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The International Comparative Legal Guide to:

Private Client 2017

6th Edition

A practical cross-border insight into private client work

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EDITORIAL

Welcome to the sixth edition of *The International Comparative Legal Guide to: Private Client.*

This guide provides corporate counsel and international practitioners with a comprehensive worldwide legal analysis of the laws and regulations of private client work.

It is divided into two main sections:

Nine general chapters. These are designed to provide readers with a comprehensive overview of key issues affecting private client work, particularly from the perspective of a multi-jurisdictional transaction.

Country question and answer chapters. These provide a broad overview of common issues in private client laws and regulations in 28 jurisdictions.

All chapters are written by leading private client lawyers and industry specialists and we are extremely grateful for their excellent contributions.

Special thanks are reserved for the contributing editors Jonathan Conder and Robin Vos of Macfarlanes LLP for their invaluable assistance.

Global Legal Group hopes that you find this guide practical and interesting.

The *International Comparative Legal Guide* series is also available online at www.iclg.co.uk.

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Special Issues Arising for Estates with Foreign Beneficiaries or Legal Representatives

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Where an estate has foreign beneficiaries or legal representatives, a multitude of special considerations and issues arise. This article highlights a number of them and is written from the perspective of Canadian and Ontario law; however, similar considerations and issues can arise in many jurisdictions, in particular common law jurisdictions.

Foreign Beneficiaries

Various tax and non-tax-related issues arise during the administration of an estate which has foreign beneficiaries, including:

- withholding tax on payments made to a foreign beneficiary;
- the characterisation of distributions made to non-resident beneficiaries, including whether capital distributions can be made tax-free to a non-resident beneficiary or are subject to tax on capital gains;
- requirements to obtain a certificate from taxing authorities prior to making distributions to a non-resident beneficiary;
- multiple taxation on death;
- foreign currency and exchange;
- transfers of interests in domestic corporations; and
- payment of a deceased beneficiary's share to a non-resident legal representative.

(a) Withholding Tax Issues

By way of example, in Canada, income which is paid or payable to a non-resident beneficiary does not generally retain its character in the hands of the non-resident beneficiary and is subject to non-resident withholding tax. The trust is liable to withhold the appropriate rate of tax of 25% (unless reduced by treaty). This tax has to be received by Canada Revenue Agency (CRA) or by a Canadian financial institution on or before the 15th day of the month following the month during which the tax was withheld. The trustee must complete an NR4B Summary and Supplementary Slips reporting the income paid or credited to non-resident beneficiaries and remit the tax withheld. Withholding tax on interest income paid to non-residents was eliminated as of January 1 2008.

(b) No Rollover

Under Canadian tax rules, there is generally no rollover on a distribution of capital property by a trust to a non-resident beneficiary in satisfaction of all or any part of a capital interest. The trust will be deemed to have disposed of the property at proceeds equal to fair market value and the beneficiary acquires the property at that amount. The beneficiary is deemed to have disposed of the capital interest for proceeds equal to its cost amount. A rollover will apply for a distribution of certain types of property including real property situated in Canada, property of a business carried on in Canada through a permanent establishment, and shares of a non-resident owned investment corporation. These types of property remain subject to Canadian taxation rules.

(c) Section 116 Certificate Requirements

Section 116 of the *Income Tax Act* (Canada) (ITA) imposes an obligation to obtain a clearance certificate on a non-resident person who disposes of certain taxable Canadian property.

The obligation will apply to a non-resident with respect to a disposition of a capital interest in a trust that occurs because of a distribution of capital by the trust to the non-resident, but with the exception of a cash distribution, unless more than 50% of the fair market value of the estate is derived from Canadian real property.

Under Section 116, the estate is considered a "purchaser" of taxable Canadian property – i.e., the capital interest in the estate – and the non-resident beneficiary is considered the vendor.

