The Private Wealth & Private Client Review

Fourth Edition

Editor
John Riches

Law Business Research

The Private Wealth & Private Client Review

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For further information please email
Nick.Barette@lbresearch.com

The Private Wealth & Private Client Review

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Editor
John Riches

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PUBLISHER
Gideon Roberton

SENIOR BUSINESS DEVELOPMENT MANAGER
Nick Barette

SENIOR ACCOUNT MANAGERS
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EDITOR'S PREFACE

There is no doubt that the twin recurring themes for 2015 at a global level in private wealth planning are those of transparency and regulation. The zeal of policy makers in imposing ever more complex and potentially confusing sets of rules on disclosure of beneficial ownership information seems unabated.

i Common reporting standard (CRS)

The centrepiece of cross-border automatic information exchange is CRS. This FATCA equivalent for the rest of the developed world is set to come into effect from 1 January 2016. At the last count just over 90 countries had committed to CRS. Its principal effects will be felt in two waves – among the so-called early adopters group the rules will take effect from 1 January 2016 and first information exchanges will apply in September 2017. For the second wave, there will be a year's delay.

What is interesting about CRS is that the OECD has taken a central role in producing coordinated guidance on its interpretation. The draft guidance initially published in July 2014 was somewhat sketchy in nature and we can expect, as we move towards the beginning of next year, revised and more detailed guidance on a number of key issues.

Deep concerns exist about the extent to which information exchange between tax authorities under CRS will remain secure in the hands of the 'home' countries of beneficial owners. While the 'normal' way of signing up to CRS is via the multilateral convention that provides for exchange with other signatory nations, there are indications that some jurisdictions (at this stage the Bahamas, Hong Kong and possibly Switzerland) may seek to adopt a more 'bilateral' approach implementing CRS. If this approach becomes more widespread, then the practical implementation of CRS could be significantly delayed by jurisdictions who negotiate treaties on a one-by-one basis with 90 other countries.

While CRS is often compared to FATCA, there are some material differences that emerge from closer scrutiny. Whatever the shortcomings of FATCA, the ability to issue a global intermediary identification number and to sponsor entities on a cross-

border basis somewhat lessens the bureaucratic excesses of its impact. What is distinctly unclear about CRS at this point is whether equivalent mechanics will emerge. As CRS is currently written as a series of bilateral treaties between jurisdictions with no domestic law 'anchor' (as is the case with FATCA) concerns are being expressed about the potential duplication for complex cross-border structures of reporting. In this context, the July 2014 introduction to CRS notes that the rules as to where a financial institution (FI) will be deemed resident differs between jurisdictions – in some cases this will be based on the place of incorporation whilst in others it may be based on the place of effective management.

There are concerns as to how non-financial entities (NFEs) will be dealt with under CRS. There is anecdotal evidence emerging already in the context of FATCA that financial institutions, driven by concerns about fines from regulators for NFEs and the related ownership structure are subjecting bank account applications for NFEs to additional enquiries that generate very significant costs and delay.

It is noteworthy that there has been a significant crossover from the anti-money laundering (AML) or terrorist financing regime coordinated by the Financial Action Task Force (FATF). This is expressly provided in the CRS model treaty that imports into CRS the FATF concept of beneficial ownership. In the CRS world, this is known as 'controlling persons'. By expressly linking the definition of controlling persons to that of beneficial ownership employed for FATF purposes, there is the prospect of the beneficial ownership definition evolving over time in accordance with principles adopted in that domain. It is noteworthy that, as well as looking to ultimate legal and beneficial ownership of an entity, these definitions also look to the capacity to exert influence and control in the absence of any formal legal entitlement. Thus the expanded definition is as follows.

Beneficial owner refers to the natural person who ultimately owns or controls a customer or the natural person on whose behalf a transaction is being conducted. It also includes those persons who exercise ultimate effective control over a legal person or arrangement.[1]

It is completely appreciated that, in a law enforcement context, criminals and terrorists do not typically advertise their involvement in ownership structures where they are liable to be detected by the appropriate agencies. Transporting this definition wholesale, however, into the world of tax information exchange where domestic tax authorities may draw unfair and adverse implications from an attribution of being a 'controlling person' is more questionable. It is not a complete response to this concern to say, in the final analysis, if someone has no ability to enjoy the benefit of assets held within a particular structure that they can demonstrate this – the potential costs and bureaucracy of an unwarranted tax audit that may arise from such a misunderstanding will be more difficult to quantify.

