

Advisory

Blended Families: Planning Considerations and Strategies

INTRODUCTION

Canadian census data indicates that blended families are more common than ever, and their numbers are rapidly increasing. It is not unusual for individuals to marry more than once and/or have several common-law relationships. Families with stepchildren are equally prevalent. Separating or divorcing from a spouse does not necessarily sever all financial obligations. Individuals who have children with a new spouse often wish to provide for children from previous relationships.

In this Advisory, we will explore the various issues that can arise for individuals with a blended family. We will discuss the delicate balancing act involved in creating an estate plan that responds to the needs of blended family members, with the ultimate goal of preserving family harmony both before and after death.

WHAT IS A "BLENDED FAMILY?"

A blended family is a family unit where one or both spouses bring children from a previous relationship into a new relationship, creating a combined household. Blended families can take many forms, but the key element is the merging of children and adults from previous family units into a new family unit.

Examples of blended families include: a man with children from a prior relationship marrying a divorced woman and having a child together; or a divorced man and woman entering into a common-law relationship, both with children from a previous marriage.

COMMON ISSUES THAT ARISE FOR BLENDED FAMILIES

a. Unintended Consequences: No Up-To-Date Will and Beneficiary Designations

Without a will, Ontario's intestacy laws are generally not favourable for blended families and can create harsh results. On an intestacy, the estate is divided among the surviving married spouse and children, with the married spouse first receiving a preferential share of \$350,000. If there are no designated beneficiaries for life insurance policies or registered assets, these proceeds become part of the estate and are distributed according to intestacy laws. Common-law spouses and stepchildren do not receive a share under these laws. Separated spouses must meet certain criteria to be disentitled. The default position often does not align with the current family situation.

Individuals usually prepare wills and make beneficiary designations favouring their spouse at the time they prepared or made them but may fail to update these documents after life changes such as separation or divorce. Overlooked updates to an estate plan that does not provide for a current spouse can lead to such spouse making a claim against the estate, delaying its administration, creating family tensions, and sometimes resulting in expensive litigation which depletes the estate.

b. Balancing the Needs of a Current Spouse and Children of a Prior Relationship

If an individual has entered a new relationship and has children from a prior relationship, he or she needs to carefully balance the competing interests involved, particularly in the estate planning context. It would generally be ill-advised to leave the estate entirely to a current spouse trusting that he or she will provide for the deceased spouse's children on the surviving spouse's eventual death. A tailored estate plan is required to ensure that the needs of the current spouse are met while also providing for the succession of capital to the children from a prior relationship.

c. Financial Obligations to a Former Spouse and Children from a Prior Relationship

It is critical to consider pre-existing financial obligations to a former spouse and/or children from a prior relationship that may be binding on the estate. A spouse may be party to a separation agreement stipulating certain obligations, such as payment of a lump sum or periodic payments or designating the former spouse as a life insurance beneficiary. These obligations must be carefully considered when determining the provisions that need to be included under a will and for beneficiary designations. Similarly, if a former spouse or children from a prior relationship qualify as dependants under *Ontario's Succession Law Reform Act* or equivalent legislation in another jurisdiction, they must be adequately provided for to avoid possible claims against the estate. At the same time, the estate plan must

consider the needs of the current spouse and children. This can be a challenge if the estate has limited assets and there is simply not enough to go around.

NAVIGATING THE ABOVE ISSUES

a. Legal Representation: Joint Retainer vs. Individual Retainer

Blended family spouses may feel comfortable jointly engaging a lawyer for their estate planning in order that there is transparency and they jointly create a plan they each can provide input for. However, in other situations, each spouse may prefer to retain their own counsel and, if they wish, share information and details of their planning with each other as needed, particularly on common issues. Whether to have a joint retainer or an individual retainer is an issue that should be carefully considered before embarking on the estate planning journey.

b. Insurance and Registered Plans

Determining who to designate as beneficiaries for insurance policies and registered plans is another challenging issue.

Proceeds from insurance policies and registered plans can be dealt with separately from the estate. The entitlement of the designated beneficiaries does not depend on what is remaining in the estate after paying debts and liabilities and there is clarity on the amount a beneficiary will inherit, as it is not contingent on the terms of the will. In particular, with a life insurance policy, the designated beneficiaries can be certain of the amount they will receive upon the insured's death. Additionally, the designated beneficiaries will have almost immediate access to funds without the need to probate the will through the courts and be subject to possible delays in the administration of the estate. In the usual course, the executor will need to consolidate and liquidate estate assets and pay debts, taxes, and liabilities before making any distributions. As well, under Ontario law, generally the proceeds of a life insurance policy and registered assets for certain family members named as a beneficiary are protected from creditor claims. Life insurance can offer the ability to provide for a second spouse or children from a prior marriage so their interests are separated and not combined under an estate. This severance can often result in more harmony and less potential for a dispute.

