Estate planning and family dynamics

A guide for estate planning in the not-so-traditional modern family

BMO Wealth Management provides insights and strategies around wealth planning and financial decisions to better prepare you for a confident financial future.

For more insights on this topic, read the BMO Wealth Report
bmo.com/wealth/reports/familydynamics

Traditionally, the focus of family estate planning was to ensure property would be passed on to a spouse and/or children in the context of a traditional family.

In today's world, family structures are different from the traditional model. They include blended families, common-law spouses, single households, one-parent families, divorced/separated couples, same-sex relationships, and, multiple-spouse family structures. These 'atypical' family structures warrant new and, different estate planning strategies that may have to address the needs of multiple camps of beneficiaries or heirs-at-law with conflicting (or adverse) interests. Today's global lifestyle adds to the complexity, as families may straddle several geographical jurisdictions.

The family dynamics of such households raise issues for Canadians to consider and to address in consultation with their financial professionals, as they prepare to put in place an estate plan for what may be a non-traditional family unit.

This concept sheet provides insights and technical discussion around many of the issues to be addressed when preparing an estate plan for a variety of family structures, and outlines some of the relevant estate planning considerations and tax implications.[1]

The makings of an estate plan

For families or individuals of high net worth, a simple Will may not be sufficient to form a complete estate plan. While a well thought-out estate plan should definitely include a Will, you may also want to consider trusts for children and spouses, powers of attorney for property and for personal care, domestic contracts, beneficiary designations outside the estate, and life insurance. An estate plan should be kept up to date and reviewed as changing laws and life circumstances occur.

As a good rule of thumb, revisit and reconsider the details of your plan every three to five years. Here are some of the estate planning aims and strategies you may want to consider:

- making adequate provision for surviving dependants (i.e., your spouse, minor child, or a financially dependent adult child or parent) to be able to maintain their current standard of living
- providing sufficient capital to fund future life events, such as a child's post-secondary education, a wedding, birth of grandchildren, or the purchase of a home
- ensuring the smooth succession of the family business
- passing on valuable and treasured family heirlooms, art, and recreational real estate without causing resentment and dispute among family members
- considering philanthropic endeavours and, charitable bequests
- planning for deferral and reduction of personal and corporate tax during your lifetime
- minimizing and deferring of taxation upon death
- reducing probate fees
- planning for future incapacity (mental or physical)
- gifting to children or grandchildren during lifetime and after death either equally or equitably
- recognizing and accommodating for the special needs of certain beneficiaries

Contact your BMO financial professional to learn more about these estate planning issues, and consult your tax accountant and/or estates lawyer for assistance in determining the relevant strategies, and tax and legal implications.

Family status, ownership structures, and your intentions

The foundation of your estate plan is established on three fundamental aspects. The first is your core family unit and your extended family, the second is the nature and location of your worldwide assets (personal and business holdings), and the third is the sum of your intentions and legacy goals.

This concept sheet focuses on the effects of family status on estate plans. For more information about the influence of ownership structures on estate planning, ask your BMO financial professional for the BMO Wealth Management publication Understanding the structure of ownership. If you need more information to help you determine your estate planning goals, ask for the BMO Wealth Management publication Estate planning for a starting point for exploring your estate planning intentions.

When considering your family unit, compare with these examples of family structures in today's society:

- married couples (including same-sex)
- separated (but not divorced) couples
- divorced couples (former spouses)
- blended (or reconstituted) families
- common-law couples
- unattached individuals with no children
- single parents

Laws differ by province and are subject to change

In Canada, the laws of the province of residence of the testator apply to Wills, trusts and estates. These laws differ provincially, and continue to evolve. Laws are always subject to change, and estate law is no exception. For example, the rights of common-law and same sex partners have been expanded in recent years in most jurisdictions. The information given here is general in nature, and it is necessary, particularly in view of provincial differences and ongoing changes, to seek professional legal advice to assist you with your estate planning and Will preparation.

Married and divorced couples

Among wealthy families, estate planning issues are typically addressed prior to marriage, but they can also be dealt with at any time during the marriage. In any marriage, spouses' respective property rights, financial arrangements, and obligations toward each other and their common children are intertwined. This makes the drafting of a Will for each spouse paramount. The nature of estate planning by spouses is such that each spouse's Will affects the other's financial status and subsequent flow of assets to the next generation or other intended beneficiaries, and thus affects the other spouse's succession plan. To learn more about the specific estate planning considerations for spouses, ask your BMO financial professional for the BMO Wealth Management publication United we stand: Planning by spouses.

Some of the solutions to issues faced by couples are provided by law, but typically they are also addressed in a domestic contract, known as a marriage contract. For instance, a spouse's rights in the event of marriage breakdown (divorce or death) regarding property owned by the other spouse may be defined. A marriage contract does not deal with child custody and child support, which would be determined at the time the marriage is dissolved.