Another area of concern is the capacity for banks who have, in the past, misclassified or misunderstood information about ownership structures. If this information is simply

1 http://www.fatf-gafi.org/pages/glossary/a-c/ – The Recommendations were adopted by FATF on 16 February 2012. (emphasis added).

'copied over' from AML records for CRS purposes then there is scope for false and misleading information to be exchanged in circumstances where the 'beneficial owners' may be completely unaware of such mistakes or misclassifications.

What follows from this is an increased importance for professional advisers to actively engage with clients to discuss the implications of these changes. Taken together, the combined impact of these changes is likely to be seen in years to come as a 'paradigm shift' in international wealth structuring. It is therefore critically important that the advisory community equips itself fully to be able to assist in a pro-active manner.

ii Public registers of beneficial ownership

On 20 May 2015, the EU published the final version of its fourth anti-money laundering directive (4AMLD). This commits the EU Member States to providing a public register of beneficial ownership within the next two years. What is noteworthy about the terms of the regulation is the fundamental distinction that has been drawn between ownership information about 'legal persons' (including companies and foundations) on the one hand, and 'legal arrangements' (including trusts) on the other. There is an obligation for information on legal persons to be placed in the public domain while information relating to trusts and equivalent arrangements will be restricted so that it is only made available to competent authorities.

The acceptance in the drafting of these regulations that there is a legitimate distinction to be drawn between commercial entities that interact with third parties, primarily in the context of business arrangements, and private asset ownership structures that are primarily designed to hold wealth for families is an encouraging one.

It should not, however, be assumed that the emphasis on privacy that underpinned this particular distinction will necessarily be a permanent one. There is a very strong constituency within the EU that still argues that a public register of trusts should be introduced at some stage in the future.

Turning to the UK, 2016 will see the introduction of a public register of beneficial ownership for companies in the UK. This legislation, to a large extent, anticipates the impact of 4AMLD although it is not completely symmetrical. The centrepiece of UK domestic legislation is the public identification of persons with influence over UK companies, known as 'persons exercising significant control' (PSCs). There are significant penalties for non-compliance. In particular, in circumstances where a PSC does not respond to the request for information from a company, not only can that refusal generate potentially criminal sanctions, it can also result in any economic benefits deriving from the shares as well as the ability to vote being suspended.

While it is appreciated that there are reasons why sanctions need to be applied to encourage people to comply, the harsh economic penalties may be seen as totally disproportionate to non-compliance. It is interesting to note that the PSC concept analogous to that of the 'controlling persons' in the context of CRS. As with CRS, the most complex area here is the extent to which those being seen to exert 'influence' without formal legal entitlement may be classified as PSCs.

One further interesting issue that needs to be considered as matters move forward is whether the impact of the EU public register for corporate entities will result in a 'back door' trust register in many cases. One of the categories for disclosure of PSCs in

the UK register is 'ownership or influence via a trust'. In circumstances therefore where a trust holds a material interest in a company, this can result in not only the trustees and protectors of the trust, but also family members with important powers (such as hire and fire powers) being classified as PSCs and having their information placed on a public register. While this register will not give direct information about beneficiaries as such, in many cases it will provide a significant degree of transparency about family involvement. It seems likely that, over time, the EU will also look to 'export' a requirement for beneficial ownership information on public registered companies to be incorporated in many of the international finance centres. While IFCs have indicated that they are sceptical about the adoption of such registers in circumstances where there is not a common standard applied to all jurisdictions, it remains to be seen how long this stance can be maintained once 4AMLD is in full force.

iii Position of the United States

The United States stands out as having secured a position for itself in the context of cross-border disclosure that many feel is hypocritical. Specifically there is a carve out from CRS on the basis that the US has implemented FATCA. The constitutional position in the US where measures of this nature would tend to be introduced at a state rather than federal level also complicates the picture. In the absence of any comprehensive regime to regulate trustee and corporate service providers, the US appears to have achieved a competitive advantage in administering 'offshore' structures because it has exempted itself, in practical terms, from reciprocation on automatic information exchange. This is already leading to many considering the US as an alternative base from which to administer family structures in a more 'private' setting than is possible in IFCs once CRS take effect.