There are also tax benefits to designating beneficiaries. Insurance policy proceeds and proceeds of registered plans with a designated beneficiary pass outside of the estate and are not subject to Ontario Estate Administration Tax (currently 1.5% of the value of the estate in excess of \$50,000) ("OEAT"). This can result in significant savings. Also, a life insurance death benefit is typically received tax-free as a receipt of capital. Additionally, registered

assets can be rolled over to a surviving spouse on a tax-deferred basis and taxed only upon the spouse's death.

c. Spouse Trusts

A spouse trust is a structure that typically involves all or a portion of a deceased's estate being held in trust for the spouse's benefit during the spouse's lifetime, but sometimes for a shorter period. The spouse can be a married or common-law spouse.

Under Canadian income tax rules, for the spouse trust to qualify for a rollover of any capital gains arising on the death of the first spouse, the surviving spouse must be entitled to receive all of the income of the spouse trust during his or her lifetime and no one else other than the surviving spouse can be entitled to receive income and capital or benefit from the spouse trust during the spouse's lifetime.

An attractive benefit of a spouse trust is that it can provide for succession of capital on the surviving spouse's death or an earlier termination of the spouse trust, including to the children of the deceased from a prior relationship.

To preserve capital for the beneficiaries who will ultimately receive the remainder of the spouse trust, the spouse trust can be drafted in a way to limit the surviving spouse's right to receive capital. For example, the spouse trust can direct that there be an "even hand" between the surviving spouse and capital beneficiaries so their interests are equally balanced, or that capital can only be paid to the spouse for their medical, health and emergency needs, or can contain a cap on how much capital can be paid each year. A spouse trust can also be created to hold certain special assets, such as the cottage that has been in the family for several generations or shares of a private company so they pass to children from a prior relationship.

An additional benefit of a spouse trust is that it can be structured to provide for multiple trustees to act and where desirable along with the spouse to manage assets to ensure that the value of the trust fund is preserved for the ultimate capital beneficiaries.

d. Mutual Wills

Mutual wills and mirror wills are often conflated but are different. Mirror wills create parallel provisions, usually leaving assets to the survivor with a gift to children upon the surviving spouse's death. The risk is that the surviving spouse may change their will, excluding the deceased's children or other family members from a prior relationship.

In contrast, mutual wills have “mirroring” provisions, but the surviving spouse is under a legal obligation to not change their will due to an agreement not to revoke or vary their wills, except as provided by the agreement. There is a growing body of case law in Ontario that supports mutual wills if a court can determine there was a valid agreement between the spouses.

Mutual wills and a written mutual wills agreement may not suit every situation but they are an option to consider, particularly if the spouses do not wish to include a spouse trust for each other. However, they can limit future planning flexibility. A surviving spouse may remarry and face new obligations, but they are locked into the mutual will agreement. A prudent approach is to allow the surviving spouse to dispose of a certain percentage of the estate freely and without any restrictions.

e. Children From Prior and Current Relationships: Use of a Common Trust to Achieve an Equitable Distribution

If an individual enters into a new partnership and has children with a second spouse and also has children from a prior relationship, all children can be treated as equal beneficiaries if that is the intention. If the children are not close in age, provision can be made for the estate or a portion of the estate to be held in a common trust and amounts paid out of that trust for expenses and maintenance of the children with the final division and distribution from the trust being made once the youngest child attains a certain age. Use of a common trust allows for greater equality and for younger children to be raised using the resources of the common fund, as opposed to having their extraordinary expenses, such as university and college, paid out of their respective share of the estate.

f. Marriage Contracts and Cohabitation Agreements

Individuals entering a second marriage or common-law relationship, particularly when they are more financially established and have accumulated significant wealth, may wish to preserve it for their children and that they not be subject to claims by their spouse arising out of their relationship, including for equalization of family property. Marriage contracts and cohabitation agreements are often used in the estate planning context. For a more detailed review, Advisory, [“Considerations in Using a Domestic Contract”](#) provides an in-depth look.

In Ontario, a marriage contract for married spouses and a cohabitation agreement between common-law spouses gives spouses the ability to agree about the division of property and spousal support on a relationship breakdown including on death. A marriage contract in particular can stipulate that neither party can claim an equalization of property upon death.

