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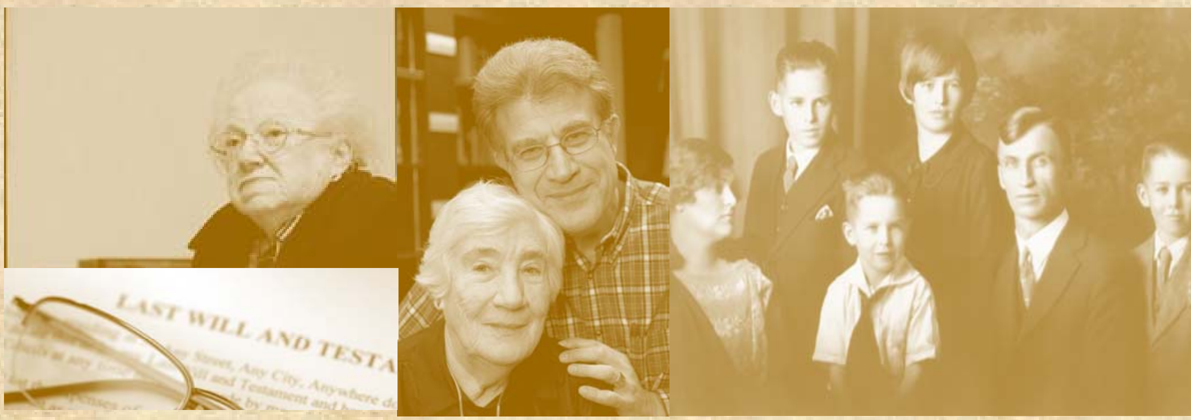

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THE JEWISH COMMUNITY FOUNDATION OF MONTREAL
LA FONDATION COMMUNAUTAIRE JUIVE DE MONTREAL

Henson Trusts

Presentation to:
JEWISH COMMUNITY FOUNDATION
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Nature of Henson Trust

- Absolute discretionary trust where the beneficiary has no legal right to claim a benefit from the trust

(Updated as of April 1, 2011)

Ontario decision – Henson

- First dealt with by the Supreme Court of Ontario in *Ontario (Minister of Community & Social Services) v. Henson*, 1987 CarswellOnt 654
- Ontario law forbids social benefits if someone has liquid assets worth more than $3,000
- Ontario regulation defined liquid assets as, among other things, "…a beneficial interest in assets held in trust and available to be used for maintenance"

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Ontario decision – Henson (cont'd)

The Will provided:

- "*To pay so much of the income therefrom, or the whole of the income therefrom, together with so much of the capital thereof to or for the benefit of my daughter AUDREY JOAN HENSON as my Trustees shall in the <u>exercise of their absolute and unfettered discretion consider advisable from time to time</u>. Any income not so paid in any year shall be accumulated by my Trustees and added to the capital of the residue of my estate, provided, however, that if it becomes unlawful for my Trustees to continue such accumulation of income, then the income not so paid in any year to or for the benefit of my said daughter shall be paid to The Guelph and District Association for the Mentally Retarded Incorporated.*"

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Ontario decision – Henson (cont'd)

- *The residue of my estate and the income therefrom shall not vest in my said daughter and the only interest she shall have therein shall be the payments actually made to her, or on her behalf, and received by her or for her benefit therefrom. Without in any way binding the discretion of my Trustees, it is my wish that in exercising their discretion in accordance with the provisions of this paragraph, my Trustees take account of and in so far as they may consider it advisable take such steps as will maximize the benefits which my said daughter would receive from other sources if payments from the income and capital of the residue of my estate were not paid to her for her own benefit, or if such payments were limited to an amount or time. In order to maximize such benefits, I specifically authorize my Trustees to make payments varying in amounts and at such time, or times, as my Trustees in the exercise of their absolute discretion may consider in the best interests of my said daughter."* [our emphasis]

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Ontario decision – Henson (cont'd)

The Court held:

Those, briefly, are the facts before us. In a very able argument it was advanced that the interest of Miss Henson fell within the ambit of the term "liquid assets", and that is the issue before the court. To put it briefly, the question is simply whether or not the respondent has, "a beneficial interest in assets held in trust and available to be used for maintenance" in respect of this estate pursuant to s. 1(1)(a) of Regulation 318

In our view, the provision of the will, set out above, <u>gives the trustees absolute and unfettered discretion</u>; the respondent <u>could not compel the trustees to make payments to her if there were not funds available to her under the Family Benefits Act</u>, sufficient to meet her needs. Therefore, in our view, Miss Henson <u>does not have a beneficial interest</u>, as that term is used in the definition of liquid assets." [<u>our emphasis</u>]

