR 838.

26 *Bradford v. Lyell*, 2013 SKQB 330 (CanLII).

27 *Sawdon Estate*, 2014 ONCA 101 (CanLII).

28 2015 ONCA 171.

29 *Andrade v. Andrade*, 2016 ONCA 368.



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the down payment, mortgage and expenses, but the property was held in the names of two of her seven adult children at any given time. The court indicated that the trial judge had erred in finding that the mother had not contributed any of her own funds to the home, and that once her children had provided funds to their mother, the funds became hers. The court also noted that while the tax treatment of the asset post-transfer is one factor to be considered in determining intention at the time of a transfer of a property (in this case, units in the home had been rented out to third parties over the years and the title-holders had reported the rental income on their returns, while their mother had actually received the rent), but it is not determinative of the transferor's intention. Adding a further dimension to the presumption of resulting trust, a 2015 Alberta Queen's Bench decision considered, among other matters, whether the presumption applies when a person designates a beneficiary of a retirement plan (or other financial products capable of being designated).[30] The judge ultimately avoided deciding the issue by finding evidence of the deceased's intention on a balance of probabilities to gift the retirement plans proceeds to his son as the named beneficiary, leaving the question open for future judicial determination.

In Quebec, there is no equivalence to joint tenancy or rights of survivorship. In *Gauthier v. Gauthier*,[31] the deceased and his son signed an account opening agreement in Florida that held the deceased's inheritance. The will named the deceased's three children as beneficiaries, but the son submitted that the account agreement left the inheritance to him, or in the alternative, his father intended to gift the account. The Court did not apply *Pecore*, but rather looked to the deceased's intentions. The Court held that the deceased did not intend to gift the account.

Most recently, in the British Columbia Court of Appeal decision in *McKendry v. McKendry*,[32] the deceased transferred property into joint tenancy with her son and executed a trust declaration to support her intention that the property was to be held in trust. The deceased later decided to gift the property to her son. The deceased executed a two-page document drafted by her lawyer and revised her will to include a clause outlining that the property was to be a gift. The trial court held that the property was held in trust for the deceased by the son and an executed deed would have perfected the gift, but the Court of Appeal found the deceased's intentions to be 'manifest and unambiguous' in providing an *inter vivos* gift to her son. The presumption of resulting trust was not considered in this case. This decision highlights the importance of providing clear evidence of intention, whether that is through a third party or supporting documentation.

### *Legal presumption of advancement as between spouses in BC*

In *F(VJ) v. W(SK)*,[33] the British Columbia Court of Appeal recently confirmed the common law presumption of advancement between spouses was not abolished by the enactment of that province's new Family Law Act[34] in 2011, and noted that a BC statute contained no express provision altering the impact of or abolishing the presumption as was the case in the family law statutes of other Canadian jurisdictions such as Alberta, Saskatchewan and Ontario.

30 *Morrison Estate (Re)*, 2015 ABQB 769.

31 2016 QCCS 2333.

32 2017 BCCA 48; similar decision by the Ontario Court of Appeal in *Laski v. Laski*, 2016 ONCA 337.

33 2016 BCCA 186 (currently under appeal).

34 SBC 2011, c.25.



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***Exempting certain matrimonial property from the equalisation regime***

The 2012 Ontario Court of Appeal decision in *Spencer v. Riesberry*[35] held that in the circumstances, a matrimonial property held by a family trust where one of the beneficiaries resided did not qualify as a matrimonial home for the purposes of Ontario's Family Law Act and excluded it from the equalisation calculation as the beneficiary in question did not have an 'interest' in the property within the meaning of the Act (although the value of the interest in the trust was still included for the purposes of the calculation). This case represents a frustration of the matrimonial home protection contained in the Act, as well as a potential circumvention of the usual requirements for the spouse's consent on the sale or encumbrance of a matrimonial home and the right of possession for the non-titled spouse.

***Proprietary estoppel***

The equitable claim of proprietary estoppel has been successfully used in two recent Ontario cases as the basis for a cause of action in respect of an unfulfilled or reneged promise or assurance relating to a cottage property.[36] In both *Clarke v. Johnson* and *Love v. Schumacher*, the equity resulted in the appropriate remedy being, based on the facts and the exercise of judicial discretion, a proprietary one in the form of an exclusive, irrevocable and time-specific licence (as a monetary award was found in both instances to be inappropriate or insufficient). In both decisions, the courts followed the modern UK test to establish proprietary estoppel, being the establishment of three criteria:

*a* encouragement or acquiescence in respect of land;
*b* detrimental reliance; and
*c* unconscionability.

