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DISTRIBUTION DELAYED
REASONS TO WAIT

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DISTRIBUTION DELAYED: REASONS TO WAIT

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The time-worn friction between beneficiaries wanting their inheritance without delay and executors who want protection before distributing is likely here to stay. In fact, as the intergenerational wealth transfer gathers steam, this intrinsic conflict will more likely increase in stridency and frequency. Estates are becoming larger, investments more varied as to location and type, and estate planning more complex.

All of this means more potential issues to be dealt with by executors. More issues leads to more work and greater risks for executors, who need more time and protection in the result. Protection can take many forms, but the most reliable is also the simplest: do not distribute all of the assets of the estate until you can safely do so without issues popping up after you have divested yourself of the very resources required to deal with the issues. Explanations to the beneficiaries of the reasons they must wait may help reduce complaints. If not, then in spite of all best intentions, executors may face legal proceedings brought by beneficiaries as a result of alleged delay, which delay has paradoxically been incurred to ensure the executor is protected from the consequences of other potential legal proceedings.

The list of emerging or potential risks seems to lengthen year by year. Some of these risks lurk on the fringes or outside the scope of the usual estate administration practice, ready, willing and very able of causing no end of trouble for executors and their solicitors. To compound the dilemma, some risks can be reduced or eliminated

altogether by a quick distribution of the estate's assets, creating a Catch-22 situation where the prudent course of action can only be guessed.

Three growing areas of risk are the increasing focus on resulting trusts, foreign tax issues and dependant support claims.

Resulting Trusts

The May, 2007 Supreme Court of Canada decisions in *Pecore v. Pecore*, 2007 SCC 17 ("*Pecore*") and *Madsen Estate v. Saylor*, 2007 SCC 18 ("*Madsen*") dealing with resulting trust issues will no doubt generate considerable commentary in the months to come. They may also provide a strong rationale to delay distributions of estate assets. As these decisions filter through the profession and eventually help increase public consciousness about joint assets and resulting trusts, beneficiaries will likely become more sophisticated and demanding.

In the past, provided beneficiaries did not raise significant objections to a child of the deceased taking joint assets by right of survivorship on death, there was a tendency to accept the joint ownership at face value, assume the presumption of advancement applies and move on to administer genuine estate assets. In fact, there was no particular stress on determining the extent of jointly-held assets at the outset. That tendency was perfectly reasonable at the time, but not any longer.

Some excerpts from *Pecore* confirm the new law regarding resulting trusts and the presumption of advancement as set out by the SCC :

> First, given that a principal justification for the presumption of advancement is parental obligation to support their dependent children, it seems to me that the presumption should not apply in respect of independent adult children. [...] Second, I agree with Heeney J. that it is common nowadays for ageing parents to transfer their assets into joint accounts with their adult children in order to have that child assist them in managing their financial affairs. There should therefore be a rebuttable presumption that the adult child is holding the property in trust for the ageing parent to facilitate the free and efficient management of that parent's affairs. (para. 36)
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> [...]
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> I do not agree that affection is a basis upon which to apply the presumption of advancement to the transfer. Indeed, the factor of affection applies in other relationships as well, such as between siblings, yet the presumption of advancement would not apply in those circumstances. However, I see no reason why courts cannot consider evidence relating to the quality of the relationship between the transferor and transferee in order to determine whether the presumption of resulting trust has been rebutted. (para. 37)
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> [...]
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> I am therefore of the opinion that the rebuttable presumption of advancement with regards to gratuitous transfers from parent to child should be preserved but be limited in application to transfers by mothers and fathers to minor children. (para 40)

Given that the presumption of advancement has now been curtailed to apply only to minors, executors would be prudent to investigate very closely all significant jointly-

held assets. Since the evidentiary burden in cases of joint assets with children of the deceased has shifted, a particularly close look at those joint assets is warranted. Solicitors will need to decide for themselves how best to cover off these potential new issues, but certainly letters to the financial institutions with whom a deceased held accounts and investments should confirm that all jointly-held assets must be disclosed at the outset. In appropriate cases, the ambit of which has just widened considerably, the financial institutions should be put on notice that pending the results of the executor's inquiries, the assets must not be liquidated.