As a result, each spouse's expectations are managed, and greater certainty is created in their estate planning.

Courts have the power in certain situations to set aside a marriage contract or cohabitation agreement. It is important that spouses receive independent legal advice and make full and frank disclosure of their financial position to reduce the risk of a contract being set aside.

g. Joint Ownership vs. Tenants in Common

How assets are owned can dramatically affect who ultimately inherits. If assets are owned jointly with right of survivorship, when the first joint owner dies, ownership passes automatically to the surviving joint owner, subject to certain limited exceptions. There is no OEAT payable on such assets because the assets can pass to the surviving joint owner without the need for a probated will. However, in a blended family situation, particularly where a home has significant value, it may not always be desirable to have ownership pass by right of survivorship to the surviving spouse. If there are significant other assets, including insurance, provision can be made in the will that they pass to a spouse trust or possibly directly to the children from a prior relationship. However, if the intention is for *all* assets to be rolled over into a spouse trust so capital gains are deferred and capital preserved for the children, it should be considered that assets owned jointly with right of survivorship will pass outright to the surviving spouse and will not be subject to the spouse trust provisions.

If property is held as tenants-in-common, each owner has a fixed percentage of the asset and can decide how their share should be dealt with upon their death as it will form part of their estate. If spouses choose to own property as tenants-in-common, a sometimes undesirable consequence is that on the first spouse's death, the children from a prior relationship may end up as part-owners of the property with the second spouse. Consideration should be given to having a "buy-sell" agreement to deal with ownership of each party's interest and a process to liquidate it.

CHOOSING ATTORNEYS, EXECUTORS AND TRUSTEES

In a blended family, choosing the right attorneys, executors, and trustees is crucial for a well-crafted estate plan. Tensions can arise when a spouse becomes incapable or passes away, leaving a second spouse, making it essential to appoint one or more persons who can effectively administer and distribute assets.

Appointing individuals with competing interests, such as a surviving spouse and children from a prior relationship, may lead to delays and conflicts. However, appointing only one party can leave others feeling excluded and lacking control over asset management.

It is worth exploring appointing one or more neutral parties such as a trusted friend, professional advisor or trust company, who is sophisticated, financially responsible, has some insight into the family and their needs and importantly, can remain objective. Neutral parties are often a good choice to appoint as trustees of an estate and a spouse trust to act if appropriate with the spouse and help effectively manage and transition the assets to the ultimate beneficiaries upon the death of the surviving spouse.

OPEN COMMUNICATION, EMOTIONAL INTELLIGENCE AND PLANNING ARE KEY TO MINIMIZE CONFLICT

Generally, even the most well-intentioned plan to transfer wealth can be tarnished by poor communication and a lack of transparency. There are many cultural taboos when it comes to speaking about death which can create an additional obstacle. However, sweeping these conversations under the rug is at best inviting confusion about why the estate plan was structured in a certain manner, but at worst, can pave the way for family disharmony and conflict.

a. Family Meetings

Family meetings can be helpful in the blended family context, dependent on the relationship between the children from the prior relationship and the second spouse. If there is the potential for a dispute, a neutral party can help facilitate the discussion. A family meeting is a way to ensure that everyone's expectations are managed, especially as family and financial circumstances change.

b. Letters of Wishes

Letters of wishes are also great tools because an individual can express his or her intentions clearly and can offer the executors, trustees, and beneficiaries a great deal more detail and context than what is included in the will to explain the individual's intentions and motivations and as well provide guidelines behind their estate plan. An additional benefit is that letters of wishes remain private unlike a will, which becomes part of the public record if submitted to the court for probate.

PROBLEMATIC ASSETS

Certain asset classes may require careful consideration and planning to ensure they do not escalate tensions and conflict.

a. Cottages and Other Vacation Homes

Children may feel a strong attachment to the cottage they have used every year and that has been in the family for generations. If it is held jointly with a second spouse and passes by right of survivorship on death, this can cause issues, especially if the second spouse made no financial contribution to the property.