A third case arising in BC, resulting in a successful proprietary estoppel claim involving a horse farm that saw the trial judge award the entire horse farm to the applicant, has been remitted back to the trial judge to assess the outstanding claims of unjust enrichment and express or implied trust, as well as the proportionality of the trial judge's remedy to the proprietary estoppel claim.[37] An application for leave to appeal this decision was recently dismissed by the Supreme Court of Canada.[38] *Cowper-Smith v. Morgan*[39] is a recent BC Appellate Court decision in which the proprietary estoppel claim was unsuccessful as the person against whom the claim was advanced did not own the property in question at the time the assurance or representation was made.

## IV WEALTH STRUCTURING & REGULATION

### i Common vehicles for wealth structuring

Trusts and holding companies are perhaps two of the most common vehicles used in wealth structuring.

35 *Spencer v. Riesberry*, 2012 ONCA 418.
36 *Clarke v. Johnson*, 2014 ONCA 237 and *Love v. Schumacher Estate*, 2014 ONSC 4080.
37 *Sabey v. Rommel*, 2014 BCCA 360.
38 *Jesse Sabey v. Warren Scott Beardsley as executor of the will of Kim Louise von Hopffgarten, deceased, et al.* 2015 CanLII 16734.
39 2016 BCCA 200 (currently under appeal).



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***Trusts***

*Income splitting*

Trusts can be established *inter vivos* or by will. *Inter vivos* trusts are often used to split income between family members who have lower tax rates, where the trust earns income and acts as a conduit to allocate income, including taxable capital gains, among lower rate taxpayers. Effective planning involves careful attention to the possible application of the attribution rules, which can attribute income back to a high tax rate taxpayer.

*Trusts used in conjunction with an 'estate freeze'*

Trusts are also commonly used in conjunction with an estate freeze to hold growth property, such as common shares of a private holding company, which reflect the future growth of appreciating assets to defer taxation of capital gains to the next generation, as opposed to on death of a founder, thereby achieving significant tax savings. Use of a trust can allow for control of the timing of distribution of property and selection of beneficiaries, and for general wealth protection purposes, and a fully discretionary trust is often used for such purpose.

*Trusts as will substitutes*

Trusts are also increasingly used as will substitutes, in particular 'alter ego' and 'joint partner' trusts that are specifically defined under Canadian income tax legislation and allow persons aged 65 and over, provided certain conditions are met, to roll over capital property on a tax-deferred basis, as opposed to triggering capital gains. The alter ego and joint partner trusts are often used to provide for primary succession to property on death as a substitute to a will. They offer several perceived benefits, including: (1) avoiding expensive court fees and tax paid to probate a will, as well as the attendant court process, which can be protracted; (2) more privacy than a will; (3) ensuring capital succession to property on death; and (4) protection against estate litigation, including will challenges and other claims arising on death. They are also an effective and sophisticated vehicle to manage assets on incapacity in contrast to a power of attorney.

*Use of testamentary trusts for income splitting and other benefits*

Testamentary trusts, that is those created by will, have been used to provide for income splitting on death. Generally, certain estates and testamentary trusts calculate federal tax using the graduated rates applicable to individuals, whereas trusts established during lifetime are subject to the top federal tax rate applicable to individuals. Prior to 2016, testamentary trusts allowed for income splitting between the trust and one or more beneficiaries, which resulted in significant tax savings. However, commencing in 2016, testamentary trusts are now subject to the top federal tax rate applicable to individuals and, consequently, the above tax benefit has been eliminated, but it will still be possible to 'sprinkle' income among a group of beneficiaries of a discretionary testamentary trust if the trust terms permit. Also, use of a testamentary trust provides for probate fee minimisation, capital succession planning and can safeguard against beneficiaries' matrimonial and possible creditor claims, among other benefits.

*Multiple wills used to minimise probate fees*

Multiple wills are increasingly used in certain provinces to minimise estate administration tax and probate fees. For example, in Ontario, estate administration tax is approximately 1.5 per



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cent of the value of estate assets. Assets are often segregated under two wills: a primary will and a secondary will. Assets that generally do not require a probated will to administer by way of proof of executors' authority to third parties, such as financial institutions and others, are segregated under a secondary will, including private company shares, family loans, tangible personal property and beneficial trust interests. Only the primary will is typically probated, and applicable tax or court fees are then based on a more modest asset base.

*Holding companies*

Holding companies are a common feature of Canadian estate planning. They are commonly used to hold US securities and certain other US situs assets to protect against exposure to US estate tax, to defer tax on active business income where shares of an active business are held by the holding company, to split income, including in conjunction with use of a family trust, and for asset protection and retirement planning.

*Potential tax advantages of holding companies*

The utility of an investment holding company to earn investment income at a lower tax rate than if earned personally will depend on changing tax rates, which historically have at certain times offered tax advantages and at other times are neutral and less advantageous.