Whether the erosion of the heretofore presumption of advancement in favour of adult children (even disabled adult children no longer benefit from the presumption) will have significant ramifications in cases which inevitably turn on evidence of intention is open to some, but currently not much, doubt. Certainly it will impact on settlement negotiations, and given the percentage of these cases which settle, at the very least executors are likely to begin reaping better settlements in these types of cases.

It is a safe assumption, given rarity of SCC forays into the Estates and Trusts realm and the significance of the changes in the law heralded by *Pecore* and *Madsen,* that the decisions signal a considerable shift in the landscape favour of those making resulting trust claims in any situation, particularly executors doing so on behalf of estates. Some of the *obiter* commentary from the decisions will not doubt be showing up in factums in cases involving jointly-held assets with non-children.

In the face of *Pecore and Madsen*, executors who lean against challenging rights of survivorship by asserting a resulting trust against the surviving account holder in a

particular case would do well to demand clear and comprehensive releases and indemnities from all beneficiaries. Where independent legal advice is feasible, it should be encouraged. Even with those releases and indemnities, deciding not to proceed with a claim to joint assets on the basis of resulting trust still has risks. In situations with spousal or other testamentary trusts the circumstances or even the identities of the gift-over beneficiaries can change so much over time that a release or indemnity may not be enforced by the court. New beneficiaries can be born or come into play by the death of an initial beneficiary, and those new beneficiaries may not be as generously inclined as their predecessors. Family relations change as well, leading to bad feelings, hardening attitudes and a less forgiving approach. Certainly executors/solicitors relying on releases will expect them to be enforceable, but the executor will need to demonstrate consideration flowing to the beneficiary for signing a release of her entitlement to the proceeds of a resulting trust.

The risks are exacerbated by the fact that in view of the *Hartman Estate v. Hartfam Holdings Ltd.*, [2006] O.J. No. 61, (OCA), there may be no limitation period applicable to resulting trust and constructive trust claims:

> It is apparent that there is no clear, general answer to the question of whether claims to land based on resulting or constructive trust are subject to a statutory limitation period and, if so, whether the exceptions in s.43(2) (of the *Limitations Act, R.S.O.*, since repealed) apply to all trustees who hold property by way of resulting or constructive trust. In the case at bar, however, if the statutory limitation period does apply to such claims, for the reasons already given, [...] I would give a plain reading to s. 43(2) with the result that the proposed (constructive and resulting) trust claims fall within the second exception. para 85.

It is possible that the *Hartman* decision will need to be applied and even reassessed given the new *Limitations Act, 2002*, but until then, prudence suggests that executors assume there is no limitation period. Therefore, while the beneficiaries may initially profess not to want the Executor to chase after joint assets, such protestations can be transitory. Assets apparently or allegedly forming the corpus of a resulting trust, particularly real property, may be held over the long term, so the Executor could be asked, long after the administration is otherwise complete, to start proceedings to recover alleged trust assets. If the estate has been distributed, there will be no assets left with which to finance the litigation. Certainly there seems to be a growing pattern, ascertainable to many estate litigators, for beneficiaries to revisit prior views about the administration, long after the fact.

Executors may well wish to delay distribution of estates until one of the following can be established:

1. Undisputed joint assets of the deceased have been identified, realized, and treated as residue.

2. Questionable joint assets have been investigated and it is undisputed that the deceased demonstrably intended for rights of survivorship to apply. This, it must be stressed, will be an extremely difficult standard to meet with any degree of certainty. Each situation will have its own mix of unique facts and family history, much of which will be very much in dispute. In *Pecore*, for instance, the deceased signed a letter specifically saying that he was "the 100% owner of the assets and the funds are not being gifted to Paula", used and controlled the

accounts and declared and paid all taxes on the accounts: Nevertheless, three levels of Court found that a gift was intended.

3. With respect to disputed or questionable joint assets where the beneficiaries (and creditors to an insolvent estate) have been consulted and have unanimously released the executor from pursuing claims to the joint assets the release ought to specifically state that the beneficiary has been made aware of the potential expenses, risks and delays which could result from litigation to recover the resulting trust assets, and in order to avoid those pitfalls and hasten the winding up of the estate the beneficiary wants the executor to forego that litigation. An executor's letter to the beneficiaries explaining the expenses, risks and delays sent before the release was signed would help in later demonstrating that the beneficiary did indeed understand the situation. A Certificate of Independent Legal Advice would also be recommended where feasible.