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Ontario decision – Henson (cont'd)

- Judgment confirmed by the Ontario Court of Appeal *Ontario (Minister of Community & Social Services) v. Henson*, 1989 CarswellOnt 542

Quebec legislation

- *Individual and Family Assistance Act*, R.S.Q., c. A-13.1.1
- *Individual and Family Assistance Regulation*, R.R.Q., c. A-13.1.1, r. 1
- There are two regimes:
  - the Social Assistance Program
  - the Social Solidarity Program

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Quebec legislation (cont'd)

The Social Assistance Program

- Provides last resort assistance for persons whose capacity for employment is not severely limited
- Person has less resources (liquid assets) that are necessary to provide for their needs
- If admissible, person receives the basic benefit less the income, earnings and benefits, liquid assets and property

Quebec legislation (cont'd)

The Social Solidarity Program

- Provides last resort assistance for persons whose capacity for employment is severely limited
- To be eligible one must produce a medical report establishing that the adult's physical or mental condition is significantly and in all likelihood permanently or indefinitely deficient or impaired and therefore, in view of the adult's socio-professional profile, the adult's capacity for employment is severely limited

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Eligibility

- Liquid assets cannot exceed amounts set in the Regulation
- Liquid assets include deposits with financial institutions, securities, amounts owing, instrument payable on demand, etc.

Jurisprudence

- In *C…L… c. Ministre de la Solidarité sociale,* SR-66202, 5 March 1999, the Administrative Tribunal of Québec (the “Tribunal”) held that the income distributed to the minor daughter of the deceased from a testamentary trust in the amount of $100 per week must be taken into account for the purpose of determining the amount of financial assistance

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Jurisprudence (cont'd)

- "In M…M c. Ministre de la Solidarité sociale, SAS-Q-059761-0002, 8 January 2003, the Tribunal disallowed the benefits since the recipient could receive $1500 per month from his mother's testamentary trust"

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Jurisprudence (cont'd)

- The fact that the will provided for a monthly payment of $1500 that was not obligatory, but strongly suggested and the fact that the son was the sole beneficiary of the trust were elements that justified cancellation of the benefits

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Jurisprudence (cont'd)

- Article 1261 of the Civil Code of Quebec provides: "the trust patrimony, consisting of the property transferred in trust, constitutes a patrimony by appropriation, autonomous and distinct from that of the settlor, trustee or beneficiary and in which none of them has any real right."
- However this article does not prevent a beneficiary from claiming payments which are owed to him by virtue of article 1284 of the Civil Code of Quebec

Jurisprudence (cont'd)

- Yet in *J…R… c. Ministre de l'Emploi, de la Solidarité sociale et de la Famille,* SAS-Q-102697-0311, 9 August 2004, the Tribunal did not cancel the benefits even though certain amounts had been paid from the testamentary trust created by her mother

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Jurisprudence (cont'd)

- Payments of income and capital were at the complete discretion of the trustees
- The daughter was the sole beneficiary during her lifetime

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Jurisprudence (cont'd)

- The Tribunal fully respected the distinct patrimony of the trust and absence of any real right of the beneficiary in the trust property

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Jurisprudence (cont'd)

- It is possible to infer from this decision that payments from a true discretionary trust will not have any impact on the calculation of allowances under the Act
- To reinforce the argument that the payments are not income distributions of a regular and permanent nature, it may be preferable to make sporadic payments from capital

Jurisprudence (cont'd)

- It would also be advisable that the trust payments be expended before the last day of the month in which they are received so as to comply with the monthly liquid asset test (non-compliance could reduce future allowances)

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Jurisprudence (cont'd)

- In *R…D… c. Ministre de l'Emploi et de la Solidarité sociale*, SAS-Q-121675-0511, 21 September 2006, the Tribunal held that the Minister was justified in cancelling the benefits of an intellectually disabled child who was the sole beneficiary of the testamentary trust created by his father

Jurisprudence (cont'd)

- The will provided that the trust "shall use" the income for the maintenance, etc. of the son

Jurisprudence (cont'd)

- The Tribunal was of the view that the testator had conferred a certain discretion upon the trustees as to the amounts and modalities of the payments, however there was no discretion as to whether they could make the payments; the trustees were obliged to do so

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Jurisprudence (cont'd)

