

SOCIETY OF TRUST AND ESTATE PRACTITIONERS – ATLANTIC

Asset Protection: Are the Family Jewels Really Safe?

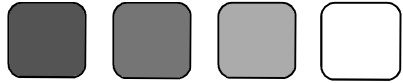
February 21, 2013

Presenters:

**Richard Niedermayer
Stewart McKelvey**

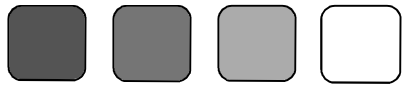
**Maurice P. Chiasson, Q.C.
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Davis Reiersen**



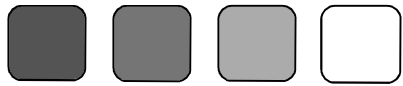
Setting the Stage

- A 2012 survey of high net worth families by Rothstein Kass Family Office Group determined that 51.4% of families surveyed have been involved in unjust lawsuits or divorce proceedings and 90.5% of those families were concerned that family members will be involved in unjust lawsuits or divorce proceedings.
- But only 47.3% of families had put in place a formal asset protection plan.



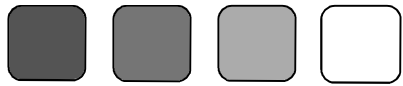
Setting the Stage, cont'd

- While we will discuss some tax issues in this presentation, tax planning and the tax implications of the strategies discussed are not the primary focus.
- Note: caution should be exercised when considering any of these asset protection strategies to ensure that the tax implications for establishing and maintaining these structures are properly understood, analyzed and addressed.



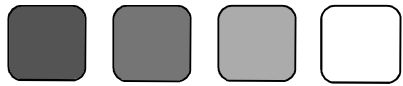
What types of claims could a person face in his or her lifetime or in his or her estate?

- Normal business debts, including those secured by personal guarantees.
- Damages for personal injuries and claims arising from motor vehicle accidents which exceed insurance policy limits.
- Personal liability imposed on directors of corporations by various federal and provincial statutes in connection with employee source deductions, environmental claims and other matters.



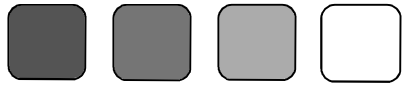
What types of claims could a person face in his or her lifetime or in his or her estate? (Cont'd)

- Claims by a spouse for division of matrimonial assets under matrimonial property legislation arising on marriage breakdown or death.
- Claims by a spouse and/or children under dependants' relief legislation arising from failure to make "adequate provision" for them in a will.

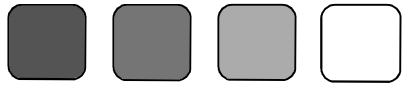


Regional Scope

- Although this seminar is addressed to estates and trusts practitioners in all four Atlantic Provinces, individual provincial statutes vary.
- While reference will be made to variations between the provinces from time to time, most of this seminar is based on Nova Scotia statutes.
- Comments on differences between provinces are welcome.

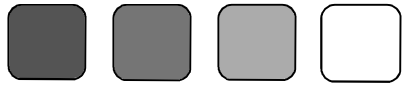


Fact Pattern

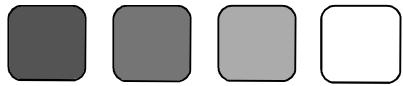


Meet Dick

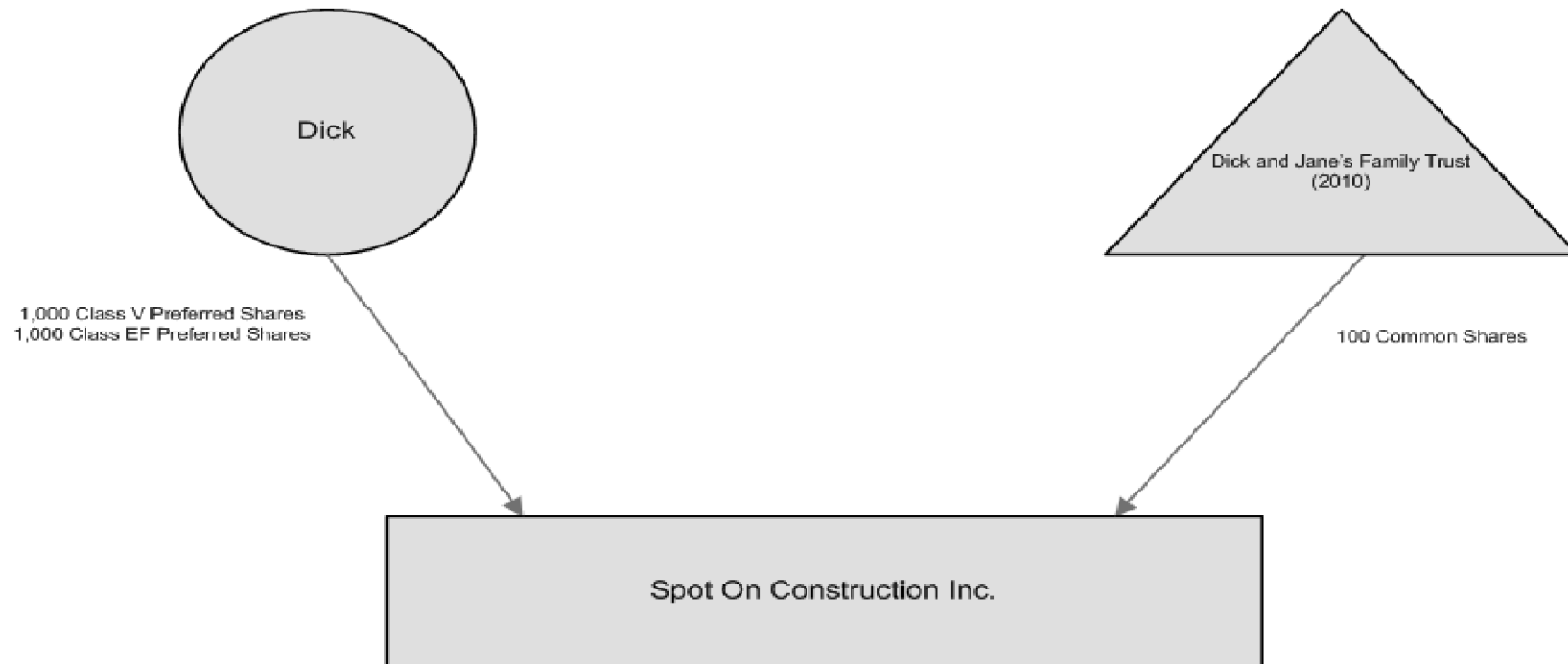




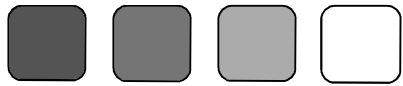
- Dick is 51 and is a successful businessman.
- He operates a construction company, Spot On Construction Limited, which does commercial property construction.
- At the suggestion of his accountant, Dick did a corporate reorganization a couple of years ago and put in place a family trust. Dick's org chart follows:



DICK'S CORPORATE HOLDINGS

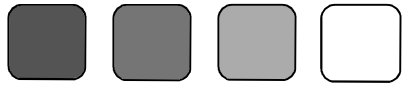


- NOTES:
1. Class V shares have nominal value
 2. Class EF shares have aggregate redemption value of \$5M
 3. Spot On runs business valued at \$1M (equipment and goodwill) plus owns a rental building worth \$3M and \$1M of investments/cash



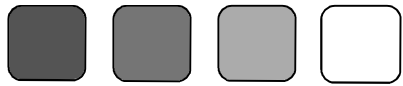
Dick's Company

- Most of the profits in Dick's company have been ploughed back into the company over the years as it expanded and took on bigger contracts.
- Spot On also holds:
 - corporate-owned life insurance on Dick's life with a \$1,000,000 death benefit;
 - a rental building worth \$3,000,000; and
 - redundant cash and investments of \$1,000,000.



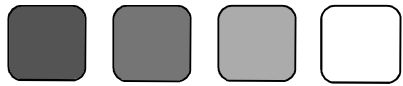
Dick's Family

- Dick is married to Jane, who carries on an immigration consultancy business as a sole proprietorship.
- They have two children, Nick and Sally, who are 22 and 18.