iv Global legal entity identifier system (GLEIs)[2]

A development flowing from the 2008 financial crisis is the introduction of GLEIs. In December 2014 a regulatory oversight committee relating to GLEIs introduced a task force to develop a proposal for collecting GLEIs information on the direct and ultimate parents of legal entities. The policy is to ensure financial intermediaries can track who they are dealing with as counterparties in investment transactions. The underlying policy that drives the creation of the GLEIs is to create transparency in financial markets. In the current phase 1 of the project, the information required to be collected is limited to 'business card information' about the entities concerned and will therefore be limited to a name, address and contact number. However, the 'level 2' data that is likely to be required will extend the reference data to relationships between entities. This could result in beneficial ownership information being required in due course. This proposal is likely to see some development in the course of the next six months but is yet another illustration of overlapping regimes for collecting beneficial ownership information that are likely to have a substantial effect on the operation of family wealth holding structures in the years ahead.

2 http://www.leiroc.org/.

v Conclusion

The challenges of keeping abreast of changes in the regulatory and transparency arena are significant. These issues look set to be a significant driver in wealth strategy in the next three to five years. Navigating these issues will increasingly become a required skill set for professional advisers.

John Riches
RMW Law LLP
London
September 2015

Chapter 12

CANADA

Margaret R O'Sullivan, Jenny K Hughes and Christopher Kostoff[1]

I INTRODUCTION

i Canadian wealth – skating on thin ice: collapsing oil prices deliver a seismic shock to the Canadian economy

Everything seemed to be on course for 2015 – Canada's stable financial system helped secure Canada's emergence from the 2008 global financial crisis in relatively good shape. But storm clouds remained: continuing low interest rates fuelling an impending housing bubble continued. And then the dramatic fall in 2015 of world oil prices exposed the fragility of the Canadian resource-based petro-economy, leaving it vulnerable to a return to recession. Although ultimately in the longer term cheaper oil and a cheaper Canadian dollar will help the Canadian manufacturing sector, there will be short-term pain for long-term gain as the economy readjusts.

On the wealth management side, an increasingly ageing Canadian demographic is beginning to result in a rising tide of legislative changes at both the federal and provincial levels, which affect private client work in all spheres, as highlighted below. In addition, wealth management and private client work is gaining currency as a growth area for financial institutions and the general wealth planning community.

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

1 Margaret R O'Sullivan is principal, Jenny K Hughes is a legal administrator and researcher and Christopher Kostoff is an associate lawyer at O'Sullivan Estate Lawyers Professional Corporation. The authors would like to thank Claudia A Sgro, formerly of O'Sullivan Estate Lawyers Professional Corporation, for her past assistance with this chapter.

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.

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 50 per cent in combined federal and provincial rates on taxable income above C$136,000 in a taxation year, less applicable tax credits. Surtaxes of a province can result in elevated effective tax rates.

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 2015, 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$813,600 in 2015) 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 2015 range from 39 per cent in Alberta to 55 per cent in New Brunswick. The highest tax rates in Ontario and British Columbia are 50 per cent and 46 per cent, respectively. Recently, Alberta introduced graduated tax rates for taxpayers with income over C$120,000. 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 tax rate for Albertans will be 44 per cent.

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. Following a public consultation, the federal government in the 2014 federal budget announced its intention to eliminate the graduated rates applicable to certain trusts and estates. Commencing in 2016, the top federal marginal rate will be applied to testamentary trusts and to estates after a reasonable period of administration of 36 months. Notwithstanding the changes, the 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. Also, the new legislation will change administrative requirements, including legislating a calendar year end for testamentary trusts commencing in 2016, or for existing testamentary trusts on 31 December 2015, and testamentary trusts will no longer be exempt from the general requirement to make instalment payments of income tax and will lose access to certain other exemptions.

Taxation of life interest trusts

In draft legislation released in 2014, which has now been enacted, and which has caused concern in the professional estate planning community, the federal government proposed changes to the taxation of certain life interest trusts, such as 'alter ego trusts' and 'spouse trusts', on the death of the life interest. A transfer of property to such trusts generally does not result in any taxation. Instead, under the current rules, on the death of the life interest, the trust is deemed to have disposed of all of its capital property for fair market value and any resulting capital gains are taxed in the trust. Commencing in 2016, under the new rules, the estate of the deceased life interest will be primarily liable for any taxes owing on the deemed disposition. This may result in an issue where, for example, the beneficiaries of the relevant estate and trust differ. If the estate of the deceased life interest is unable to pay the taxes owing on death, the trust will then be required to pay any unpaid taxes.