If a non-resident beneficiary does not obtain a clearance certificate, the estate must withhold and remit tax equal to 25% of the deemed proceeds to CRA, as well as report the distribution to CRA within 10 days of making the distribution and within 30 days after the end of the month in which the distribution is made. Failure to do so could result in personal liability to the estate trustees for any unpaid tax. No withholding is necessary in certain situations where the vendor and purchaser are related and certain other provisions are met.

(d) Multiple Taxation on Death

Generally, tax on assets which pass on death may be levied on the estate (or the deceased) or, less commonly, on the beneficiary, on various bases relating to personal characteristics of the deceased or beneficiary such as: citizenship; domicile and residency; and including where a person has recently ceased physical residency in a jurisdiction but maintains tax residency. Furthermore, tax may be levied on the basis of the location of the inherited assets.

Most jurisdictions impose some type of death, succession, or estate tax. In a small number of jurisdictions (including Canada, Australia, New Zealand, and Denmark), capital gains tax applies to the gain in the value of the deceased's property arising on death which may take the place of estate or inheritance tax in that jurisdiction. In such jurisdictions, it may in certain circumstances be possible to effectively defer realisation of capital gains until disposition of the assets by the heirs or beneficiaries.

The possibility for double or even triple taxation arises in various situations, including taxation by multiple jurisdictions, and/or in the hands of different taxpayers. Few double taxation treaties provide for relief against double taxation with respect to gift or inheritance taxes, although unilateral measures may take such double taxation into consideration. From a Canadian perspective, a notable exception is the tax treaty between Canada and the United States: *Convention between Canada and the United States of America with respect to Taxes on Income and on Capital* and the treaty between Canada and France: *Convention Between Canada and France for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and on Capital*. However, even where provisions for relief against double taxation have been made, the situation may be complicated where the identities of the taxpayers and/or the timing of the tax liabilities differ as between jurisdictions.

It will be of increasing importance to understand the impact foreign taxes can have on the administration of an estate, even one which is purely domestic, but may have foreign beneficiaries. In this regard, certain countries impose inheritance taxes whereby the heirs or beneficiaries pay tax based on the value of their inheritance, including the following: Croatia, the Czech Republic, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Japan, Korea, Luxembourg, the Netherlands, Norway, Poland, Serbia, Spain, Switzerland (most cantons), and Venezuela.[1] Most wills have a debts and death taxes clause which provides that all taxes arising as a result of death are paid by the estate so that all beneficiaries are treated equally, notwithstanding local taxation. In certain jurisdictions, inheritance tax rates are high and may produce an unintended result. It will be increasingly important, in particular where a beneficiary resides in a jurisdiction which has a significant inheritance tax, to seek the testator's instructions with regard to whether the estate or the beneficiary should bear the burden of the inheritance tax.

(e) Foreign Currency Issues

It is important to consider foreign currency and exchange issues in making distributions to non-resident beneficiaries.

Consider seeking instruction from beneficiaries regarding denomination of currency, wiring of funds (and the expense of this), in which jurisdiction the best foreign exchange may be obtained, any problems in negotiating cheques including delays, etc. prior to effecting distributions.

(f) Interest in a Domestic Corporation

Problematic issues may arise where a foreign beneficiary holds an interest in a domestic private corporation, in particular under the beneficiary's domestic tax laws. For example: a U.S. resident may be exposed to double taxation on earnings of the corporation due to a mismatch of foreign tax credits and be subject to certain filing requirements. Additionally, the U.S. resident may be subject to the controlled foreign corporation and passive foreign investment company rules, which can be punitive.

One must also consider whether the domestic private corporation is subject to favourable tax treatment, which it could lose if it loses its status because of a change of tax residence of the estate that controls the corporation. For example, in Canada, a Canadian-controlled private corporation has various favourable tax advantages and treatment.