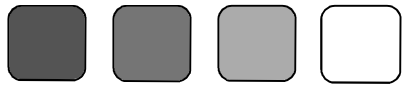
Dick & Jane's Assets

- In addition to Dick's corporate holdings, Dick & Jane's personal assets include:
 - the matrimonial home in Halifax, worth \$800,000;
 - a cottage on the South Shore worth \$300,000 (inherited by Dick);
 - Dick's RRSP of \$750,000;
 - Jane's RRSP of \$200,000; and
 - non-registered portfolio investments in Dick's name worth \$500,000.

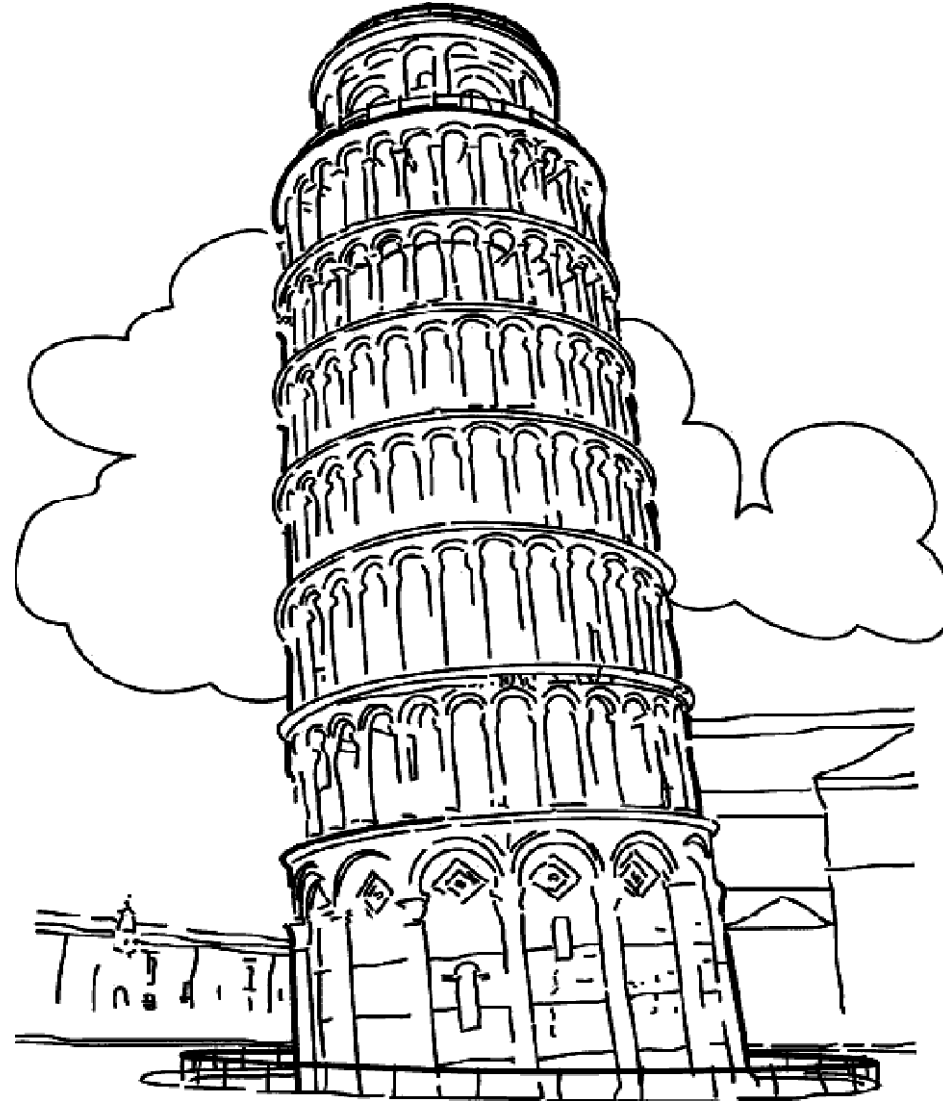


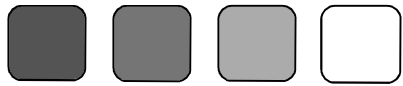
Dick & Jane's Assets, cont'd

- Dick was advised several years ago by his mentor to put all personal assets in his wife's name to avoid creditor claims that can arise in the construction industry.
- At Dick's direction, both the house and cottage were transferred solely into Jane's name.

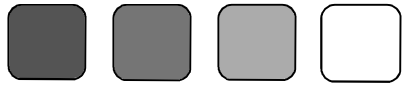


Scenario 1



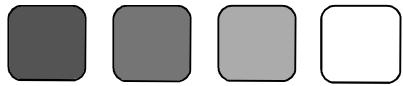


- Dick's business collapses (literally) after a partially finished building he was constructing collapses due to shoddy workmanship by his company, and there is no insurance as one of his employees lied on the construction bond application and coverage is denied.
- Dick faces lawsuits personally because of personal guarantees he had given to the company's lender.
- What can the bank get at in that situation?
- What about the employee source deductions that were not made before the collapse?



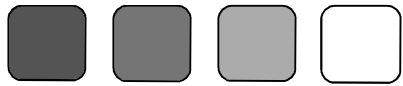
Address each specific asset in terms of creditor claims:

- Residual value of corporation/shares.
- Dick's RRSP.
- House and cottage.
- Non-registered investment assets.
- What if Dick files under the *Bankruptcy and Insolvency Act* – what rights would a trustee in bankruptcy have on behalf of creditors?



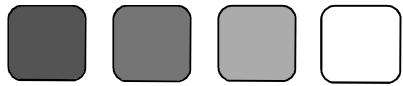
Creditor Issues

- For the purposes of the discussion, assume that Spot On has provided a general security agreement to its bank covering all present and after-acquired assets of the business.
- It is likely that the claims arising from the building collapse will trigger a default under the bank security (assuming normal covenant patterns and the company's inability to respond to the claim after the denial of coverage).



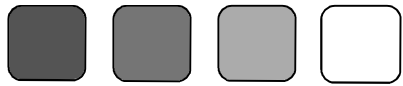
Creditor Issues

- Assuming that the bank has properly perfected its security interests with respect to the personal property of the company (*Personal Property Security Act*) and the real property of the company (*Land Registration Act*), the bank would have a first charge on the assets of Spot On ahead of the claims of any holder of a judgment arising from the collapse of the building.



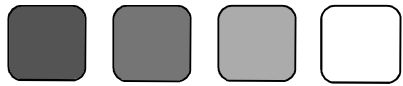
Creditor Issues

- The bank would enforce its security either through:
 - The appointment of a receiver to take over the business and ultimately sell the business (if there is any value) or the assets on a piece-meal basis;
 - A petition in bankruptcy and the resulting appointment of a trustee (not likely with a secured lender); or
 - Enforcement of security without taking control of the business.



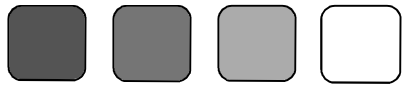
Creditor Issues - Specific Asset Issues

- Residual value of the corporation/shares:
 - Depends on whether the bank also has a pledge of shares.
 - Practically, not needed if the bank's security covers all assets. It can sell the business as a going concern or on a piece-meal basis depending on the best scenario for the bank.



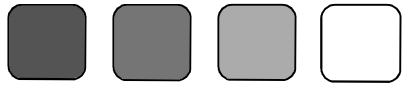
Creditor Issues – Specific Asset Issues

- Dick's RRSP
 - The rights of creditors are dependent upon the form of the RRSP contract.
 - Assume the bank does not have any specific security from Dick as collateral for guarantee.
 - The bank would rank as an unsecured creditor with respect to any claims against Dick.



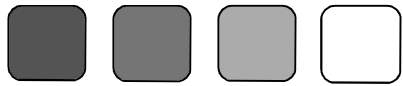
Creditor Issues – Specific Asset Issues

- If the RRSP is backed by a life insurance contract, the RRSP is exempt from execution provided there is a beneficiary designation in favour of a spouse, common-law partner, child, grandchild or parent of insured (*Insurance Act*, s. 198(2)).
- There is no exemption if the beneficiary is Dick's estate.
- There is no exemption (under provincial law) where the RRSP is not backed by life insurance.
- Corporate life insurance policy not protected from creditors – cash surrender value could be available



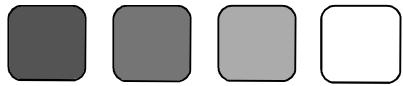
Creditor Issues – House and Cottage

- Since the house and cottage are in Jane's name, they are not within the reach of Dick's creditors (unless Jane has provided a guarantee of Spot On's debts).
- Even if Jane provided such a guarantee, there would be no claim against the matrimonial home unless Jane had consented to a mortgage on the property (*Matrimonial Property Act*, s. 8(1)(a)).