Holding companies are also used in conjunction with probate fee and estate tax minimisation strategies as outlined above. Private company shares can pass under a secondary will, which typically may not need to be probated, thereby saving fees and tax, which can be significant where the shares have a high value. There is potential for double taxation on death where assets are held in a holding company, since a deceased person will be subject to personal taxation on the deemed disposition of the shares of the holding company giving rise to possible taxable capital gains, and also the same gains may be reflected in the holding company's underlying assets, on which tax will be paid at the corporate level on sale of the assets or wind-up of the company. It is therefore necessary to implement proper post-mortem tax planning to avoid potential double taxation on death.

## ii Anti-money laundering regime

The federal Proceeds of Crime (Money Laundering) and Terrorist Financing Act came into effect in 2001. It introduced requirements for a compliance regime, record-keeping, client identification and reporting. Reporting entities must implement a compliance regime, keep certain records, obtain certain client identification and report suspicious transactions to an independent agency, the FINTRAC. Certain other financial transactions, as well as terrorist property must also be reported. Reporting entities include financial institutions, such as banks, trust companies, loan companies, life insurance companies, brokers and agents, securities dealers, accountants and accounting firms carrying out certain transactions, real estate brokers, and certain others. The legislation imposes harsh financial and criminal penalties, including imprisonment for failure to report. Reporting entities have to send large-cash-transaction reports to FINTRAC when they receive an amount of C$10,000 or more in cash in the course of a single transaction and financial entities, money service businesses and casinos have to report incoming and outgoing international electronic funds transfers of C$10,000 or more in a single transaction.



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## V CONCLUSIONS & OUTLOOK

The ominous pronouncements in the 2017 Canadian federal Budget left a sense of apprehension with regard to what the government's plans were with respect to tax planning for private corporations and their shareholders. Certainly, with its statements, the government set the groundwork for the controversial changes contained in the tax proposals released in July 2017, which will undoubtedly have the effect of further curtailing tax opportunities for entrepreneurs, business owners, and professionals, and create an unfriendly tax environments for the many small business owners that drive much of the economy.

The prospect of increasing taxation in future to meet exploding government debt is certainly not a cheery one. At the same time, the relative stability of the Canadian wealth scene, our sound banking system, and the attractiveness of Canada as a safe haven continues, which perhaps underscores that there is a real price tag for social cohesion and the high quality of life that most Canadians are privileged to enjoy, relative to most other countries.

On its 150th birthday, Canadians had the opportunity to reflect on their good fortune, on all that has been achieved when it comes to the most important issues, to take a balanced perspective, and with pride and a sense of great satisfaction, celebrate the results.



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Appendix 1

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Margaret O'Sullivan exclusively practises estate planning; estate litigation; advising executors, trustees and beneficiaries; and administration of trusts and estates. Prior to establishing an independent trusts and estates boutique firm, she was a partner at Stikeman Elliott, where she directed its trusts and estates practice. She is a past deputy chair and member of the board of directors and council for the Society of Trust and Estate Practitioners (STEP) Worldwide; past chair of the professional standards committee of STEP Worldwide; past member of the management and finance committee; past deputy chair of STEP (Canada); past chair of the editorial board for STEP Inside; past chair of the Trusts and Estates Law section, Ontario Bar Association; elected fellow, ACTEC, 1995; and academician of The International Academy of Estate and Trust Law. She received the 2014 STEP Founder's Award for Outstanding Achievement and the Ontario Bar Association's 2013 Award of Excellence in Trusts and Estates Law. She has written two textbooks for the Trust Institute of the Institute of Canadian Bankers: *Engineering of a Trust* and *Trust and Estate Management*. She is also author of the Canada chapter of *International Succession Laws* (Tottel 2009) and contributing author to Widdifield on *Executors and Trustees* (Carswell 2002), *Key Developments in Estates and Trusts Law in Ontario* (Canada Law Book 2008) and to *The International Comparative Legal Guide to: Private Client 2016* (Global Legal Group 2015). She was called to the Ontario Bar in 1983.

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Sara's practice involves estate planning, estate administration, estate dispute resolution and real estate matters arising in the trust and estate context. Sara's estate planning practice includes will and trust planning, incapacity planning and estate administration. Sara also advises executors, beneficiaries and trustees on estate and trust administration. Sara is frequently retained by lawyers, financial institutions, executors and individuals to act on real estate issues arising in estate planning, estate administration and estate litigation matters. Sara also has broad experience in real estate transactions and estate conveyancing matters. She also provides title opinions and advice on claims affecting title, fraud prevention and the registration of title transfers, cautions, court orders and certificates of pending litigation.



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