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.

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 giving rise to the tax benefit was an 'avoidance transaction' (or series of transactions) 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 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

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

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 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.

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.

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, will be 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 2015, *Bloomberg Markets* magazine ranked two Canadian banks (Canadian Imperial Bank of Commerce and Desjardins Group) among the world's top 20 strongest banks with US$100 billion or more of assets. 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 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 25 per cent and 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 11 per cent to 16 per cent in the provinces, except Quebec, on the first C$425,000 to C$500,000 of active business income. A small business corporation includes a Canadian-controlled private corporation with capital under C$10 million carrying on active businesses in Canada. 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, as are certain qualified farm and fishing properties.

Investment income earned in a corporation is taxed at approximately the highest personal income tax rate (39 to 55 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. An amendment has been made to the gross-up and dividend tax credit mechanism such that dividends paid by a small business corporation (in respect of income taxed at the small business tax rate) will be grossed up by 18 per cent and the dividend tax credit will be 13/18 of the gross-up amount, which will now only partly compensate for the corporate tax paid. The 2015 federal budget announced that such dividends will effectively be taxed at slightly higher rates in 2016.

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.

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 laws 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.

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 dividing the estate between spouse and children. In this context, spouses are married spouses, including same-sex married spouses and, in some provinces and the 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.

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. 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.

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, Prince Edward Island and the Yukon, death does not trigger a statutory property claim for the surviving spouse. This is generally also the case in Alberta for the time being; however, under pending amendments to the Matrimonial Property Act death will be a triggering event for a marital property claim, but only for legally married spouses. 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

Alberta's Wills and Succession Act and Estate Administration Act

Two western provinces – Alberta and British Columbia – recently updated their succession law statutes. Alberta's Wills and Succession Act modernises succession law in that province and consolidates and harmonises the operation of five statutes. Highlights include the court's ability to rectify a will or purported will by adding or deleting text and admit extrinsic evidence for will interpretation. On intestacy, if the deceased's descendants are also those of the surviving spouse, the deceased's estate in its entirety will go to the spouse. Children who are full-time students aged 18 to 22 as well as minor grandchildren may be family members eligible for support. The testator's subsequent marriage or entrance into an adult interdependent partnership agreement does not revoke a pre-existing will; however, a gift in a will to a separated spouse may be invalid. Survivorship rules are modernised and certain common-law presumptions abolished.

Alberta's new Estate Administration Act came into force on 1 June 2015. The new Act is meant to make the administration of estates by estate representatives in that province more streamlined and user-friendly, as well as help them to better understand the process and their role. In addition to providing clearer rules on certain administration matters, the Act also codifies certain processes and procedures that were already in

place. In particular, the Act stipulates, among other matters, the specific core duties, tasks and liability of personal representatives who apply for probate, and the same for personal representatives who do not apply (which, for the latter, includes rules regarding providing notice and other required information to beneficiaries). The Act also codifies rules regarding the ranking and apportionment of debts and a personal representative's standard of care.

British Columbia's consolidated Wills, Estates and Succession Act

British Columbia's Wills, Estates and Succession Act came into force on 31 March 2014 and represents a significant updating, consolidation and harmonisation of that province's succession laws by repealing and replacing four statutes. It includes as a spouse a *de facto* spouse who has cohabited with the deceased for two years. Property division on intestacy is updated including in respect of the share to the surviving spouse. The Act modernises survivorship rules and adds a five-day survival provision failing which certain deeming provisions apply. It permits the court to rectify wills and cure deficiencies, including orders for the validity of documents that do not meet statutory formality requirements based on substantial compliance considerations. Under the Act, a will is not presumed to be revoked by marriage or a change in circumstances. The Act provides a reverse onus for allegations of undue influence in certain circumstances, and new procedures apply to the administration of small estates under C$50,000.

With respect to the definition of spouse,[3] the British Columbia Supreme Court released its first judicial consideration of the term under the Act in *Re Richardson*[4] – a case involving an application by a surviving partner to be declared a spouse when her partner died intestate and essentially confirm her status as the beneficiary of the estate. The decision is significant as the two persons found to be spouses lived in different municipalities during their entire relationship. While a shared residence is one of the factors a BC court will consider, it is not the only factor for determining spousal status. While the case does not represent a significant change in BC's law, it does continue case law under earlier legislation holding that cohabitation of unmarried partners is not determinative of their relationship status.