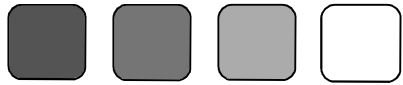
Creditor Issues – House and Cottage

- The facts tell us that the conveyance of the properties was made to Jane “several years ago”.
- A creditor may wish to confirm exactly when the conveyance was made and what Dick’s circumstances were at the time.
- The *Bankruptcy and Insolvency Act* refers to the concept of a transfer “at undervalue” (i.e., less than fair market value).



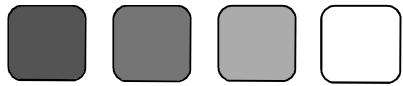
Creditor Issues – House and Cottage

- Such a transfer can be reviewed by a trustee:
 - If made within one year of bankruptcy to a person dealing with the debtor at arm's length and where debtor was insolvent at the time and transfer made with an intention to defraud, delay or defeat creditors.
 - Time period is five years with reference to a transaction with a non-arm's length person subject to same tests as above. Within one year, the tests need not be met.



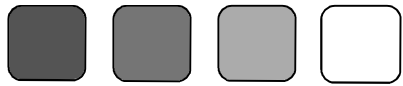
Creditor Issues – House and Cottage

- If successfully attacked by trustee, conveyance is essentially put back into Dick's hands and the property would become subject to claims from Dick's creditors
- However, in the case of the matrimonial home, Jane's consent would still be needed for a claim against her half-interest (which makes the home practically not subject to attack).



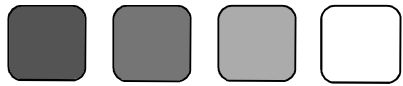
Creditor Issues – House and Cottage

- Even if there is no bankruptcy, creditors may have resort to:
 - *Assignments and Preferences Act*, R.S.N.S. 1989, c. 25
 - Applies to transfers to creditors (i.e., would only apply where Jane was a creditor at the time the transfer was made).
 - Attacking creditor must prove intent to “defeat, hinder, delay or prejudice” creditors.
 - There is a presumption of such intent where claim is made within 60 days of transfer.



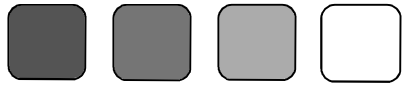
Creditor Issues – House and Cottage

- Even if there is no bankruptcy, creditors may have resort to:
 - *Statute of Elizabeth, 1571* (13 Eliz. 1, c. 5)
 - Transfer with intent to delay, hinder or defraud creditors and others can be voided.
 - No time limit.
 - No need to prove debtor was insolvent at the time.



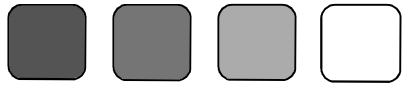
Creditor Issues – House and Cottage

- General Comment
 - All such proceedings are expensive and likely difficult to prove.
 - Particularly messy where matrimonial homes are involved.
 - Requires a creditor who is owed a great deal of money, who has the resources to pursue a claim, and is particularly angry with the debtor.



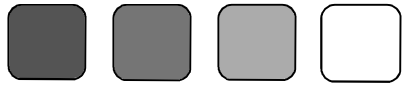
Creditor Issues – Unregistered Assets

- The facts tell us that there are unregistered assets owned by Spot On and some by Dick personally.
- Unless these assets are backed by life insurance, they should be available to Spot On's and Dick's creditors – most likely the bank.



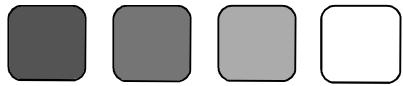
Creditor Issues – CRA Claims

- Spot On had not made its employee source deductions prior to the collapse of the building
- Canada Revenue Agency will have priority over the bank and Spot On's other creditors for any amounts not remitted.
- CRA will have the same claim for any HST collected from Spot On's customers but not remitted.



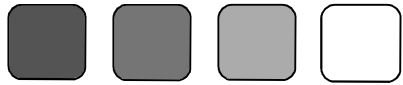
Creditor Issues – CRA Claims

- The claim from CRA for source deductions will survive the bankruptcy of Spot On.
- The claim from CRA for unremitted HST will not survive a bankruptcy.
- Common for a secured lender to cause the bankruptcy of Spot On to reverse the HST priority.



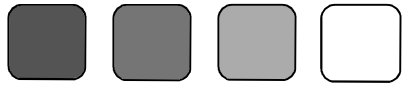
Creditor Issues – CRA Claims

- Where there is a shortfall for CRA, Dick (and any other directors) may face a personal claim from CRA:
 - Defence – director must exercise due diligence
 - Claim must be made within two years after person ceased to be a director.
 - Just because the company is bankrupt or otherwise insolvent does not mean the directors have ceased to be directors. Must actually resign in accordance with corporate law requirements.



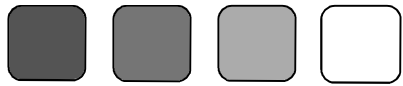
Creditor Issues - Bankruptcy

- Dick makes an assignment in bankruptcy.
- Dick will be absolved of “most debts” when discharged.
- If never bankrupt, discharge generally happens after nine months without conditions.
- Second time, could take up to 24 months, likely with payment conditions (which could take an extra year).



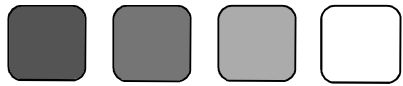
Creditor Issues - Bankruptcy

- CRA may contest discharge where there is an outstanding tax debt.
- Other creditors may also contest.



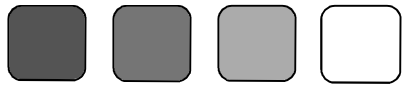
Creditor Issues - Bankruptcy

- Some debts not released by bankruptcy (*BIA*, s. 178)
 - Any fine, penalty or restitution order imposed by court in respect of an offence;
 - Award for damages for bodily harm or wrongful death;
 - Liability for alimony or child support;
 - Debt arising from fraud or similar matter; and
 - Debt arising from obtaining property or services under false pretences.



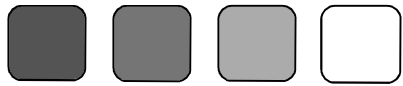
Creditor Issues - Bankruptcy

- If there is a claim made against Dick personally under *Occupational Health and Safety Act*, this claim may survive bankruptcy.
- Matrimonial claims.



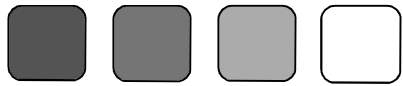
Creditor Issues – Bankruptcy

- *BIA* (s. 67) exempts certain property from the reach of the trustee:
 - Any property held in trust for another person.
 - Property exempt from seizure under provincial legislation (RRSP backed by life insurance).
 - RRSP or RRIF (not otherwise exempt) except for contributions made within the last 12 months.
 - GST credits.



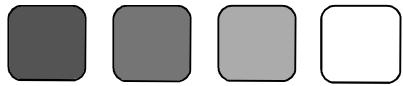
Spin – What if Jane also has a creditor claim because of a problem with her business? How will that affect her assets?

- House and cottage.
- Her RRSP.
- Dick's assets.



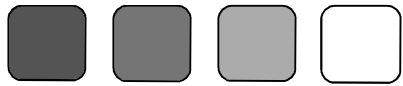
Insolvency Issues - Jane

- House and Cottage – Since she is the title holder, these assets are potentially available subject to Dick's rights in relation to the matrimonial home.
- RRSP – same issues as for Dick, depends on whether the RRSP is backed by life insurance and whether there is a bankruptcy.
- No claim against Dick's assets unless there is some sort of guarantee.



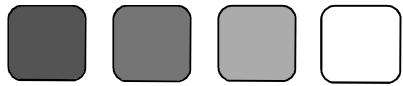
Scenario 2





Jane catches Dick having an affair with one of his female co-workers, Aimee, and seeks a divorce. How will the courts deal with the division of assets?