- In *S…M…c. Ministre de l'Emploi et de la solidarité sociale*, SAS-Q-132343-0611, 19 June 2007, the beneficiary lost his case because the will provided that the trustee " shall use" the income for the maintenance and needs of my nephew, according to his needs

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Caveat

- In M…M… c. Ministre de l'Emploi et de la Solidarité Sociale, 2010 QCTAQ 05842, 28 May 2010, the will of the mother expressly provided that the trustees were to pay her son $200 per month; as a consequence the son's benefits were reduced, despite the fact that the annual cost of lodging, groceries, and pocket money clothing, exceeded the social assistance benefits and had to be supplemented by payments from the trust

Caveat (cont'd)

- Careful drafting of Henson trust
- Independent trustee required by virtue of article 1275 CCQ
- Choice of trustee is key
  - understanding duties (re: investments, distributions, accounting, records, filing tax returns)
  - age given long duration of trust
  - familiar with beneficiary and active interest in his/her well-being
  - avoid potential conflicts of interest: query: should future beneficiary be a trustee?
- Close monitoring of operation of trust and legislation
  - e.g. - respect "liquid assets" thresholds

    - no regular income payments

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Caveat (cont'd)

"[…] There is much greater likelihood that a Court will consider a handicapped individual who is the sole, albeit discretionary, beneficiary during his/her lifetime of the trust as actually owning the assets of the trust. Consequently, a discretionary « sprinkling » trust with several beneficiaries, including the individual with the handicap, may be more appropriate to protect the continued entitlement of the handicapped individual to receive governmental benefits, since it would presumably be more difficult to imply sole ownership in such a situation.

While such a trust could impose obligations to distribute income or capital, the trustee must be given complete and unfettered discretion to decide which of the beneficiaries will benefit."

> Howard S. Black, "Trusts for Handicapped Beneficiaries", CCH, Canadian Estate Planning Guide

Caveat (cont'd)

Query: is a right of habitation in a residence owned by the trust excluded?

Not an expressly mentioned exclusion, but the reference in section 55(2)(a) to "any earning or other benefits received" might suffice to exclude it

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Tax Considerations

- Deemed disposition of capital property on transfer to trust: no rollover available
- 21-year deemed disposition applies, but it is possible to rollout pursuant to subsection 107(2) ITA before the 21-year deemed disposition
- Preferred beneficiary election

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Moral and Practical Considerations

- Wealthy families who can afford to maintain their children without public support should utilize alternatives to the Henson trust
- Planning an estate to maintain public support is ultimate insurance against economic catastrophe
- Application of income and asset tests for access to public support implies these programs intended to provide a safety net for the worst-off disabled people
- Foregoing income support may also implicate loss of ancillary health benefits, e.g. medications, medical apparatus, dentistry, eyeglasses, etc.

Moral Considerations (cont’d)

- Public policy structures programs of public support so that disabled persons must be impoverished before they are entitled to public support and they lose public support if, through their own efforts or inheritances, they rise above poverty
- Estate planning with Henson trusts provides relief from a fundamentally immoral policy

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JEWISH COMMUNITY FOUNDATION

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TRUSTS FOR SPECIAL NEEDS

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TRUSTS FOR SPECIAL NEEDS

It is well-known that trusts have an important role to play in estate planning but, in particular, the fact that they may be attractive in planning for the special needs of disabled persons and older persons should not be surprising.

Many lawyers and estate planners aspire to be “trusted advisors”. This implies a shift in focus from technical estate planning to broader humane considerations, and a corresponding move towards responding to the special needs of the vulnerable. An individual approaching old age or parents with a disabled child are often confronted with conflicts and dilemmas. What they should avoid is paralysis (or doing nothing) and impulsivity (or choosing the easy way). In a sense, paralysis and impulsivity represent opposite sides of the same coin.

For the purposes of this presentation, I will focus on trusts that purportedly serve the needs of older persons and disabled persons, namely the alter ego trust and the Henson trust. In both cases, contemplating the use of these trusts raises a host of legal and tax issues which I will briefly review.

The purpose of this overview is to synthesize the issues and concerns attendant upon the use of these trusts in order to enable an older person or parents of a disabled child to work towards the formulation of a plan. To achieve this end, what is required is a goal-driven and structured process that should result in a practical solution reflecting the human needs of the persons in question while taking into account, financial, tax and legal considerations.