Increased Ontario compliance to probate a will

In Ontario, legislative measures enacted under the Estate Administration Tax Act in 2012 came into force on 1 January 2015 with little forewarning, together with a new regulation under the Act. 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, complete and file an estate information return with the Ministry of Finance within 90 calendar days of the court issuing the certificate of appointment. Most significantly,

3 Two persons are defined as spouses of each other if 'they were both alive immediately before the relevant time and (a) they were married to each other, or (b) they had lived with each other in a marriage-like relationship for at least 2 years'.

4 *Re Richardson*, 2014 BCSC 2162.

the return (a prescribed form 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. 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.

Nova Scotia probate taxes, abolishment of rules against perpetuities and updated Variation of Trusts Act

While Ontario previously had the highest provincial probate tax rate at approximately 1.5 per cent, Nova Scotia's has surpassed Ontario's in recent years, with a current rate of approximately 1.645 per cent on a large estate, as of April 2013. This represents an increase of over 30 per cent since 2000 on a C$5 million estate, and is significantly greater than equivalent fees in other Atlantic provinces.

Nova Scotia's new Perpetuities Act came into force in July 2013 and for the most part abolished the rules against perpetuities in that province retroactively, with few exceptions. This change brings the number of provinces to three – Manitoba and Saskatchewan included – in which rules against perpetuities have been abolished entirely. Simultaneously, the Nova Scotia legislature updated the Variation of Trusts Act to expand the court's authority to maintain, vary or terminate trusts in light of certain considerations. Previously, a court had no power to vary or terminate trusts if an adult capable beneficiary objected.

Uniform Trustee Act

In August 2012, the Uniform Law Conference of Canada approved the Uniform Trustee Act. The Act is meant to serve as a model to the provinces and territories for the purpose of modernising trust law, as well as to some extent harmonising it across Canada. It would reform both the common law and statutory rules relating to a variety of matters, including the duties and powers of trustees, as well as trustee remuneration and the variation, termination and resettlement of trusts. Except for certain mandatory provisions considered essential to the operation of trusts, a trust deed may exclude and override the operation of the Act's provisions, which function as default rules when the trust deed is silent. Each province and territory must now consider adopting and implementing the Act. In 2014, British Columbia's Ministry of Justice undertook a public consultation on the Act as a basis for new legislation in that province.

Gifts in wills altered for public policy reasons

There has been recent Canadian case law (one decision from New Brunswick and another from an Ontario court) in which gifts in wills have been altered for public policy reasons. The New Brunswick decision of *McCorkill v. Streed*[5] had the effect of striking

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

an unconditional bequest to a racist corporation on the basis of public policy. In the Ontario decision of *Spence v. BMO Trust Co*,[6] the 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. Both cases are currently under appeal.

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$5.43 million for 2015) 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.

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. 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

6 *Spence v. BMO Trust Co.*, 2015 ONSC 615.

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.

It is unclear exactly what obligations trusts with Canadian resident trustees will have under FATCA and the IGA if it applies. It seems clear that certain trusts may be considered foreign financial institutions under FATCA. Other trusts may be considered passive non-financial foreign entities and the trustees are required to report information about US interest holders. Alternately, certain trusts are considered by US law to be owned by the settlor. It is unclear what effect, if any, the IGA will have on the reporting and compliance requirements for trusts including those considered foreign financial institutions under FATCA, since Canada's IGA, unlike the United Kingdom's, does not expressly address trusts.

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.

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.

Uniform Substitute Decision-Making Legislation

The Uniform Law Conference of Canada (ULCC) is working towards the adoption of the Recognition of Substitute Decision-Making Documents Act (Uniform Act). 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. Once adopted by the ULCC, it will be 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: (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 are now available to same-sex married spouses, 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.

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*,[7] 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 2011, with the national average being 16.7 per cent) and there are few legal rights provided to these spouses on relationship breakdown.[8] 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*

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

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

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*,[9] 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[10] and Alberta,[11] with no helpful valuation analyses having been reported to date.

9 [2011] SCJ No. 10.

