TAB 10

Costs and Consequences - Avoiding the Pitfalls of Legacies and Bequests

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Costs and Consequences - Avoiding the Pitfalls of Legacies and Bequests

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Rosanne T. Rocchi[1]

INTRODUCTION

Several years ago my partner, Michael Kerr, and I were involved in a contentious proceeding regarding an estate. It was a much litigated estate despite the relatively small size of the estate. Based on our experience, we co-authored a paper entitled "Legacies: A Matter of Some Interest", which was published in two parts in the Estates and Trusts Journal.[2]

In the twelve years since the paper was written, the jurisprudence regarding legacies has not changed significantly. However, a review of the issue of legacies and bequests is pertinent for the following reasons:

1. Interest rates have dropped considerably with the result that it will not be possible in many instances to have the estate generate the type of income that is necessary to pay the appropriate rate of interest on unpaid legacies;

2. Multiple Wills have become popular in the last twelve years with the result that priorities between legacies and bequests must be freshly examined; and

3. Probate tax avoidance has spawned a number of "planning" techniques whereby property is held either in trust or in joint tenancy for the testator with the intention that the holder of such property either distribute the jointly held property or property held in trust on the same basis as that provided in the Will or take such property in satisfaction of the holder's interest in the estate. These planning techniques can render a Will unsuitable or cause abatement problems.

The first part of this paper will review basic principles relating to legacies and bequests using material largely from the co-authored paper where appropriate.

The second part of the paper will focus on the two trends noted in items 2 and 3 above with a view to assessing how the general principles relative to legacies and bequests are impacted by these trends.

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[1] Partner, Miller Thomson LLP. The first part of this paper has been based on a paper co-authored with Ms. Rocchi's partner, Michael W. Kerr, Partner, Miller Thomson LLP, for whose assistance and skills in contentious proceedings Ms. Rocchi continues to be most grateful.

[2] (1997) 16 E. & T.J 257 and (1997) 16 E. & T.J. 305

A. LEGACIES

The first part of this paper will examine three specific questions which frequently arise, creating vast amounts of litigation. All of these can be avoided at the time of receiving instructions for the Will:

- When are legacies payable?
- When does interest become payable on the legacies?
- At what rate is interest paid?

The decision in *St. Cyr v. Leitch*,[3] has complicated this matter. The case, however, has not been judicially considered since it was decided in 1992 and therefore stands as good law.

Before examining that case, it is useful to review the law of legacies in general and some of the problems that arise, either when solicitors fail to receive specific instructions as to payment of those legacies or when the estate cannot be administered in the manner intended.

1. Characterization of Legacies

Legacies are generally divided into two broad classes: specific legacies and general legacies. A demonstrative legacy is simply a form of general legacy with unique characteristics.[4]

Theobold stresses the importance of the characterization of a legacy succinctly:[5]

> This classification of legacies is important because of the doctrines of ademption and abatement. It may not be possible to give effect to a legacy because the subject matter of the gift is no longer available to satisfy it: in that case the gift is said to be adeemed. It may not be possible to pay all the legacies in full because the net estate available for distribution is too small to satisfy them in full, in that case some or all of the gifts must abate. The classification is also relevant in determining what income or interest is carried by a legacy and whether a legatee bears any expenses incurred by the personal representatives in preserving the assets.

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3 (1992), 37 A.C.W.S. (3d) 782, [1992] O.J. No. 2778.

4 *Halsbury's Laws of England*, 3rd. ed., vol. 16, paras. 609-11. There is some question as to whether a demonstrative legacy is to be considered a separate category of legacy. In *Walford v. Walford*, [1912] A.C. 658, Viscount Halding L.C. divided legacies into three categories: specific legacies, general legacies and "an intermediate class of legacy, namely, a demonstrative legacy, which is simply a general legacy, with the quality attached to it that it is directed to be paid out of a specific fund".

5 *Theobald on Wills*, 15th ed. (London; Sweet & Maxwell, 1993), p. 243.

(a) Specific Legacies

A specific legacy must be something forming part of the testator's estate. Specific legacies are usually referred to as specific devises or specific bequests because they are readily identifiable as an "item" of the testator's estate.[6]

Generally, a specific legacy is the gift of an identifiable asset. According to Theobald, a specific legacy is "a gift of a severed or distinguished part of the testator's property, thus showing an intention that the property shall pass to the legatee *in specie*".[7]

(b) General Legacies

A general legacy (sometimes called a "pecuniary legacy") need not be paid out of the testator's property existing at the date of death. It has no reference to the actual state of his or her property and is a gift of something which must be raised out of the general estate.