ALTER EGO and JOINT SPOUSAL TRUST or COMMON-LAW PARTNER TRUST

The terms "alter ego trust" and "joint spousal trust" or "joint common-law partner trust" (the latter two collectively referred to as the "joint partner trust"), refer to particular *inter vivos* trusts which satisfy certain requirements set out in the *Income Tax Act* ("ITA") and which are defined in section 248 of the ITA. References herein to the alter ego trust include the joint partner trust wherever the context permits or unless otherwise indicated.

The requirements for an alter ego trust are as follows:

(1) The settlor must be 65 years of age or older;

(2) The settlor must be resident in Canada;

(3) The trust is created after 1999;

(4) The trust is resident in Canada (essentially, the trustees ought to be Canadian residents and ensure compliance with the mind and management test recently enunciated by the courts);

(5) The settlor as beneficiary is entitled to receive <u>all the income of the trust</u> arising before his or her death [in the *alter ego* trust] or the settlor or his or her partner (that is, married spouse or common law partner, as defined in the ITA) is entitled to receive <u>all the income of the trust</u> arising before the death of the survivor of them [in the joint partner trust];

(6) No other person is entitled to receive or otherwise obtain the use of any of the income or capital of the trust during the settlor's lifetime [in the *alter ego* trust] or during the lifetime of both or the survivor of the settlor and the partner [in the joint partner trust];

(7) The trust does not make an election referred to subparagraph 104(4)(a)(ii.1) of the ITA.

The requirements in items (1) to (6) above also apply in the case of a joint partner trust.

Although beneficial tax consequences will flow to the settlor and the trust respectively, two pitfalls ought to be avoided: (1) to allow the income tax tail to wag the estate planning dog (while tax planning is important, it is only part of the process); and (2) to fulfil the technicalities of the *Income Tax Act*, but to fail to satisfy the requirements of civil law for the constitution of a valid trust.

What follows is a brief review of the benefits and drawbacks of these trusts both with respect to tax considerations and civil law considerations.

1. TAX CONSIDERATIONS

Of course, it has always been possible to remove assets from one's estate or patrimony by means of transfers to an *inter vivos* trust. However, transfers (other than to a spousal trust) generally result in a disposition at fair market value of the transferred assets. The novelty of alter ego trusts is that assets can be settled on them without immediate taxation.

These trusts effectively extend the spousal trust rule in section 73 (1.01) of the ITA (allowing the transfer of property to the trust without triggering capital gains) to allow the settlor to be a beneficiary as well. There will be no taxation of the assets transferred by the settlor to the trust, at the date of transfer, and the trust will acquire those assets at the settlor's adjusted capital cost. Furthermore, there will be no deemed disposition of the trust assets on the date which is 21 years after the creation of the trust. The trust will be deemed to have disposed of the trust assets at fair market value on the earlier of these dates: (1) the date of actual disposition of trust assets; or (2) the date of death of the settlor [in the *alter ego* trust] or of the survivor of the settlor and his or her partner [in the joint partner trust]. The disposition will be taxable to the trust, not to the deceased settlor [of the *alter ego* trust], or to the subsequently deceased survivor of the settlor or partner [of the joint partner trust].

In the case of what would otherwise be an alter ego trust, the trust can make an election under paragraph 104(4)(a)(ii.1) of the ITA, in its income tax return for its first taxation year, not to have a deemed disposition on the death of the settlor. If this election is made, the "21 year rule" will apply to the trust and also, pursuant to paragraph 73(1.02)(c) of the ITA, there will be no rollover with respect to the transfer of assets into the trust.

There are, then, two features that make these trusts attractive substitutes for wills: (1) the availability of the tax free rollover; and (2) the ability to appoint in advance contingent beneficiaries to whom the trust assets will be transferred at the death of the settlor or at the death of the survivor of the settlor or partner.

Title to a principal residence can be transferred to an alter ego trust without impairing the principal residence exemption. However, RRSPs, RRIFs, LIRAs and LIFs as well as TFSAs cannot be transferred to these trusts.

During the lifetime of the settlor, capital gains and losses realized in the trust should normally enable an offset against the settlor’s capital gains and losses unless the trust precludes capital encroachments for the benefit of the settlor. (In such case, a careful assessment of the settlor’s ability to minimize income tax by offsetting capital gains and losses should be made before assets are transferred to the trust.)

At the death of the settlor, an alter ego trust is deemed to dispose of its assets. Any resulting gain or loss is taxed to the trust. Being created during the life of the settlor, an alter ego trust is by definition an *inter vivos* trust. *Inter vivos* trusts are taxed at the highest marginal rate; they do not enjoy the progressive rates at which individuals are taxed. Accordingly, a capital gain arising from the deemed disposition triggered by the death of the settlor may be taxed at a higher rate than would have been the case if the settlor had held the asset at death, unless the trust is then resident in a low tax province.