10 *Grosse v. Grosse*, 2012 SKQB 464 (CanLII).

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

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

In two companion cases, *Pecore v. Pecore*[12] and *Madsen Estate v. Saylor*,[13] 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*,[14] a Saskatchewan court recently 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 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.

Two recent 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.[15] In *Mroz v. Mroz*[16] 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.

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12 *Pecore v. Pecore*, 2007 SCC 17.

13 *Madsen Estate v. Saylor*, 2007 SCC 18.

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

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

16 *Mroz v. Mroz*, 2015 ONCA 171.

Exempting matrimonial property from the equalisation regime

The recent Ontario Court of Appeal decision in *Spencer v. Riesberry*[17] 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.[18] 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 a 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 so-called 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 involving a horse farm 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.[19]

IV WEALTH STRUCTURING AND REGULATION

i Common vehicles for wealth structuring

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

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

17 *Spencer v. Riesberry*, 2012 ONCA 418.

18 *Clarke v. Johnson*, 2014 ONCA 237 and *Love v. Schumacher Estate*, 2014 ONSC 4080.

19 *Sabey v. Rommel*, 2014 BCCA 360.

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, and 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 marginal rate applicable to individuals. At the time of writing, use of one or more testamentary trusts under a will can allow for income splitting between the trust and one or more beneficiaries resulting in significant tax savings. However, commencing in 2016, a testamentary trust will be taxed at the top marginal tax rate, but with the exception that graduated rates will continue to apply to the estate for 36 months and to certain testamentary trusts with disabled beneficiaries. These changes will eliminate certain tax benefits of income splitting with testamentary trusts, but it will still be possible to 'sprinkle' income among a group of beneficiaries of a discretionary 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 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 also are 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 companies' 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 Financial Transactions and Report Analysis Centre of Canada (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.

V CONCLUSIONS AND OUTLOOK

The aftershock of the direct hit to the Canadian petro-economy of a plunge in world oil prices is only beginning to reverberate and the true fall-out remains to be seen.

No doubt, we are in very unusual times. Interest rates at the time of writing are now forecast to go even lower, raising the spectre of deflation on the one hand. But at the other extreme are housing prices in some Canadian centres including Vancouver and Toronto, fuelled by low interest rates, which are going only higher. And we now seem on the verge of another recession, with forecasts for GDP growth lowered.

Yes, it is true that Canadians are known to be excellent ice skaters – but the ice we are now skating on is black ice and one false move poses high risk and imminent danger.

Meanwhile, new legislative measures continue to curtail tax minimisation strategies and impose an increasing burden of greater compliance, including the elimination of the preferential tax treatment of testamentary trusts to come into effect in 2016, one of the most significant changes to Canadian estate planning in the past several decades.

Appendix 1

ABOUT THE AUTHORS

MARGARET R O'SULLIVAN

O'Sullivan Estate Lawyers Professional Corporation

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 member of council, Ontario Bar Association (1993–1998). 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 2015* (Global Legal Group 2014). She was called to the Ontario Bar in 1983.

JENNY K HUGHES

O'Sullivan Estate Lawyers Professional Corporation

Jenny performs a broad range of roles, including office management and administration, legal research and writing, document preparation, as well as marketing and social media coordination. Since 2004, she has worked solely in the areas of trusts and estates, both as a law clerk and lawyer. Jenny was called to the Ontario Bar in 2004.

CHRISTOPHER KOSTOFF

O'Sullivan Estate Lawyers Professional Corporation

Christopher practices in the areas of estate planning, administration and litigation including will, trust and incapacity planning, advice to executors and trustees, and estate litigation and alternative dispute resolution. He was called to the Bar of Ontario in 2011. Prior to joining O'Sullivan Estate Lawyers, Christopher was an associate at a tax boutique where he had a broad tax planning and dispute resolution practice. He has co-authored articles on the topic of the taxation of partnerships for the Law Society of Upper Canada and the Ontario Tax Conference.

O'SULLIVAN ESTATE LAWYERS PROFESSIONAL CORPORATION

Toronto-Dominion Centre
TD Bank Tower
66 Wellington Street West, Suite 3430
PO Box 68
Toronto
Ontario M5K 1E7
Canada
Tel: +1 416 363 3700
Fax: +1 416 363 9570
mosullivan@osullivanlaw.com
www.osullivanlaw.com