- House and cottage.
- RRSPs.
- Non-registered investments.
- Dick's shares of company.
- Shares held in the family trust.



Basic *Matrimonial Property Act* (Cont'd)

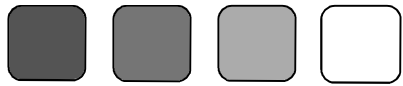
- s.4 “matrimonial assets” defined

4(1) In this Act, “matrimonial assets” means the matrimonial home or homes and all other real and personal property acquired by either or both spouses before or during their marriage, **with the exception of**

(a) gifts, inheritances, trusts or settlements received by one spouse from a person other than the other spouse **except to the extent to which they are used for the benefit of both spouses or their children;**

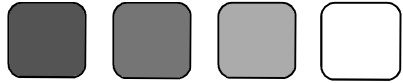
...

(e) business assets;



Basic *Matrimonial Property Act* (Cont'd)

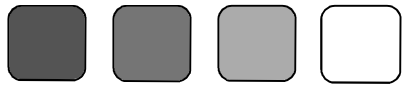
- s.2 (a) “business assets” means real or personal property **used or held for or in connection with a commercial, business, investment or other income-producing or profit-producing purpose**, but does not include money in an account with a chartered bank, savings office, loan company, credit union, trust company or similar institution where the account is ordinarily used for shelter or transportation or for household, educational, recreational, social or aesthetic purposes.



Basic *Matrimonial Property Act* (Cont'd)

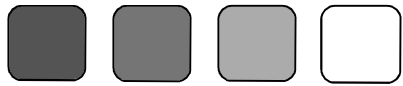
Court's interpretation of the definition of Business Assets:

- “assets which are truly of a business character”
- “to find assets are business assets simply because they are connected with a business is contrary to the intention of the legislation”
- “employment of capital for the purpose of generating income in an entrepreneurial sense”
- “used for relatively immediate gain and not once that is merely held for the purpose of future security”



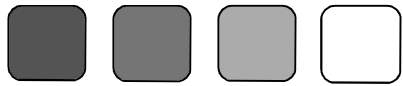
Basic *Matrimonial Property Act* (Cont'd)

- s.13 Factors considered on division
- 13 Upon an application pursuant to Section 12, the court may make a division of matrimonial assets that is not equal or may make a division of property that is not a matrimonial asset, where the court is satisfied that the division of matrimonial assets in equal shares would be unfair or unconscionable taking into account the following factors:
- ...
- (f) **the effect of the assumption by one spouse of any housekeeping, child care or other domestic responsibilities for the family on the ability of the other spouse to acquire, manage, maintain, operate or improve a business asset;**
 - (g) the contribution by one spouse to the education or career potential of the other spouse;
 - (h) the contribution made by each spouse to the marriage and to the welfare of the family, **including any contribution made as a homemaker or parent;**



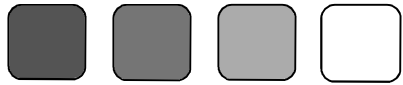
Basic *Matrimonial Property Act* (Cont'd)

- s.18 Contribution to business asset by spouse
- 18 Where one spouse has contributed work, money or moneys worth in respect of the **acquisition, management, maintenance, operation or improvement of a business asset** of the other spouse, the contributing spouse may apply to the court and the court shall by order
- (a) direct the other spouse to **pay such an amount** on such terms and conditions as the court orders **to compensate the contributing spouse** therefore; or
 - (b) **Award a share of the interest of the other spouse in the business asset** to the contributing spouse in accordance with the contribution, and the court shall determine and assess the contribution without regard of husband and wife or the fact that the acts constituting the contribution are those of a reasonable spouse of that sex in the circumstances.



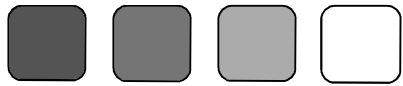
Matrimonial Assets

- (a) It does not matter who holds title to real property;
- (b) Cottage inherited by Dick but was used for family purposes?;
- (c) No – your investment account is not a “business asset” even if you give your broker “instructions”; and
- (d) RRSPs are equally divided.



Business Assets

What I go looking for 😊



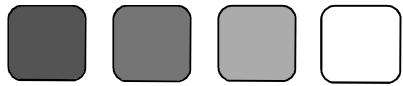
Business Assets, cont'd

(a) Who holds shares?

(i) Dick – common/preferred shares and/or Jane (for “income splitting” purposes);

(ii) Trust

- What you call it
- Who controls it/who are the trustees
- Who are the beneficiaries



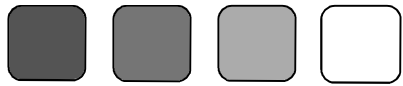
Business Assets, cont'd

- (b) Redundant Assets (investment accounts, vacation property, vehicles, boat)

- (c) Shareholder Loan account
 - (i) What is it?

 - (ii) What does it look like (cash or not)?

 - (iii) How is it “used” (personal savings account, personal operating bank account)?



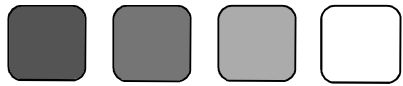
Business Assets, cont'd

Eyking v. Eyking 2012 CarswellNS 914, 2012 NSSC 409

115 . . . The Respondent **did not provide convincing evidence of a good business reason to retain the loans** by the corporation aside from generalities about the future capital needs of the business and the desire to maintain a healthy balance sheet to avoid unexpected risks in the business. Approximately six years after the date of separation there was no indication the loans were used for these purposes. A capital budget was not prepared or made available to the Petitioner for review and assessment of the unreasonableness of the Respondent's claims that funds are needed.

. . .

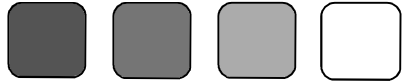
117 The desire to maintain healthy company balance sheets which will ensure the continued successful operation of the businesses and the involvement of future generations of the family through self financing and other conservative business practices is commendable. However, these objectives and the shareholders agreement that unanimous consent is needed to withdraw funds from the shareholders account are subject to appropriate claims pursuant to statutes like the *Matrimonial Property Act*.



Business Assets, cont'd

118 One of the advantages of operating a family business is the ability to extract funds from the business on a discretionary basis and when the family has personal financial needs. Declaring a bonus is away to extract funds not related to performance. Large bonuses were paid to the shareholders and then returned to the business. It then appears that these funds were invested in marketable securities which generated additional income in the company.

119 **The business holds many redundant assets that are not needed for the daily operation of the business.** I am aware of the Respondent's argument that the funds provided by the loans are being held as additional capital to address unexpected risks which may arise in the business, the need for capital expenditures and the desire not to rely on outside financing for these needs. However, **there appears to be overcapitalization of the company** as evidenced by Mr. Keough's finding that 76% of the company's assets were in non farm related assets. Therefore, **it is reasonable to conclude that the debt investment in the business represents the Respondent's investment in the business which is not required for business purposes.** I have considered the total amount of shareholder loans by all shareholders and not just the Respondent in concluding that the businesses are overcapitalized for their needs.

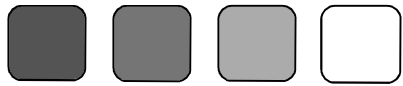


Business Assets, cont'd

120 In my opinion, if the shareholder loans are not needed for the day to day operations of the business or reasonably foreseeable capital requirements, they are more fairly classified as a family investment and not a business investment...

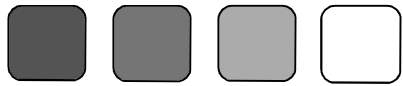
...

122 If I am incorrect in classifying the shareholder loans as matrimonial, I would order a division of these loans pursuant to s.13 of the *Matrimonial Property Act*, supra.