Because these trusts are *inter vivos*, the beneficial tax rates accorded to testamentary trusts are not available and there is no minimum tax exemption. This will mean that taxation of any trust income will be at the top marginal rates after the death of the settlor if the assets are not immediately distributed to the beneficiaries. It is ironical that these trusts serve to reduce provincial probate fees where applicable while increasing federal income taxes upon death.

Because of the application of a specific attribution rule found in sub-section 75(2) ITA, an alter ego trust will not afford income splitting opportunities since the settlor, while alive, will be taxable on all income and taxable capital gain from the property transferred to the trust or from property substituted therefor. If the attribution rules are avoided (i.e., no possibility for the settlor to benefit from the capital or second generation income) still the alter ego trust will not provide income splitting opportunities during the lifetime of the settlor considering its maximum marginal tax rate. Following the death of the settlor, an attractive option might have been to have the remaining assets of the alter ego trust pour over into a testamentary trust and thus become subject to a more beneficial tax treatment for the future. However, the CCRA is firm in its position that a trust receiving assets from an alter ego trust will not qualify as a testamentary trust and hence, generally speaking, the highest marginal tax rate will continue to be applied. In addition, an alter ego trust must select a calendar year end, unlike a testamentary trust.

Depending on the income of the trust, charitable donations made by such a trust following the death of the settlor may be less tax effective than if made by will. The donation tax credit available to the trust is limited to 75% of the trust's income for the year in which the gift is made, while in the year of death and the preceding year, 100% of an individual's net income is eligible for the donation tax credit. Further, because a trust can only use the donation tax credit to offset its own income (and not the deceased's), the trust could have an unused donation tax credit for the charitable gift but the deceased's estate could have a tax liability. Unlike the special treatment available for a donation made in a will, the charitable tax credit in an alter ego trust cannot be carried back – it can only be carried forward. Because of the basic requirements of alter ego trusts, donations cannot be made prior to the death of the settlor (or in the case of a joint partner trust, prior to the death of the surviving spouse).

Like other trusts, an alter ego trust will be taxed in the province in which it is resident. The *Income Tax Act* does not set out rules for determining the residence of a trust, but, generally, a trust is considered to reside where a majority of the trustees reside provided they act by majority vote and are unfettered in the administration of the trust. This standard derives from the leading case on trust residency, *Thibodeau Family Trust* v. *The Queen*. In two recent decisions, *Garron Family Trust* v. *The Queen* and *Paul Antle and Renée-Marquis Antle Spousal Trust* v. *The Queen*, the test was recast to resemble that for corporations, that is, the actual residence of a trust is where central management and control is exercised. This creates the possibility of setting up a trust such that it could be resident in a low tax province. However, unless the trust is structured in such a way as to make it impossible for the settlor to access the capital of the trust, it will be impossible to benefit from the low provincial rate while the settlor is alive.

The possession of foreign assets by an alter ego trust may result in a degree of double taxation. The benefit of foreign tax credits may be lost because the settlor pays the Canadian tax on the resulting income according to subsection 75(2) of the ITA while the trust has the benefit of the foreign tax.

Should the settlor wish to provide for his or her children after his or her death by keeping his or her assets in trust for them for an extended period, the fact that one or several of the children is a U.S. resident may be problematic. Income paid from a Canadian trust to a non-resident of Canada is subject to withholding tax. *The Canada-United States Tax Convention* (1980) as amended (the "Treaty") provides at Article XXII, paragraph 2, that income distributed by an estate or trust is subject to tax not exceeding 15 percent of the gross amount of the income. The Canadian tax may be credited against any tax payable in the United States on the income distributed to the beneficiary. Distributions of income from an *inter vivos* Canadian resident trust which are characterized as "designated income" will trigger application of a Part XII.2 tax at a rate of 36% for the trust, in addition to the withholding tax. Since the Part XII.2 tax is assessed to the trust and not the U.S. beneficiary, no relief is available under the Treaty.

2. CIVIL LAW TECHNICALITIES

While the alter ego trust is designed to give the settlor considerable control and flexibility regarding the trust during his or her lifetime, it is necessary for the settlor to act with an independent trustee pursuant to article 1275 of the *Civil Code of Québec* ("CCQ").
It may be advisable to have the settlor as one of several trustees (say three) with the other trustees being the same persons as the liquidators of the settlor's future estate. Consequently, when the settlor dies, or if he or she becomes mentally incompetent, those persons would continue as the trustees.