Regardless of age, there are many reasons why spouses-to-be may want to enter into a marriage contract. In most provinces, provincial family law regimes equalize the difference in net worth acquired or accumulated by each spouse during the marriage at valuation date (date of separation). In a lifetime it is possible to enter into multiple marriages, some of which may be short lived. Many individuals wish to avoid sharing their wealth repeatedly as the result of marital breakdown. Those marrying for the second or third time, particularly where children from previous relationships are included in the mix, may wish to limit future sharing of wealth, or what they may consider a "financial loss."

In Québec, the effect of a marriage contract is to engage the regime which the spouses have elected (e.g. separation of property, partnership of acquests) to govern the division of their property in the event of marriage termination. In all other provinces, a marriage contract is used to override the terms of provincial family law in the event of divorce.

In all provinces and territories (other than Alberta, British Columbia, and Québec), marriage revokes the existing Wills of spouses, but does not revoke powers of attorney or beneficiary designations. Divorce, on the other hand, does not revoke a Will but does void all appointments and gifts written in the Will which are in favour of the former spouse. That leaves a legal vacuum with respect to appointments of executor of the estate and trustee of any trusts, and for gifts of property originally intended for the former spouse. In this case, other members of the family will inherit that property instead. However, beneficiary designations and appointments of powers of attorney which are in favour of the former spouse are not revoked by the divorce. Consequently, it is recommended that estate planning documents such as Wills, powers of attorney, and beneficiary designations (for registered plans and life insurance policies) should be redrawn after marriage breakdown, in order to establish current intentions.

Separating from a married or common-law spouse is a traumatic and difficult experience. In this emotionally challenging time, it is important to understand how separation may affect your wealth from a tax and estate planning perspective, and to take the necessary steps. These may include some of the following actions:

- rewriting your will
- severing jointly held property into co-tenancy
- purchasing life insurance to fund child or spousal support payments
- changing beneficiary designations on existing plans and policies

For more information about some of the necessary steps to consider when a marriage dissolves by death or divorce, ask you BMO financial professional for the publication Can your financial plan withstand one of life's unwelcomed surprises?

Tax implications for married and divorced couples

Once married, spouses file their annual income tax return jointly. Married couples can arrange their financial affairs as one family unit, so that they pay as little tax as possible.

The federal Income Tax Act (ITA) provides married couples with many tax advantages, such as employer pensions, spousal RRSPs, TFSAs, and capital gains tax deferral on transfer of property from one spouse to the other (although attribution rules may apply, if the property is going to generate income after the transfer).

These tax advantages available to married couples cease when a divorce is granted. Hence, during divorce proceedings, certain tax implications or advantages could be negotiated between the separating couple.

To learn more about some of the tax planning opportunities for couples, ask your BMO financial professional for the publication Pension income-splitting provides tax planning opportunities for couples.

Estate planning for common-law couples

In most provinces in Canada, common law status generally commences after three years of consecutive cohabitation (two years in British Columbia), or after a shorter period if the partners are the parents of a child for family law purposes. While common-law couples are treated by the ITA (cohabitees for one year or parents of a child) like legally married spouses for taxation purposes, the same is not necessarily true with respect to provincial statutes governing family and succession law as they relate to estate planning. There are some key points to remember:

- Common-law partners are not always recognized under provincial property or succession laws regarding property rights. A common-law partner may not have an automatic right to any portion of the estate of his or her deceased spouse.
- Depending on circumstances, a common-law partner may apply to the courts for continued support from a deceased spouse's estate under provincial dependants' relief legislation, or for a share in the value of property in the deceased spouse's estate under a constructive trust claim (the law of equity).
- Common-law partners are recognized under the ITA for tax purposes, and thus assets of a deceased partner may be rolled over to the surviving partner or to a qualified partner trust on a tax-deferred basis.

Common-law couples can enter into a cohabitation agreement similar to a marriage contract in order to limit property entitlement and financial rights, and obligations between them. While a common-law spouse does not share in the value of property owned by the other spouse in most provincial regimes, the non-owning spouse may be able to make a claim for a share in the value under a constructive trust claim. Most cohabitation agreements restrict this right. A restriction on spousal support, however, depending on circumstances, may not be enforceable.

Tax implications for common-law couples

For taxation purposes, the ITA defines that common law status commences after one year of cohabitation. Although common-law couples can take advantage of tax planning strategies as do married couples, their respective property rights may not be the same as those of married couples. Since the ITA is a federal statute while succession law and family law governing spousal property and support rights are under provincial statutes, the estate planning implications of common law spouses must be considered provincially.

Estate planning for blended families

Blended families generally consist of reconstituted family groupings of spouses/partners and their respective children. Typically, these family groupings have little in common with one another beyond the relationship of the spouses. The management of property and estate planning of blended families can involve complicated family dynamics, such as reluctance of the groups to communicate openly with each other, and a potentially mutually exclusive possessive and protective approach by each group toward its members, especially the children.

Stepchildren do not automatically share in the estate of their deceased step-parent under provincial intestacy legislation or at separation or divorce under family law. Spouses of the marriage that formed the blended family, however, do have such rights, which may be seen to encroach on expected inheritances or support of children from a previous relationship.