Business Assets, cont'd

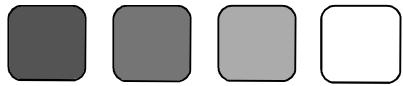
- (d) Hold Co. and/or rental or other “side” business
 - (i) What you call it / how you describe it (at a family party, meeting with the bank or to your father-in-law!)
aka don't brag
aka keep your mouth shut
 - (ii) How you run it
 - (iii) Who is involved



Business Assets, cont'd

(e) Other Problems for Dick

- (i) Personal guarantees and other ways of putting business assets at risk (start up and ongoing)
- (ii) “Splitting income” – tax effective but . . .
- (iii) Jane working for Spot On
 - With pay
 - Without pay
- (iv) Fairness / discretion in court
- (v) Lack of understanding by the Court of “capital” / “retained earnings” and “trusts”
 - *Prince v. Prince* Trial Decision
 - *Prince v. Prince* Court of Appeal Decision



Business Assets, cont'd

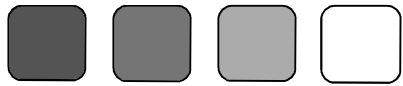
Prince v. Prince 1996 CanLII 5362 (NS SC): [Trial Decision]

"The "capital portion" was acquired by Mr. Prince. It remained the asset of Mr. Prince. The burden is on Mr. Prince to show it should be excluded from the category of matrimonial assets because it falls within the exception of business assets by virtue of Section 4(1)(e).

...

What is the evidence adduced on which Mr. Prince can say the "capital portion" was held or used for the production of income or profit? Has Mr. Prince satisfied the burden on him to prove the purpose of the "capital portion" is the generation of income in an entrepreneurial sense? There was little evidence on the use and purpose of the money. Mrs. Prince said funds of hers went into the business and when required for matrimonial purpose, came out of the business.

I find that Mr. Prince has not met the burden. **The sum of money is simply an account Mr. Prince maintains and which he chooses to keep in his business accounts.** Taxes have been paid on the sum. It is not an asset which generates income or a profit. Mortgages are assets which generate income for the business. Mr. Prince stated in his evidence that money for the couple's joint account come from taking money from the business. I accede to the description given to the money by Mrs. Prince when she says it is no different from a personal bank account of Mr. Prince. It could have been brought home for matrimonial purposes at any time."



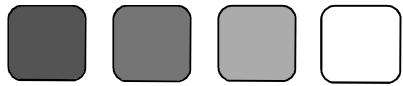
Business Assets, cont'd

Prince v. Prince 1997 CanLII 1209 (NS CA): [Appeal Court Decision]

The "capital portion" so-called, is not a bank account and not an asset separate from the business. Either PFC was a matrimonial asset, or it was not. It is clear from the trial judge's analysis that he considered the "capital portion" to be an asset distinct from the business itself. In this regard he asked himself. "What is the evidence adduced on which Mr. Prince can say that the 'capital portion' was held or used for the production of income or profit?" In answering that question the trial judge said:

The sum of money is simply an account Mr. Prince maintains and which he chooses to keep in his business accounts. Taxes have been paid on the sum. It is not an asset which generates income or a profit. Mortgages are assets which generate income for the business.

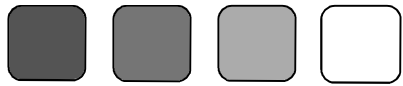
It was the evidence that Mr. Prince not uncommonly paid household bills from the business. Where he did so, however, the funds expended were characterized as a withdrawal by him for the purposes of calculating his taxable income. The fact that Mr. Prince could control the flow of funds from the sole proprietorship did not define its character as a business or matrimonial asset. PFC was a business owned by the husband prior to marriage. From that business he derived his income which he contributed to the support of the family. **There was no evidence that Mr. Prince had withheld funds from the family or structured his affairs so as to preclude Ms. Prince sharing in this asset.** In this respect the trial judge said: "That is not to say that Mr. Prince attempted to thwart the provisions of the **Matrimonial Property Act** or that this arrangement was made in any way to purposely divest Mrs. Prince from moneys to which she is entitled." Any entitlement by Linda Prince to share in this asset turned solely upon the classification of PFC. It is clearly a business asset within the definition of the **Matrimonial Property Act**:



Business Assets, cont'd

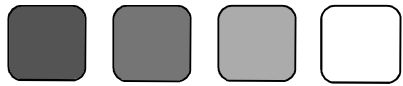
2(a) "Business assets" means real or personal property primarily used or held for or in connection with a commercial, business, investment or other income or profit-producing purpose, but does not include money in an account with a chartered bank, savings office, loan company, credit union, trust company or similar institution where the account is ordinarily used for shelter or transportation or for household, educational, recreational, social or athletic purposes.

The trial judge apparently concluded that the "capital portion" of the PFC fit within the latter part of this definition of "business asset" as money in an account used for matrimonial purposes. With respect, he erred. PFC is a business asset. The appellant shall succeed on this ground of appeal.

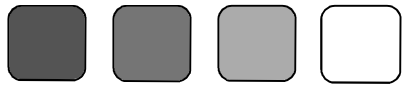


Scenario 3



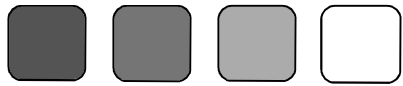


- Dick surreptitiously has an affair with Aimee and has a lovechild, Cherie, with his paramour.
- Fast forward fifteen years. To protect Aimee and their child, Dick, unbeknownst to Jane, leaves his shareholder loan in the company (all his freeze shares have been redeemed over time for a note) and his non-registered portfolio (which has grown to \$1,000,000) to Aimee in trust for Cherie, now age 14, in his will.



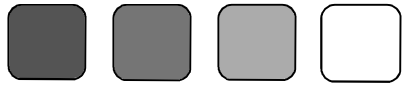
Scenario 3, cont'd

- Other assets remain passing to Jane, including his RRSP, which is designated directly to her already.
- Dick then dies suddenly at age 66. What happens?



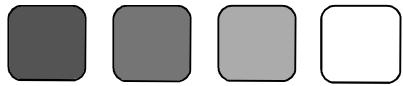
How Would the Court Deal with These Issues?

1. Jane's claim under the *Matrimonial Property Act*.
2. Jane's claim under the *Testators' Family Maintenance Act*.
3. Do Nick and Sally have any claim?
4. Does Cherie have any greater claim?



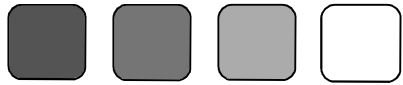
1. *Matrimonial Property Act*

- Provides for division of a family's property when the relationship ends, whether by separation or death (except PEI *Dependants of a Deceased Person Relief Act*)
- s. 12 allows surviving spouse to apply for equal division of matrimonial assets on death



MPA, cont'd

- Right of surviving spouse under *MPA* is in addition to rights arising on intestacy or by will
- So Jane is presumptively entitled to everything passing to her by will, plus 50% of any other matrimonial assets not left to her by will
- This can be addressed by an election clause in the will - take the gift but only if, within six months, the spouse waives a division of matrimonial assets (condition precedent to gift)



Compare Jane's Share and Cherie's Share (current values)

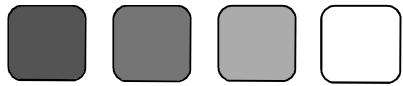
Jane

- \$1,000,000 Dick's RRSP
 - \$ 500,000 Jane's RRSP
 - \$1,000,000 house
 - \$ 500,000 cottage
 - \$1,000,000 common shares
(held by trust)
 - \$1,000,000 life insurance
(from Spot On)
 - personal & household effects
- \$5,000,000**

Cherie

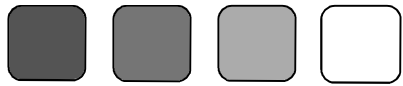
- \$1,000,000 portfolio
- \$5,000,000 shareholder loan

\$6,000,000



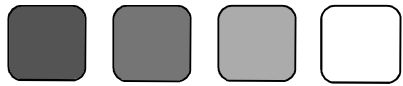
Matrimonial Assets

- If Jane can seek equal division under s. 12 of *MPA*, non-registered investment portfolio is going to be caught as matrimonial asset (as Lynn noted, not going to succeed in claiming it's a business asset)
- Shareholder loan – argue it's a business asset and exempt from division, but will likely fail (per *Eyking v. Eyking*)



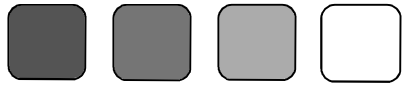
Unequal Division

- Presumption is for equal division, but Court may make unequal division under s. 13, where equal division would be unfair or unconscionable in circumstances
- Strong case for unequal division in situation where there are competing moral claims between Jane (adult spouse) and Cherie (minor child of another relationship)
- Safe to assume Cherie will not be provided for in Jane's will



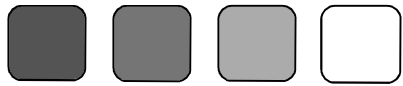
Unequal Division, cont'd

- Also consider cottage, which was inherited by Dick from his family
- Could argue that it should not be marital asset, but likely that it was used for the benefit of whole family



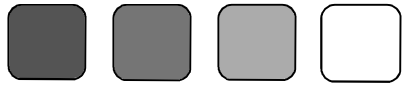
Marriage Contracts or Pre-Nuptial Agreements

- Couples can enter into an agreement
 - before (marriage contract/pre-nuptial agreement) or
 - at the end (separation agreement)
- Marriage contract must be in writing, signed and witnessed
- Contracts must be of “utmost good faith”
- Financial disclosure and independent legal advice are key



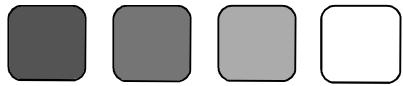
2. Dependants' Relief Legislation

- At common law, a testator has the right to dispose of his or her property in any way he or she chooses (subject to some policy considerations).
- But where a testator dies without having made adequate provision in his or her will for proper maintenance and support of a dependant, Court has power to order adequate provision out of the estate.