It will be necessary to transfer title to property intended to be held in the trust to the trustees. Mutation taxes would not be payable on transfers of land.

There may be a very real possibility that the relationship between the settlor/trustee and the alter ego/joint trust may become hopelessly muddled because he or she does not respect or understand the significance of creating and maintaining the trust. As mentioned earlier, he or she may forget to register new assets in the name of the trustees or the trust. If it is not clear that if the assets are held by the alter ego trust, will they end up in the estate of the individual, rather than the trust? If so, perhaps a bequest of the assets intended to be in trust should nonetheless be provided in order to prevent the assets ending up governed by a will with the "wrong beneficiaries"?

3. WILL SUBSTITUTE

After the death of the settlor (of an alter ego trust) or the last to die (of a joint partner trust), the remaining assets of the trust are distributed directly to the designated beneficiaries according to the terms of the trust agreement.

When the alter ego trust was first announced, it was viewed as an ideal estate planning tool and vehicle for avoiding probate in some provinces such as Ontario where probate fees or estate administration taxes are high (1.5%) and in British Columbia (1.4%).

This is not a relevant advantage for Quebec where notarial wills for which probate is not required are primarily used and, in the case of a witness will or holograph will which do require probate, there are no probate fees or taxes in Quebec.

Nonetheless, the alter ego trust is an imperfect will substitute insofar as the settlor may only transfer presently-owned property to an *inter vivos* trust pursuant to articles 1818 and 1823 CCQ. Therefore, any property acquired by the settlor after the trust is established would devolve according to the settlor's will, or in the absence of a will, pursuant to the intestate rules.

4. Privacy and Confidentiality

Whereas a probated will is a public document, and thus cannot remain confidential or secret, an *inter vivos* trust need never come to the attention of anyone other than the settlor, trustees and beneficiaries. The same high degree of confidentiality is inherent in notarial wills.

There is no publication or registration requirement for personal trusts in Quebec.

5. Changes More Difficult to Make

As noted above, an alter ego trust can serve to replace a will, subject to the comments above. One of the fundamental tenets of the law of wills is that, as long as a testator has the requisite testamentary capacity, he or she can change his or her will "at will" – even from his or her deathbed. With a trust, it is not so easy. This can be a good thing (in that it reduces the risk of undue influence) and not such a good thing (if urgent changes are legitimately desired). Indeed, concern has been raised that amending a trust to add new beneficiaries may effectively constitute a resettling of the trust or a disposition of a portion of each beneficiary's interest which could be problematic for tax reasons even if the trust itself provides an amending formula. Some Quebec authorities even question the validity of such an amending formula, maintaining that only the court may amend or vary the terms of a trust. Furthermore, in Quebec, there is a caselaw to the effect that even the discretion of the court to amend a trust does not extend to the addition of a beneficiary.

6. AVOIDING WILL CONTESTATION

It should be kept in mind that the strategy of using an alter ego trust may be effective insurance to avoid post-mortem litigation which may stem from an unhappy beneficiary's attempt to contest a will. There may be fewer grounds for successful litigation challenges to the deceased's planned disposition of assets than if a will were used.

7. UNINTERRUPTED ACCESS TO, AND MANAGEMENT OF, ASSETS

Since the alter ego trust also serves as a means of distributing assets on the settlor's death or at some later date after death, it functions like a will.

As will substitutes, these trusts also ensure immediate and continuous access to the assets of the deceased. Generally, upon death, all personally held assets, including bank accounts and registered plans, are inaccessible to heirs until the will has been probated. Until then, the family of the deceased may not be able to access funds needed for day-to-day living expenses or to pay bills. Also, delays in settling the estate may interfere with the ongoing management of an active business. By contrast, the trustee already controls the trust assets and need not be delayed in addressing these issues.

8. SUBSTITUTE FOR DISABILITY PLANNING IN THE EVENT OF INCAPACITY

In addition to serving as a will substitute, an alter ego trust can effectively supplement disability planning. There are three good reasons to consider this alternative: (1) to accommodate complex planning and unforeseen circumstances, (2) for extra-jurisdictional recognition, and (3) to prevent abuse and undue influence.