(g) Payment of a Deceased Person's Share under an Estate to a Non-Resident Legal Representative

Where an estate beneficiary is deceased and his or her legal representative is a non-resident, one must consider what authority the non-resident legal representative has to receive estate monies on behalf of the deceased beneficiary. A prudent solicitor will request a copy of the deceased's death certificate, and a copy of the document under which such legal representative claims to have authority to receive assets on behalf of the deceased beneficiary, either by way of statute, court order or other document. If there is any question as to the non-resident person's authority, one should consider obtaining either a legal opinion and/or a court order or payment of the funds into court.

Non-Resident Legal Representatives

There are a number of tax and non-tax-related considerations that may arise when an estate has foreign legal representatives.

(a) Tax Reporting and Disclosure Obligations

It is important to consider tax reporting duties and disclosure requirements of executors and trustees. Generally, executors and trustees are responsible for the payment of taxes from the estate and related compliance, including with respect to the deceased's income taxes, including relating to prior years insofar as such obligations are proper (enforceable) debts of the estate.

Reporting duties and disclosure requirements to the taxing authorities of a foreign jurisdiction typically arise pursuant to an enforceable obligation on the executors and/or trustees in the home jurisdiction to pay tax to the relevant foreign jurisdiction. In common law jurisdictions, there has historically been the "revenue rule" under which the courts have refused to enforce revenue judgments arising pursuant to the law of other sovereign states, either directly or indirectly, subject to exceptions under applicable tax treaties. Many jurisdictions have increasingly entered into bilateral tax information exchange agreements. Canada and the U.S. have an Intergovernmental Agreement (IGA) to implement the *U.S. Foreign Account Tax Compliance Act*. Under the IGA, information on financial accounts held by U.S. residents and citizens is reported to CRA. CRA exchanges this information with the IRS. As well, under the *Canada – United States Tax Convention*, Canada and the U.S. assist one another in the collection of taxes. *The OECD Convention on Mutual Administrative Assistance in Tax Matters*, which 103 countries have signed and is in force in 89 of those countries as of 26 September 2016, creates enforceable disclosure obligations. The Common Reporting Standard (CRS) was developed by the OECD as the new global standard for exchange of information to better fight tax evasion and improve tax compliance. Under CRS, foreign tax authorities will provide information to domestic tax authorities relating to financial accounts in their jurisdictions held by domestic residents and domestic tax authorities will reciprocally provide the same to foreign tax authorities on domestic accounts held by non-residents in their jurisdictions.

Multiple wills are often used where there are foreign assets which may appoint foreign executors to administer the assets located in the foreign jurisdiction. It is important to ensure that there is effective communication and cooperation among domestic executors and any foreign executors with regard to tax compliance matters.

(b) Tax Residence of the Estate

Each jurisdiction's laws will govern the determination of the tax residence of an estate. While the Canadian *Income Tax Act* does not supply any rules for determining the residence of an estate or a trust, the Canadian Department of Finance has adopted the position that the residence of a trust is a question of fact depending on the

circumstances of each particular case. Consideration should be given to the possible residence of the estate so that tax and estate administration matters may be properly addressed.

An estate is considered a trust under the ITA. The Supreme Court of Canada held in *Fundy Settlement v. Canada*, 2012 SCC 14 that the residence of a trust for Canadian income tax purposes is where the central management and control of the trust actually takes place. The trustee's place of residence will also be the residence of the trust where the trustee carries out such central management and control of the trust, and does this where he or she is resident. According to CRA, where two or more trustees of a trust are active in exercising their powers and fulfilling their responsibilities, the residency of the trust will usually be the place where the trustees, or the majority of the trustees who are exercising the majority of such powers reside, or if one trustee exercises a more substantial portion of the trust's management and control than the others, generally where that trustee resides.

Generally, a Canadian tax resident, including a trust, is liable for Canadian income tax on worldwide income from all sources. A non-resident of Canada is liable for Canadian income tax on Canadian source income and on the disposition of certain property situated in Canada including Canadian real estate. When a Canadian resident transfers funds or property to a non-resident, withholding and reporting obligations can arise.