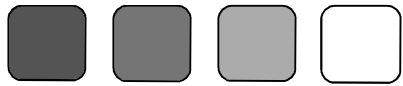


Dependants' Relief Legislation in Atlantic Provinces

- *Testators' Family Maintenance Act*, R.S.N.S. 1989, c. 465
- *Dependants of a Deceased Person Relief Act*, R.S.P.E.I. 1988, c. D-7
- *Provision for Dependants Act*, R.S.N.B. 1973, c. P-22.3
- *Family Relief Act*, R.S.N.L. 1990, c. F-3

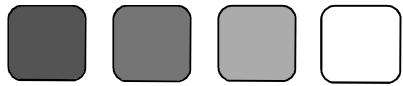


- Historically, dependants' relief legislation only applied to assets passing by will.
- Still the case in NS, but now applies on intestacy in PEI, NB, and NL, if intestate succession legislation does not make adequate provision for dependant.



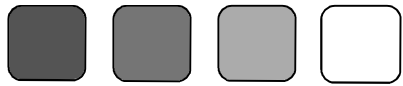
Testators' Family Maintenance Act, s.3(1)

“Where a testator dies without having made adequate provision in his will for the proper maintenance and support of a dependant, a judge ... has power, in his discretion and taking into consideration all relevant circumstances of the case, to order that whatever provision the judge deems adequate be made out of the estate of the testator for the proper maintenance and support of the dependant.”



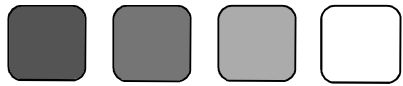
Who is a dependant?

1. Testator's widow or widower—not common law spouse in NS (unless registered domestic partners—rare)
2. Testator's child, including a child
 - a) lawfully adopted by the testator
 - b) of the testator but not born at the date of death ("*en ventre sa mère*")
 - c) of which the testator is the natural parent



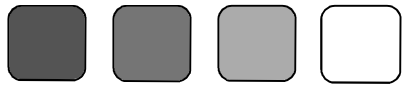
Who Qualifies as a Dependant, cont'd

- In PEI, dependant must actually be dependant if not a spouse
- In NB, legislation encompasses not only spouse and children, but any other person who is dependant on deceased at time of death, within meaning of *Family Services Act*
- In PEI and NB, common law spouses qualify as dependant



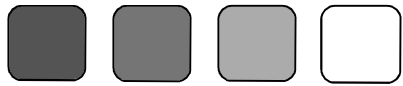
Statutory Factors under *TFMA*

1. Character or conduct of the dependant
2. Whether the dependant is likely to become possessed any other provision for maintenance and support
3. Relations of the dependant and the testator at the time of death
4. Financial circumstances of the dependant



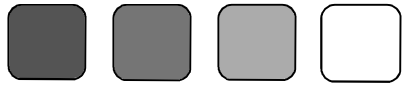
Statutory Factors, cont'd

5. Claims of other dependants on the estate
6. Any provision made for the dependant during testator's life
7. Any services rendered by the dependant to the testator
8. Any provision made by the dependant for the testator during testator's life



Evidence of Testator's Reasons

- Judge may receive any relevant evidence of the testator's reasons for making the will or for not making provision for a dependant
- Includes admitting any statement in writing signed by the testator

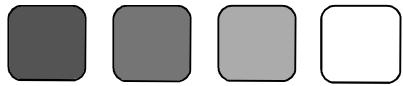


Two-Part Test

1. Is there need?
2. Is there a moral claim?

See, for example,

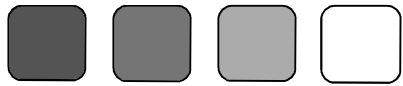
- *Garrett v. Zwicker* (1976), 15 N.S.R. (2d) 118 (S.C.A.D.)
- *Kuhn v. Kuhn Estate* (1992), 112 N.S.R. (2d) 38 (S.C.T.D.)



No Contracting Out, s. 16(2)

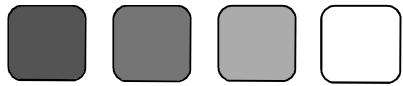
“If a dependant has entered into any agreement with a testator in his lifetime the consideration for which is a promise by the dependant not to apply under this Act for relief from the provisions of the testators will, such promise is not binding upon the dependant under this Act.”

- So, while a separation agreement or marriage contract between Dick & Jane might be a factor for a judge to consider, it's not automatically binding under the *TFMA*



Factors Court Would Consider

1. Status of Jane's consultancy business – how well is she doing on her own?
2. Aimee's circumstances and means
 - what are Aimee's income and assets?
 - is Aimee married?
 - if so, has Cherie been adopted by step-parent?
3. Circumstances of Nick and Sally
 - any need?
 - what provision already made for them before death?

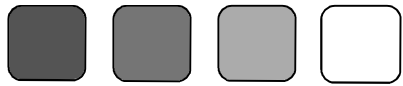


3. What About Nick & Sally?

- Might expect Jane to provide for them in her will
- No automatic rule that Court won't order a share to children even while Jane is alive, but

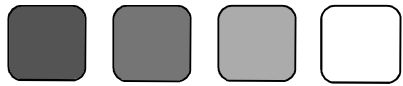
“...in the case of a widow the court will make more ample provision than in the case of children, if the children are physically and mentally able to maintain and support themselves.”

Zwicker Estate v. Garrett (1976), 15 N.S.R. (2d) 118 (S.C.A.D.),
quoting *Allardice v. Allardice* (1910), 29 N.Z.L.R. 950 (C.A.)



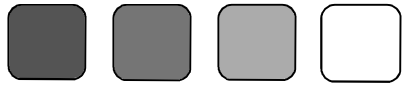
Per MacKeigan, C.J. in *Garrett v. Zwicker*

“All ‘dependents’ of a testator do not necessarily have moral claims of equal strength. A testator is entitled, for example, to discriminate among his children, giving one more than another, for good reason or no apparent reason, so long as he commits no ‘manifest wrong’ in failing to give one the minimum that is ‘proper maintenance and support’ in the circumstances...”