First, planning for disability is done customarily by using a continuing power of attorney or mandate in the event of incapacity ("mandate"). Mandates are better construed as vehicles for effecting mundane affairs (paying bills, etc.) on behalf of the incapable grantor than as tools for complex estate planning. To serve their purpose, mandates must be readily accepted by a variety of institutions and individuals (many of whom will have no legal training and little access to legal advice). This puts a premium on standardization and simplicity: a mandate laden with too many "unusual" features may not be accepted by third parties. If a mandate is not significantly customized, it may not meet the needs of the grantor. To give but two examples: the mandatary may be unable to make gifts or support payments to family members the mandator would have made (if capable); conversely, the mandatary might dispose of property the mandator would have wanted preserved. By contrast, trusts can accommodate any amount of customization without concern that the trustee's authority to deal with trust assets will be questioned by third parties.

Furthermore, a mandatary is completely restricted in his or her ability to effect changes to the mandator's estate plan, for example, to transfer assets to a trust. This is tantamount to will-making for another person and thus forbidden by the law.

Second, difficulties may arise in exercising a mandate outside the jurisdiction in which it was executed. Different provinces (and the different states in the U.S.) have different requirements of execution and, even if a mandate has been properly executed, there is no guarantee that it will be accepted by a foreign bank or financial institution, or to sell real estate, particularly if the rules of execution differ substantially from those of the province where it was executed. By contrast, once assets have been transferred to a trust, the title is drawn up in the name of the trustee and there is little risk that third parties will balk at dealing with the trustee.

Third, using a trust may reduce the risk of abuse and undue influence. While the law relating to mandates is still young, the law of trusts is well established. The nature of a trustee's fiduciary duties is generally understood and sufficiently onerous to provide some degree of protection against abuse. By contrast, mandates are notorious for lending themselves to the financial abuse, manipulation and undue influence of the elderly or infirm.

For these and other reasons, in planning for the incapacity of persons with large or complex estates, alter ego trusts make attractive supplements to the standard mandate in the event of incapacity.

9. Accounting, Legal and Trustee Fees

An alter ego trust will entail keeping accounting records for the trust and filing annual T-3 / TP-646 tax returns.

In addition to ongoing accounting fees, there will be legal fees in establishing the trust which will vary with the degree of customization required. Finally, there will be trustee fees if a professional trustee is used.

10. Limited Creditor Protection

The property of a trust does not form part of the settlor's patrimony and is not part of the common pledge of his creditors pursuant to article 2644 CCQ. Article 1261 CCQ clearly states that the settlor has no real right, in the sense of a right *in rem*, in the property held in the trust patrimony. As such, the trust property cannot be seized directly to satisfy his obligations. If the settlor is also a beneficiary of the trust, he has an interest in the trust pursuant to article 1284 CCQ which interest is itself property. This property is a part of his patrimony and is part of the common pledge to his creditors and, hence, it may be seized.

Like the settlor, the beneficiary has no real right in the trust property, which constitutes a patrimony distinct from his patrimony (article 1261 CCQ). The beneficiary has a personal claim or action against the trustee for payment of his benefit (e.g., income or capital or both) pursuant to article 1284 CCQ. This personal patrimonial right is a seizable form of property, subject always to the lawfully stipulated terms of the trust.

Once seized, and once exigible, the rights of the beneficiary can be exercised by the seizing creditor. It is important to underline, however, that the seizing creditor cannot exercise more than the beneficiary's immediate right and interest in the trust.

Inter vivos trusts may play a role in creditor protection. Generally, they are more effective in this regard if fully discretionary and if the settlor is not the trustee (or, if acting as trustee, he or she is one of more than two who act by majority), the basic logic is that if the beneficiary does not have a legally enforceable claim to the income or capital of the trust, neither do his or her creditors. Given that the settlor of an alter ego trust must be entitled to receive all of the income of the trust for the rollover to apply, the level of creditor protection afforded by this type of trust is inherently limited. It may be possible to afford some protection to the capital by ensuring that a distribution of capital to the settlor is precluded or is entirely at the discretion of the trustees.

With a joint partner trust, if the payment of income is discretionary as between the two partners, the trust can clearly be advantageous if only one of the partners is pursued by creditors or required to declare bankruptcy. In that case, the trustee can direct all of the income to the other partner, thus preserving it from creditors of the settlor, for example. Again, the bankrupt or the indebted person should not be able to demand an encroachment on capital in his favour, if this strategy is to be successful.

It will be noted that bankruptcy and insolvency legislation requires intent on the part of the transferor to defeat creditors, but the timing which is relevant is immediately prior to or after the transferor becomes insolvent. The trust patrimony may also be assailable through the Paulian action by creditors of the settlor whose claims arose before the constitution of the trust.