4. Absent unanimity among beneficiaries, proceedings to recover apparent resulting trust assets by the executor should be strongly considered. A sufficient litigation holdback to cover potential fees, disbursements and GST all the way to trial, not only those of the estate but also the other side, should be maintained. In many estates this will mean no significant distributions until the litigation is concluded.

5. Where the executor is convinced that proceedings are not prudent, but beneficiaries disagree, then the executor may wish to proceed to pass accounts, specifically raising the issue of the potential resulting trust assets in the passing of accounts materials, and giving full notice to the beneficiaries as well as the

Court that the executor will be relying on the Court's judgment as a release of liability with respect to the original assets of the estate.

These protections may not suffice in every instance, but will likely at least establish to the court's satisfaction that the executor considered the matter thoroughly and acted in good faith. A Judgment Passing Accounts ought to be protection as a matter of principle without specifically referring to joint asset issues, but in practice it seems best to specifically refer to the joint assets as not forming part of the estate, so that if a beneficiary later claims lack of information about joint assets as a reason for not having objected to the accounts, the claim will not be successful.

Foreign Tax issues

A detailed review of the issues raised by foreign assets and foreign beneficiaries is beyond the scope of this discussion, but hopefully it is helpful to at least identify some of the issues.

a) Foreign Beneficiaries

Section 116 of the *Income Tax Act* (the "ITA") mandates that a non-resident beneficiary of a Canadian estate is deemed to be disposing of a capital interest when receiving a distribution of "taxable Canadian property"[1] and liable for capital gains taxes in the result. Since non-resident beneficiaries, having received a payment, are not

[1] Defined in s.115(1) of the ITA to include real property situate in Canada, capital property used in carrying on business in Canada, shares of a private corporation resident in Canada and capital interests in personal trusts resident in Canada.

necessarily the surest source of tax remittances to the Canada Revenue Agency ("CRA"), the ITA directs executors and trustees to withhold and remit 25% of a distribution to CRA within 30 days of the end of the month of the distribution. The withholding can be reduced to 25% of the net gain from the distribution, but only if the beneficiary first obtains a tax certificate of compliance.

Even where there is no capital gain, the remittance must be made.[2] If not, the executor faces a personal penalty of 10% of the unremitted tax, not to mention the possibility of the ongoing attention of CRA once non-remittance is discovered. If the executor is not a lawyer, the estate solicitor can expect to be questioned in short order once the consequences of non-remittance make themselves known.

b) Foreign Assets

Globalisation is affecting so many areas of society that it should not be surprising to witness its increasing impact on estate administration. The most common situation for Canadians is an estate with US assets, but any foreign jurisdiction may have its own particular twists and turns. In each case, local advice may be needed to avoid or resolve problems.[3] The US provides a helpful illustration of how Canadian-based assumptions can backfire.

US estate tax is considerable, and applies upon the death of US citizens and US resident aliens and also the death of non-US persons owning US property. Estate tax is

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[2] For a more fulsome summary of this issue, see "A Pot-Pourri of Six-Minute Issues", Hoffstein and Weigl, 9th Annual Estates and Trusts Summit.

[3] See "Will Planning for Canadian Residents With U.S. Connections", Paula Ideias, Bryan McNulty and Beth Webel (PricewaterhouseCoopers LLP), 9th Annual Estates and Trusts Summit.

novel to Canadians. It applies to the fair market value, not the inherent capital gains, of the property as at the date of death. Once the applicable tax credits and exemption amounts are exceeded, the highest US estate tax rate will equal or exceed 45% until 2009, and exceed 55% for the years 2010 and after. Changes or even the abolishment of this tax is often debated, but until concrete change takes place estate planning and administration needs to deal with the tax.

Joint tenancy may not mean the same thing in the US or other jurisdictions as it does in Canada, and may not have the same effect at death:

> For U.S. estate tax purposes, when there is a spousal joint tenancy and the surviving spouse is not a U.S. citizen, the entire value of jointly held property is included in the decedent's gross estate unless the executor submits facts sufficient to show that the property was not acquired entirely with consideration furnished by the decedent, or was acquired by the decedent and the other joint owner by gift, bequest or inheritance.