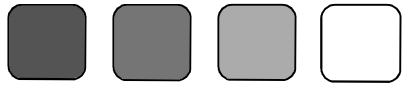
Nick & Sally, cont'd

- Nick & Sally are 37 & 33 respectively now
- Compare their situations and circumstances with Cherie
 - education completed, probably paid for by Dick
 - probably employed
 - possibly married to another income earner
- But completely disinheriting them could attract a claim, particularly given size of estate
- Grandchildren could be a factor

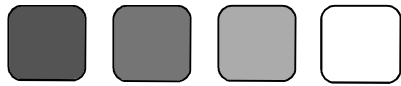


4. Can Cherie Expect Any More?

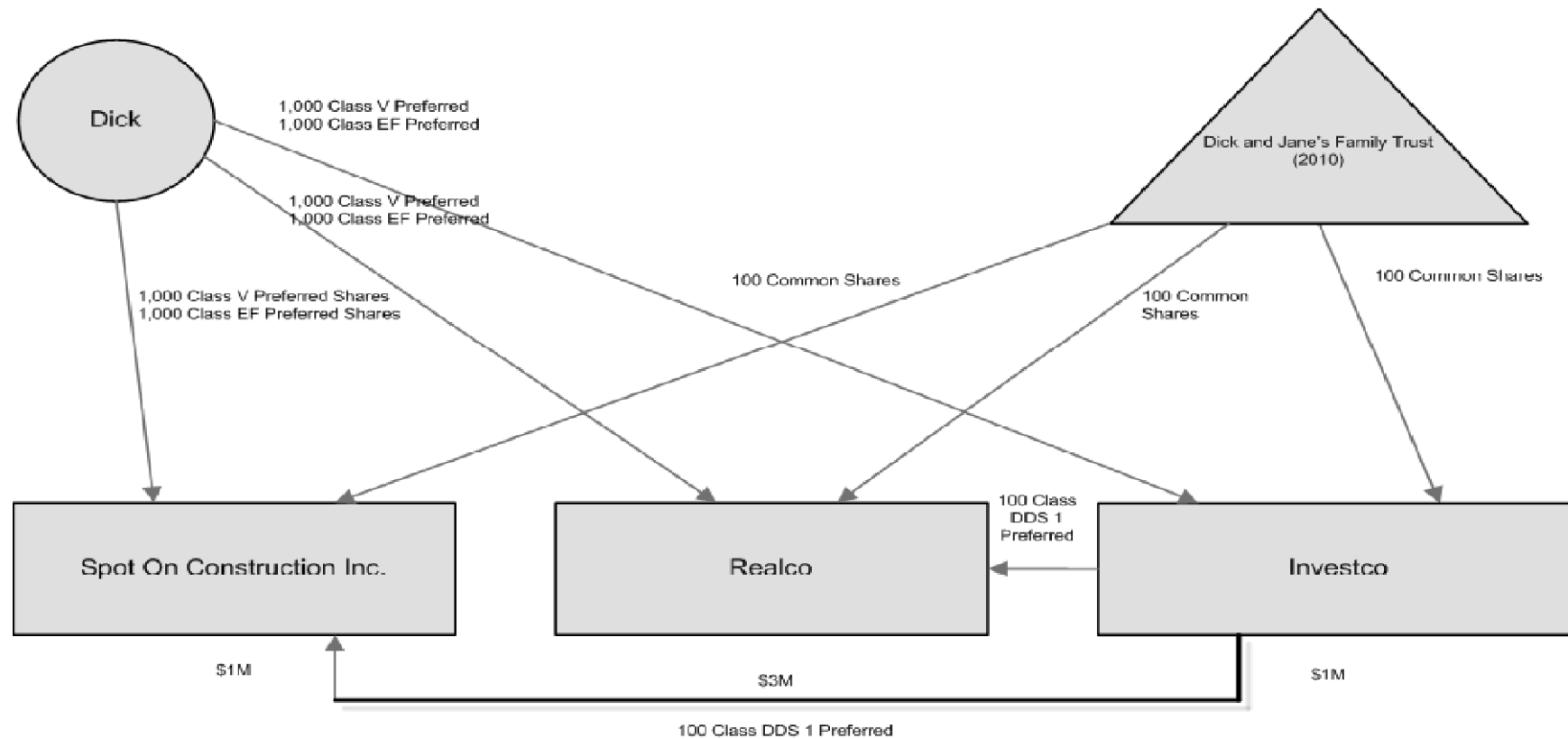
- Again, depends on Aimee's circumstances and Cherie's own circumstances, but not likely, given competing moral obligations to Jane, Nick, and Sally.



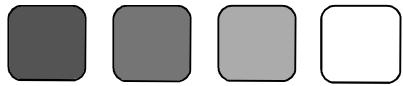
What could Dick have done differently in Scenario 1?



ALTERNATE CORPORATE STRUCTURE

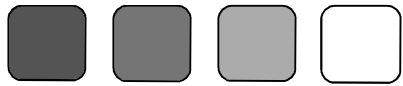


- NOTES:
1. Consider name of trust re MPA
 2. Consider Class V Preferred re creditors – is controlling through the trust a better approach? What can a creditor do with them? What if they are in an asset protection trust?
 3. Consider moving Class EF Preferred Shares to an asset protection trust (but consider tax issues on settlement to trust).



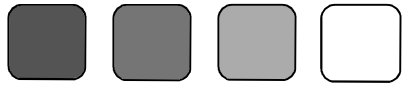
Advice for Dick on Scenario 1

- Incorporation of Holdco(s) to hold insurance and other redundant working cash and assets currently in the company.
 - Consider cross guarantees.
 - Obey the rules you set for your corporate structure.
- Consider secured loan back strategy following regular profit flow annually from operating company to holding company to help to secure working capital .

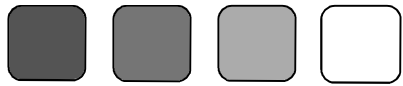


Advice for Dick, cont'd

- Consider asset protection trust in light of *Assignments and Preferences Act*, *Statute of Elizabeth*, and *Bankruptcy and Insolvency Act* considerations.
- What if the trust was offshore?

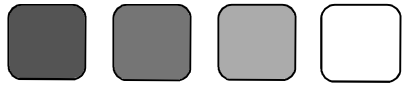


What could Dick have done differently in Scenario 2?



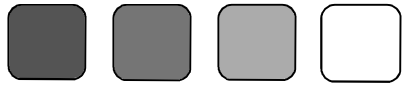
Solutions for Dick in Scenario 2

- i. Pre/Post-Nup and/or up front discussion
- ii. Mix of assets (business and matrimonial) or “what to do with corporate profits?”
- iii. Paying attention to fairness (or Don’t be a Dick...)
- iv. Lack of understanding by opposite counsel
- v. “Generous” attitude

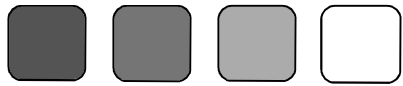


Issues for Dick's Advisors in Scenario 2

- i. Who is your client?
- ii. Who are you meeting with?
- iii. Report on advice re: getting advice

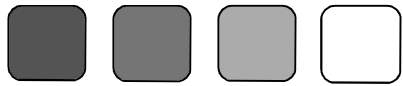


What could Dick have done differently in Scenario 3?



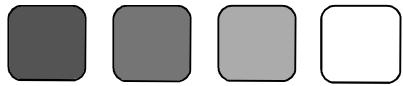
Use of Will Substitutes in Scenario 3

1. Make an *inter vivos* gift to Aimee in trust for Cherie now.
 - But triggers tax on gains immediately.
 - Creates possibility of awareness of Cherie by Jane.



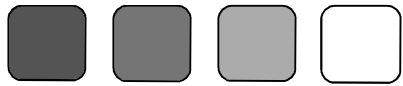
Will Substitutes, cont'd

2. Settle assets on Cherie using an irrevocable *inter vivos* trust, with Aimee as trustee, instead of leaving assets by will.
 - Could use an *alter ego* trust, since Dick is over 65, to avoid capital gains on Dick's investment portfolio.
 - However, *alter ego* trust would require that all income be paid to Dick during his lifetime.
 - Depending on circumstances of Aimee and Cherie, there may be a desire to pay income for Cherie now.
 - Same considerations about awareness.



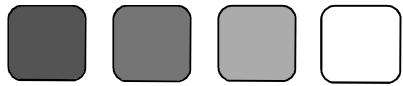
Will Substitutes, cont'd

3. Add Aimee as a joint holder on the investment account, documenting Dick's intention that legal title pass to Aimee by right of survivorship, in trust for Cherie.



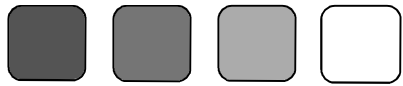
Will Substitutes, cont'd

4. Use beneficiary designation on a new insurance policy to provide for Cherie (designate Aimee in trust for Cherie).
 - Trust would be testamentary and terms could be customized to suit Cherie's circumstances.
 - Simple solution, but has costs.



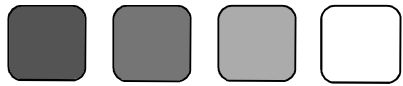
Drawbacks of Will Substitutes

- Each of these options has potential drawbacks
- e.g.,
 - loss of control over assets during Dick's lifetime
 - tax implications of *inter vivos* trusts
 - cost of additional insurance policy to fund insurance trust (could cash out investments to fund insurance)
- In each case, benefit of protecting assets from claims must be weighed with potential drawbacks, particularly tax implications.