Arguably, the decision to establish an alter ego trust or a joint partner trust, at a time when one does not have creditors and one is certainly not insolvent, is no different from the decision to incorporate a limited company to carry on a business or a decision to place the family residence in the name of one spouse, because the other spouse is employed in a risky occupation which might result in being sued in the future. In other words, even if one of the motives for establishing a trust is creditor protection, so long as there are no actual creditors who are being defrauded, and certainly if the trust is established at a time when the individual is clearly able to meet his debt obligations as they come due, it is unlikely that the establishment of such a trust can be successfully attacked.

11. MATRIMONIAL PROPERTY DIVISION

Could the spouse of a settlor of the alter ego trust, which is presumably intended only to benefit the settlor, gain access to the trust property for the purposes of partitioning matrimonial property either under the matrimonial regime of partnership of acquests or the family patrimony or both?

It would not be prudent to establish an alter ego trust if the timing is too late, that is, the spouse has already commenced action for divorce and equalization of family property. But leaving aside an attack on an alter ego trust on the basis that it is a fraudulent transfer, assume that the trust is established at a time when the settlor is clearly solvent and has no particular intention of avoiding his creditors or, for that matter, avoiding a matrimonial claim for division of property. Assume the marriage is a happy one at the time that the alter ego trust is created. Can there be a subsequent claim?

To my knowledge, there is no jurisprudence in which the spouse of the settlor of an *inter vivos* trust successfully sought to have a property division which would include the assets of the trust. Given the fact that the trust is a separate and autonomous patrimony, this would be an effective obstacle to an actual property division order, even in circumstances where the settlor spouse had significant control over the capital of the alter ego trust (certainly, if that control flowed from his or her status as settlor) whereby the settlor could terminate the trust and require the return of the capital to him or her. However, there is jurisprudence where the court did take the value of a trust's assets into consideration to achieve equitable results, especially with respect to the partition of the family patrimony when the principal residence was held in a trust and also with respect to claims for alimentary support. However, to my knowledge, there is no jurisprudence to date concerning the division of trust assets in the context of the dissolution of the matrimonial regime of partnership of acquests.

On the other hand, to take a different extreme, if the alter ego trust was established well before the date on which a partition of property is sought, and if the settlor spouse has no right to the capital, it may well be that only the income which the settlor spouse is entitled to receive from the alter ego trust would have any relevance to the court's determination of the support that ought to be paid to the other spouse.

Pursuant to the rules governing the family patrimony in the CCQ, if family patrimony assets were alienated in the year preceding the dissolution of the marriage, as for example, by death or divorce, the court may order that a compensatory payment be made pursuant to article 421 CCQ. Furthermore, the same anti-avoidance rule applies if the alienation or transfer took place over one year for the purpose of avoiding the partition with the result that the share of the spouse would thereby be decreased. In Quebec where it is only the accrued value of assets during the marriage which is subject to partition, of course, the establishment of an alter ego trust with assets owned by one of the spouses prior to marriage, would likely be a non-factor, given the age 65 requirement prescribed for an alter ego trust.

12. LIMITED PROTECTION FROM ALIMENTARY SUPPORT CLAIMS

Alter ego trusts may be vulnerable to alimentary claims pursuant to article 684 CCQ.

Married or civil union spouses (as well as former spouses subject to certain limitations), and relatives in the direct line in the first degree, may make a claim against the estate for alimentary support within six months after the death of the debtor, subject to the criteria set out in articles 684 and following CCQ.

Gifts (i.e. liberalities) made by the deceased may be taken into account when fixing the amount owed by the estate for alimentary support. With respect to gifts *inter vivos*, article 687 CCQ prescribes two limitations: a) only a claim by the deceased's spouse and children may take them into account and b) only gifts made by the deceased in the three-year period preceding his or her death are taken into consideration.

Therefore, the value of the capital of an *inter vivos* trust would be included in the calculation of the amount of the obligation of support, if the trust has been established within three years prior to the death of the deceased.

CONCLUSION

Given the advantages of having a notarial will (no probate) and the absence of probate fees (for witness and holograph wills) in Quebec, the limited protection from creditor claims, as well as the myriad tax pitfalls, the alter ego trust and joint partner trust are somewhat of a rarity in Quebec. Nonetheless, they may be useful devices in disability planning for the older person.

Should individuals who are 65 years and older establish an alter ego trust? The answer is not one-size-fits-all, but rather depends on a variety of factors such as the value of the estate, the kind of assets held, the province of residency and personal objectives.