Section 94 of the ITA prevents the avoidance of Canadian taxes by certain non-resident trusts with Canadian connections by deeming such trusts to be Canadian resident for certain purposes if the trusts have a Canadian resident contributor or a Canadian resident beneficiary. Generally, a resident contributor is a Canadian tax resident who has made a transfer of property to the trust, and a resident beneficiary is a Canadian tax resident who is a beneficiary of a trust to which a Canadian tax resident has contributed. The consequences of having a resident beneficiary or resident contributor include that the trust is generally liable for income tax calculated on the basis that it is Canadian resident and certain filing obligations respecting foreign property. However, for other purposes, the trust is treated as non-resident: for example, in respect of withholding and reporting obligations when a transfer is made to the trust.

If an estate is considered Canadian resident, it is liable for Canadian income tax on its worldwide income from all sources, including tax on capital gains of estate assets since the date of the deceased's death, and for withholding amounts on certain transfers to non-resident beneficiaries. If the estate is considered a non-resident of Canada based on the central management and control test, it is likely that it will be deemed to be Canadian resident by s. 94 of the ITA for many purposes of the ITA, if the deceased was a Canadian resident and the deceased's property was transferred to the estate on the deceased's death. It would calculate taxes generally as though it were Canadian tax resident, although in limited respects it would be treated as non-resident.

The effect of the rules applicable to non-resident trusts on an estate, if applicable, should be limited if the estate is to be distributed outright rather than held in an ongoing testamentary trust.

(c) Bonding Requirements

Many jurisdictions have bonding requirements for foreign executors. Section 6 of Ontario's *Estates Act* generally requires that an executor who lives in a non-Commonwealth jurisdiction post a bond, unless a court under special circumstances dispenses with or reduces the bond. Section 37 of the *Estates Act* states that the bond must be in an amount double the value of the property of the deceased, unless a court under special circumstances dispenses with or reduces the bond.

The general practice is that the bond can be dispensed with or reduced where the proposed non-resident estate trustee provides the court with an affidavit which outlines the "special circumstances" for dispensing with or reducing the bond, along with his or her materials for the probate application. To dispense with the bond, the applicant must prove that that the bond is not required to protect the creditors and beneficiaries of the estate, or that there is an alternate way to protect them. Other relevant factors include the size of the estate and whether the beneficiaries of the estate consent to dispense with the bond.

Dispensing with the bond is usually done, if at all, where all the beneficiaries are adult and mentally capable, and they consent to the order, and where the Court is satisfied that all debts of the estate have been or will be paid.

The court may at any time reduce or increase the amount of the bond on a motion by any person with an interest in the estate. In practice, a bond can be reduced, for example, to protect the interests of a minor beneficiary in a portion of the estate. Dispensing with or reducing a bond is at the discretion of the Court. For example, where the proposed non-resident estate trustee is the sole estate trustee and sole beneficiary of the estate, or where the proposed non-resident estate trustee is the sole estate trustee and the beneficiaries are all adult and *sui juris*, have provided their written consent to both the appointment and dispensing with the bond, and there are no liabilities of the estate, the court will often exercise discretion to dispense with the bond. In a situation where, for example, the proposed non-resident estate trustee is the sole estate trustee and one of two or more beneficiaries, the court will often exercise its discretion to reduce the bond to cover the portion of the estate under administration for the other beneficiary or beneficiaries.

(d) Administrative Efficacy

Where a non-resident executor is named in a will, consideration should be given to whether in addition to bonding issues, it may be more efficient for the estate administration to be carried out by a resident executor, or by having the non-resident executor renounce and allowing any resident executors to act. While it is possible to have a non-resident executor appointed who can settle the estate from abroad by communicating by email, courier and telephone and employing agents for certain tasks, such as filing income tax returns, it may be more expedient, but taking into account all considerations, to have the non-resident executor renounce in favour of a resident executor.