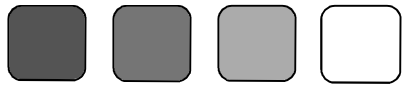
Can creditor protection legislation be used to set aside will substitutes?

- Two cases with different results:
 - *Stone v. Stone*, 55 O.R. (3d) 491 (C.A.)
 - *Mawdsley v. Meshen*, 2012 BCCA 91



Creditor Protection Legislation

- *Statute of Elizabeth* grants a claimant the statutory right to set aside conveyances, including gifts, made with the purpose and intent “to delay, hinder or defraud creditors and others of their just and lawful actions, suits, debts, accounts, damages ... and relief”
- “others” includes those who may become a creditor, although not a creditor at the time of the conveyance
- Jane is not an “other” in this situation
- Statute may not apply to “choses in action”, such as money, investments, stocks, etc.

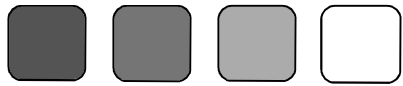


Creditor Protection Legislation, cont'd

Assignments and Preferences Act, s. 4(1):

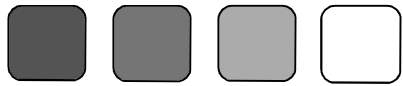
4 (1) Every transfer of property made by an insolvent person

- (a) with intent to defeat, hinder, delay or prejudice his creditors, or any one or more of them; or
- (b) to or for a creditor with intent to give such creditor an unjust preference over other creditors of such insolvent person, or over any one or more of such creditors, shall as against the creditor or creditors injured, delayed, prejudiced or postponed, be utterly void.



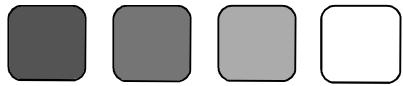
Assignments and Preferences Act, cont'd

- Only gives standing to actual creditors, not “creditors and others”
- Only applies to a debtor who is insolvent at the time of the transfer
- In this case, Dick is not insolvent, so *Assignments and Preferences Act* would not apply in any case



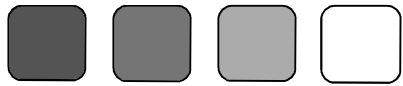
Stone v. Stone

- At issue was whether husband who learned that he was terminally ill was entitled to dispose of his property by *inter vivos* dispositions to his adult children
- Object was to frustrate an application for equalization of his net family property made by his wife upon his death
- ON Court of Appeal held that disposition could be set aside under *Fraudulent Conveyances Act*



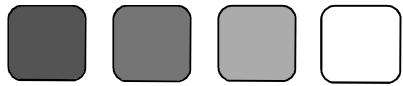
Stone v. Stone, cont'd

- Key was spouse's right to apply for equalization of family property if “there is a serious danger that one spouse may improvidently deplete his or her net family property”
- *Inter vivos* transfer of assets to children was found to be “improvident depletion” of husband's net family property



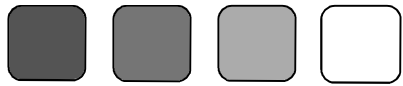
Contrast *Mawdsley v. Meshen*

- Terminally ill testator denuded her estate using *alter ego* trust, *inter vivos* gifts, and joint title
- Value of assets, including family business, exceeded \$10 million
- Testator left nearly everything to her three children (of previous marriages) and brother-in-law who helped to build family business
- Common law spouse of 18 years brought claim under BC *Wills Variation Act*



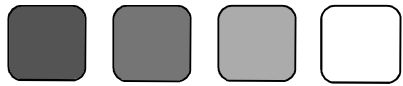
Mawdsley v. Meshen, cont'd

- At issue was whether the provisions of the BC *Fraudulent Conveyance Act* could be used to set aside *inter vivos* dispositions that had effect of defeating or hindering a claim against estate, in this case under the BC *Wills Variation Act*
- Standing to challenge a conveyance under the *Fraudulent Conveyance Act* is limited to “creditors and others” (includes future creditors)



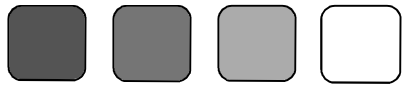
Mawdsley v. Meshen, cont'd

- Question was whether a claimant under *Wills Variation Act* qualified as an “other”
- Court concluded that to have status as an “other” under the *Fraudulent Conveyance Act*, you must have a claim that arises during the lifetime of the debtor, as opposed to one that arises only upon death
- Claim under *Wills Variation Act* only arises on death, so no standing to set aside trust, etc.



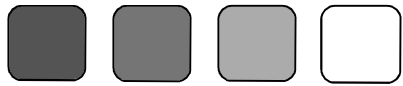
Mawdsley v. Meshen, cont'd

- Evidence at trial was that *inter vivos* dispositions were aimed at avoiding probate tax and protecting children from their own matrimonial claims and spendthrift tendencies, not avoiding obligations to common law spouse
- Court awarded 100% of residue to common law spouse, but residue was less than \$300,000 because of *inter vivos* dispositions (some joint assets ended up in estate because presumption of resulting trust not rebutted)



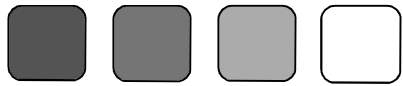
Implications for Nova Scotia

- Ontario *Family Law Act* sufficiently different that *Stone v. Stone* not applicable here
- No equivalent provision in *MPA* that crystallizes claim upon spouse improvidently depleting their net family property
- However, BC legislation similar to NS legislation, and likely same result here as in *Mawdsley v. Meshen* (except no application to common law spouses in NS)



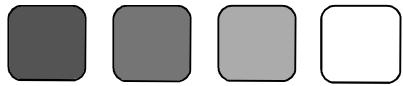
Anti-Avoidance Provisions

- Note that s. 19 of PEI *Dependants of a Deceased Person Relief Act* is an anti-avoidance provision
- It deems the value of certain transactions to be part of deceased's estate



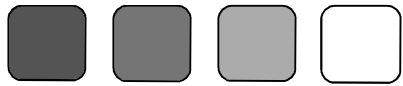
Transactions deemed part of estate under *Dependants of a Deceased Person Relief Act:*

- a) Gifts made in contemplation of death;
- b) Money deposited in trust for another;
- c) Money deposited jointly in the name of the deceased and another and payable on death to the survivor;
- d) Any disposition of property into joint tenancy with right of survivorship;
- e) Any disposition of property in trust, if deceased retained a power of revocation; and
- f) Any amount payable under an insurance policy on the life of the deceased and owned by him



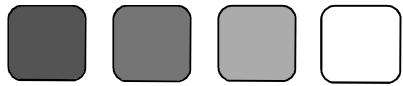
Protecting Assets that Pass by Will

- Include *in terrorem* clause in will to discourage application from Jane
- However, note dubious effect in avoiding *TFMA* applications
- *In terrorem* clause will have no practical effect on Nick and Sally because they aren't immediately beneficiaries if Jane survives Dick
- Recommend Dick sign separate memorandum explaining rationale for unequal division



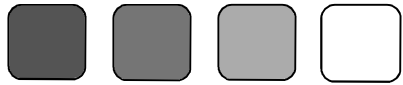
Conclusion

- Asset protection abounds with trade-offs:
 - Protection vs. tax minimization
 - Business debts vs. matrimonial/family claims
- Cost of sophisticated planning structures to protect assets may not always be warranted given likelihood of a claim.
- But exclusive focus on tax planning can leave estate exposed to creditors and claimants.

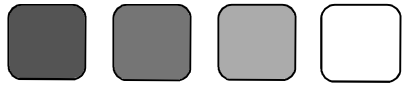


Conclusion, cont'd

- Advisors must use the various tools that are available to maximize benefits and minimize risks.
- The goal is to create a customized plan that is best for each client's personal circumstances.



Questions?



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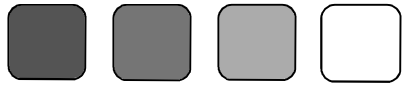
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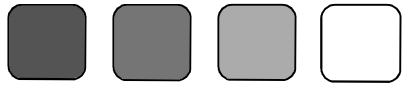
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