It is often in the blended family context that marriage contracts or cohabitation agreements are used, in order to divide wealth in a manner that adequately provides for all dependants, within the various family groupings.

New Wills are necessary

As mentioned earlier, marriage revokes a Will in all provinces except Québec, Alberta and British Columbia. The only exception to this is when the existing Will was made in contemplation of the marriage. In the event of death after the date of marriage or re-marriage, and without a new Will or a Will in contemplation of marriage, the deceased spouse will be considered to have died intestate, and provincial rules of intestacy will govern the distribution of the estate. Depending on the particular circumstances, the results can be disadvantageous to the deceased's loved ones, both in terms of tax-related – and perhaps more importantly – non-tax related consequences such as property passing to unintended heirs.

Estate planning for single households

Consider an individual with no family at all: no spouse, no children, no parents or grandparents, no siblings, no nieces or nephews. You might be tempted to suggest that such an individual does not need an estate plan. After all, there are no dependants. However, this person needs estate planning as much as anyone, and perhaps even more so. Without an adequate plan, including a Will, the entire estate may go to the government (unless there is a successful claim by a remote relative) when he or she dies, according to escheat provisions in provincial intestacy legislation. This may not be what that person would have desired. To avoid this possibility, an unattached person must prepare an estate plan, including a valid Will, to indicate how his or her estate is to be distributed.

Finding a trusted executor

If an individual has no relatives, he or she may have trouble choosing an executor. Of course, a close friend can be appointed to this role. While many people are comfortable taking on this burden for family members, they may be less inclined to place that same burden on a friend.

If the individual has no close friends residing in Canada or does not wish to burden them with this responsibility, he or she might choose to appoint a professional, such as a lawyer or accountant, or alternatively, an independent entity such as a corporate trustee, namely, a trust company, as executor of the estate.

Overlooked assets

If an individual has no relatives or close friends, there is a risk that his or her assets may not be fully accounted for upon death. Without an organized record of the assets, some could be overlooked simply because no one was aware they existed. For example, if the individual maintained that money in several bank accounts, or held investments and failed to maintain adequate records of those holdings, it is quite possible that the executor would fail to inventory those assets and fail to pass them on to the beneficiaries of the estate. Thus, an individual with no close ties must maintain an up-to-date list of assets and ensure that his or her chosen executor knows where to find that list. If the individual has a safety-deposit box, it is also a good idea to keep a duplicate, up-to-date copy of the inventory there.

Tax implications

An individual with no family has limited opportunity for tax planning. With no spouse, spousal rollover provisions for capital property do not apply. Furthermore, he or she is unable to pass tax-sheltered assets on to children or grandchildren. The Canada Revenue Agency (CRA) will consider all of the assets to be disposed of at fair market value at the time of death, which could result in a significant tax liability. However, an unattached individual can still take advantage of estate-freezing strategies to limit tax liability upon death. For example, any growth assets could be given to a friend or a charity prior to death, or the assets could be transferred to an inter vivos trust established for those beneficiaries. The individual could transfer the assets to a holding company, or reorganize the capital structure of an existing company, taking back preferred shares and selling or gifting to a friend or a business associate the newly issued common shares.

Single unattached parents

While it is true that young two-parent families would be wise to plan for their simultaneous or temporally close death, it is in fact quite unlikely that both parents would die at the same time, leaving their minor children with no parent. However, if a single parent dies, his or her minor children would definitely be without a parent. All parents need to prepare an estate plan that describes how their parental role is to be filled in the event of their death, but this is especially so for single parents.

Appointment of a guardian for minor children is done in a Will. The guardian will receive immediate temporary custody of the children upon the parent's death. Within 90 days of the date of death, the guardian must apply to the courts for permanent custody. While the courts are not obliged to honour the appointment specified in the Will, they will normally do so unless there is an obvious reason to deny the request.

Tax implications

While alive, a single parent can claim an eligible dependant allowance in respect of one of his or her children for a tax credit. On death, however, there are tax disadvantages. A single parent has limited opportunities to defer taxes upon death because spousal rollover provisions are not available. Thus, whether assets are left in trust for his or her children, or are bequeathed to some other beneficiary, the assets are deemed to be disposed of at fair market value, resulting in a tax liability for the year of death. The deceased's tax-sheltered savings (RRSPs and RRIFs), however, may be rolled over to the registered plans of minor or financially dependent adult children or grandchildren on a tax deferred basis.

Seek professional advice

Seek the advice of professionals to ensure your family's needs are addressed in your estate plans, whatever the structure of your modern family. Contact your BMO financial professional to discuss your estate plans and explore the estate planning strategies that may be appropriate for you and your family. This concept sheet is meant to be general in nature, and does not constitute tax or legal advice. You are encouraged to consult with your trusts and estate lawyer and a tax accountant before implementing your estate plan.

We're here to help.™

[1] The Civil Code of Québec differs from the common law regime in other provinces, so some of the discussion in this article does not apply in Québec.

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