(e) Ancillary and Resealing Grants

Ancillary probate is the name of the process used in many common law jurisdictions by which a non-resident executor who has received probate of a will can have the probate confirmed in another jurisdiction. If a non-resident executor has been appointed as executor by a court outside of a Commonwealth jurisdiction, under the Ontario court rules, in Ontario the non-resident executor may be confirmed as executor by providing, among other documents, two certified copies of the document under the seal of the court that granted it.

A simplified procedure for confirming a foreign grant applies between many Commonwealth jurisdictions called "resealing". Section 52 of Ontario's *Estates Act* provides that a Confirmation by Resealing of Appointment of Estate Trustee With or Without a Will can only occur if the foreign jurisdiction in which the original appointment was made is the U.K., another province or territory of Canada, or a "British possession". Confirmation by resealing gives effect to a foreign grant that provides testamentary authority to an individual. The non-resident executor may be confirmed as executor in Ontario by providing, among other documents, either two certified

copies of the document under the seal of the court that granted it, or the original document and one certified copy of the same.

(f) Need for Ancillary Grants/Resealing

- Bank accounts and insurance proceeds: Where an account is modest, a bank often will generally agree to transfer the funds to the beneficiary without probate if the beneficiary and/or legal representative provides the bank with a waiver and indemnity and affidavit information. However, bank policy may differ where the beneficiary is not in the jurisdiction. For example, in Ontario under banking and insurance legislation, banks and insurance companies may be protected in making payment to a foreign personal representative who does not have an Ontario grant by ancillary appointment or resealing, but they are not compelled to recognise the foreign grant, and may insist on an Ontario grant.
- Real property: In Ontario, real property held in joint tenancy will not require probate in order to update the title registration to the name(s) of the surviving joint owner(s). In a purely domestic situation where the personal representative is in Ontario, if the property was held solely in the name of the deceased, transfer of title will generally require probate, unless the property is registered in the registry system, or if the property was transferred to the land titles system and it is the first transfer after the property was moved from the registry system. Where there is a foreign personal representative, the general principle is that he or she has no authority over the assets of the deceased until he or she received a court grant. Under the land titles system, a transfer of land cannot be made without an Ontario grant.

(g) Foreign Trust Companies

An issue may arise where a foreign trust company is appointed as an executor of an estate. For example, the practice in Ontario is to issue certificates of appointment to trust companies authorised by law to act as estate trustees. Under Ontario's *Loan and Trust Corporation Act*, no incorporated body can undertake or transact the business of a trust company in Ontario unless it is registered under that legislation.

The position prior to a recent court decision in *Herring Estate,* Re (2009), 2009 Carswell 5164, 179 A.C.W.S. (3d) 1233 (Ont. S.C.J.) was that a court will not appoint a foreign trust company as a corporate estate trustee; however, if the foreign trust company has an Ontario affiliate, the Ontario affiliate may be appointed as a corporate estate trustee if registered in Ontario, and that if the foreign trust company has no Ontario affiliate, a trust company which is registered in Ontario may be appointed as corporate estate trustee. The court held that where a testator's will named a foreign trust company as executor and his only asset outside of his home jurisdiction was a Toronto condominium, the trust company would not be transacting the business of a trust corporation in Canada and that by fulfilling its duties under the will it would not be offering its services to the Ontario public. Accordingly, it would not be contravening the *Loan and Trust Corporation Act* (Ontario) and was not disqualified from receiving a certificate of ancillary appointment of estate trustee with a will.

As it may be seen, a host of unique considerations arise where an estate has foreign beneficiaries or foreign legal representatives which often provide challenges and can complicate the administration of an estate. With increasing globalisation, these issues will only arise more frequently in future, and need to be identified and appropriately dealt with through obtaining proper professional legal and tax advice to achieve optimum results and ensure a smooth process.

Endnote

1. See the comprehensive article on multiple taxation on death by Catherine Brown "Death as a Taxable Event – The Problem of Multi-Jurisdictional Estates for Canadians and their Heirs and a Road Map for Assessing Potential Liability", *Estates, Trusts & Pensions Journal*, Vol. 31, 2012 Thomson Reuters Canada Limited.

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