> Canadian income tax consequences should also not be ignored. If the joint tenancy is between spouses, the deemed disposition of the property at death will not occur until the death of the second spouse. This may result in foreign tax credit problems if U.S. estate tax is triggered on the first spouse's death. If there is a gain on the property, it may be best to elect out of the spousal rollover at the time of the first spouse's death.
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> [...]
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> As a result, joint ownership is not a recommended for of ownership for U.S. situs property or as a will substitute for property subject to U.S. estate and gift tax because the incidents of Canadian income tax and U.S. estate

> and gift tax may not apply at the same time or in the hands of the same taxpayer. In this case, it is very likely that double taxation will arise. Additionally, joint ownership may not allow the spouses to undertake effective will and estate planning for U.S. estate tax. [4]

In any case with US assets, of virtually any description, it is worth obtaining specialist advice to ensure that the both the CRA and US Internal Revenue Service ("IRS") can be satisfied. The last thing any Canadian executor, beneficiary or solicitor expects is problems with the IRS, particularly when used to dealing with the relatively (at least according to common perception) benign CRA. The same may be true of other jurisdictions. The best practice is to wait to make distributions until compliance with foreign rules is certain, and explain to the beneficiaries as early as possible the source of the delay.

Dependant Support Clams – Distribute Without Delay?

Under Ontario's *Succession Law Reform Act*, there is a six-month limitation period from the granting of a Certificate of Appointment of Estate Trustee during which an application for dependant's support must be brought, subject to an extension in the

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[4] Ibid, p.4.

discretion of the Court with respect to any portion of the estate remaining undistributed as at the date of the application. [5]

This limitation period does not, on its face, encourage delaying distributions: quite the contrary. Since extensions of the 6-month limitation can only be granted with respect to undistributed assets, the quicker the lion's share of the estate is distributed the sooner the risk of dependant's support proceedings is mitigated. However, increasingly alleged dependants who wait to bring claims only to find the estate has been distributed are trying to find candidates upon whom to pin blame. Executors and/or solicitors they have met with are being criticized for not having told them to seek independent legal advice. If they tell them to seek independent legal advice and a claim results, the other beneficiaries might blame the same executor for waking an otherwise sleeping dog. These problems are compounded where the alleged dependant suffers from a disability. This can be resolved by involving the Office of the Public Guardian and Trustee on a passing, but often a disability will not be severe enough to warrant that involvement. In the result, a potential claimant may not have the tools to realize on that claim.

The executor's duty is to act in good faith to maximize the residue of the estate to be distributed at the end of the day. Part of that duty is to resolve debts, liabilities and claims against the estate. It is a thorny question whether the duty to resolve claims extends to, in effect, actively inviting claims. Either way leads to exposure and some judicial direction may eventually be required.

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[5] R.S.O. 1990, c.S. 26, subsections 61(1) and (2)

From a practical point of view, it may be that all the other reasons to delay distribution will mean that alleged dependants are likely to have significant time within which to make a claim while other risks are minimized or eliminated, at least in most estates.

Solution – Litigation Holdback

With the ever-growing myriad of risks in administering estates, it can be a challenge not to allow the administration to linger into eventual or apparent paralysis. Eventually the estate must be administered and the risks ruled out so that the beneficiaries can receive their inheritance. However, due to all the possible permutations and combinations of factors dictating against rapid distribution, a considerable holdback should be considered at the outset, and of course explained at the outset to the beneficiaries so they can plan accordingly.

Many of the legal issues which hang over the administration can lead to require a trial to resolve if not settled. A litigation holdback ought to be of sufficient magnitude to cover fees, disbursements and GST all the way through trial for not one, but at least two parties, given the possibility of both sides' legal fees being ordered paid out of the estate. Obviously most beneficiaries are unlikely to take kindly to a professional or even family executor holding back tens (if not hundreds) of thousands of dollars based on unspecified and hypothetical litigation. In fact, the holdback itself could be the cause of a passing. As in so many situations involving fiduciaries, there are no easy answers. Each situation needs to be assessed and dealt with in the context of its particular facts.

Early and detailed communication with beneficiaries will resolve some, but not all, complaints.

The crucial requirement is to avoid having executors facing unanticipated problems without the resources to protect the estate and themselves.