Possible approaches include holding a cottage or other vacation home in a spouse trust, so it eventually passes to the children on termination of the spouse trust.

b. Family Memorabilia

Consideration needs to be made for the division of any personal effects that have sentimental value including family heirlooms, memorabilia, and photographs so that where desired they pass to children from a prior relationship and not automatically to a second spouse as part of a general provision that passes all personal effects to him or her. For example, specific provisions can be included for jewellery that has remained in the family for generations or a coin or hockey card collection that was promised to a child from an early age. Letters of wishes can be valuable tools for expressing how personal effects should be dealt with, however, a specific bequest needs to be included in a will to be legally binding.

c. Business Interests

An individual may want his or her child who has been active in the business to have control and ownership while at the same time ensuring that the other children and surviving spouse receive financial benefits from the business. Absent special planning, including the possible use of a shareholders' agreement, a simple gift of the shares to the spouse and children can result in a multitude of issues, can paralyze decision-making, create disputes, may force a buyout, or result in litigation.

CASE STUDIES

The case studies below highlight common scenarios in a blended family and the considerations that may be applied.

a. Raj and Mira

Mira, age 72, has three children from her first marriage. She remarries Raj, age 70, who has one child from a prior relationship. Mira has investments and a valuable cottage property that she inherited from her mother, and which has been in the family for generations. Mira added Raj to the title of their primary residence. Mira and Raj have also

designated each other as the beneficiaries of their insurance policies and registered assets. While Raj is not as wealthy as Mira, he is financially independent, and he receives a good income from his investments.

Mira and Raj prepare simple wills, leaving all their assets to each other. On the second death, their wills leave everything equally to the four children. Mira and Raj trusted each other to not change their respective will.

Mira dies shortly after they prepare their wills. All assets pass to Raj under her will, by right of survivorship and pursuant to the beneficiary designations. Raj is later diagnosed with terminal cancer. After dipping into his investments to pay for medical treatment and personal care, he is forced to sell the cottage property as he is not able to carry its costs. Raj also changes title to the primary residence into joint names with his child for ease of dealing with the property management and expenses. Raj then dies. Mira's children bring a claim against Raj's estate, claiming that the primary residence held in joint names with Raj's child belongs to the estate.

Although Raj did not change his will, the result was not what was intended and led to a dispute. To avoid this contentious result, a comprehensive estate plan would have included the preparation of a marriage contract, where each party released the right to equalization of property on death. As Raj would inherit the principal residence and the proceeds of Mira's insurance policy and registered assets on Mira's death and would be well provided for, Mira could leave the assets she inherited from her mother directly to her children or these could be held in a spouse trust for Raj on a tax-deferred basis until Raj's death, at which time her children would inherit the cottage property and investments. Raj could leave his investments to his child directly, as Mira would be able to comfortably provide for herself if Raj died first.

b. Klara and Kevin

Klara, who is 32, and Kevin, who is 48, are living in a common-law relationship. They do not intend to have children together. They have a full house with each of their two children from prior relationships living with them. Kevin has twin daughters, who are 25, and Klara has a six-year-old son and a four-year-old son. Kevin and Klara did not adopt each other's children. For convenience, they own all assets jointly. Kevin manages their finances, as he is financially savvy.

Kevin unexpectedly dies. Klara inherits all their wealth, as it passes to her by right of survivorship. Klara has a close relationship with Kevin's daughters, which continues after Kevin's death. She decides to make a will for the first time and to use an online will kit and

make a simple will providing that anything she owns at the time of her death is to be divided among her children equally. Klara lives a long life and dies at 82. Her sons discover her will among her possessions and see that they are to inherit her estate. Kevin's daughters argue that they are also considered Klara's children and have always been treated as such. A court application is commenced.

The court will need to look at the context and evidence to determine whether Klara meant to include Kevin's daughters under "children." Generally, the term "children" does not include stepchildren. Had Klara received legal advice, the will would have been drafted clearly to clarify who falls under the definition of "children." Alternatively, Klara should have named the stepchildren specifically if she wanted to benefit them as well. While the court can look beyond the terms of the will at extrinsic evidence to interpret Klara's intention, the cost and delay of the court process could have been avoided had Klara sought legal advice.

CONCLUSION

Blended families are on the rise and require strategic, thorough, and creative estate planning solutions. It is a delicate balancing act to ensure that everyone's interests are protected and to avoid disputes and sometimes litigation against the estate. It is important to start planning conversations early—they can prevent future disharmony and secure peace of mind for the entire family. This Advisory is designed to explain some of the more common issues that can arise when planning for blended families as well as useful strategies for addressing these issues. As with many estate situations, professional legal advice is necessary to successfully navigate these complex matters.

The comments offered in this Client Advisory are meant to be general in nature, are limited to Ontario law and are not intended to provide legal advice on any individual situation. Before taking any action involving your individual situation, you should seek legal advice to ensure it is appropriate to your personal circumstances.