(c) Demonstrative Legacies

A demonstrative legacy consists of a gift of a specific amount of either money or stock, to be paid primarily, although not exclusively, out of a particular fund.[8] It is general in nature. Demonstrative legacies are paid first out of the specific fund allocated for their payment. If that fund is insufficient, the unpaid portion of the gift becomes a general legacy. If a deficiency exists, the balance of the demonstrative legacy abates rateably with the general legacy.[9]

2. Significance of Characterization

(a) Ademption

(i) General

Ademption occurs when an asset specifically bequeathed no longer exists at the date of death. Ademption will frequently defeat a specific legacy. A demonstrative legacy has an advantage over a specific legacy because it is not adeemed by a failure or deficiency of a fund out of which it is to be paid, but becomes payable out of the general estate, to the extent of such failure, *pari passu* with ordinary general legacies.

A practice point should be noted here. Many practitioners will discourage a testator from providing for specific legacies, since these gifts tend to engender disappointed

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6 However, there is jurisprudence to the effect that the gift of a fund in aliquot parts constitutes a specific legacy; see *Oliver v. Oliver* (1871), 11 L.R. Eq. 506; *McClellan v. Clark* (1884), 50 L.T. 616; *Page v Leapingwell* (1812), 18 Ves. Jun. 463, 34 E.R. 342; *Jeffrey's Trusts* (1866), L.R. 2 Eq. 68.

7 *Theobald on Wills*, p. 243

8 *Asburner v. Macguire* (1786), 2 Bro. C.C. 108, 29 E.R. 62. If the legacy is payable out of the particular fund alone, it is not demonstrative; *O'Connor (Re)*, [1970] N.I. 159; *Culbertson (Re)* (1967), 62 D.L.R. (2d) 134, 60 W.W.R. 187 (Sask. CA.).

9 *Acton v. Acton* (1816), 1 Mer. 178, 35 E.R. 641; *Walford v. Walford*, *supra*, footnote 10.

expectations and problems of construction. Indeed, as Theobald notes, "the Court leans against holding legacies to be specific".[10]

A Will, being ambulatory, operates on the property in existence at the date of death. If there is some lapse of time between the date of the Will and the date of death, it is quite possible that the property specifically bequeathed will no longer form part of the testator's estate. Given the probate-avoidance tendency to give away property before death or hold it in a "trustee" account, this is a current and widespread problem. This will result in ademption, causing disappointed expectations of the specific devisee, who is likely to cause the executors to seek an interpretation of the Will. The jurisprudence points out the need for careful and precise drafting to avoid costly Court applications.[11]

Another reason to avoid specific legacies is because the value of such legacies will often fluctuate considerably. Unless a Will is reviewed on a regular basis, this can be problematic because a testator's intentions can be defeated based on the value of the specifically bequeathed property.

(ii) Saving Specific Legacies

Specific rules exist in the *Succession Law Reform Act (*"SLRA"*)*[12] to save a specific legacy where security or proceeds of sale exist which would permit a Court to construct a tracing remedy for the disappointed specific legatee. However, these instances are limited.

Section 20 of the SLRA provides as follows:

> 20.(1) A conveyance of or other act relating to property that is the subject of a devise, bequest or other disposition, made or done after the making of a will, does not prevent operation of the will with respect to any estate or interest in the property that the testator had power to dispose of by will at the time of his or her death.
>
> (2) Except when a contrary intention appears by the will, where a testator at the time of his or her death,
>
> (a) has a right, chose in action or equitable estate or interest that was created by a contract respecting a conveyance of, or other act relating to, property that was the subject of a devise or bequest, made before or after the making of a will;
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> (b) has a right to receive the proceeds of a policy of insurance covering loss of or damage to property that was the subject of a devise or bequest,

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[10] *Theobald on Wills*, p. 444, citing *Rose (Re)*, [1949] Ch. 788; *Harrison (Re)*, [1976] N.I. 120.

[11] See in particular *Rose (Re)*, *supra*, footnote 10, and *O'Connor (Re)*, [1948] Ch. 628.

[12] R.S.O. 1990, c.s.26. This section does not assist with the current and wide-spread problem that occurs when a specific asset is either held jointly or transferred on an *inter vivos* basis in a probate fee avoidance scheme.

whether the loss or damage occurred before or after the making of the will;[13]

(c) has a right to receive compensation for the expropriation of property that was the subject of a devise or bequest, whether the expropriation occurred before or after the making of the will; or

(d) has a mortgage, charge or other security interest in property that was the subject of a devise or bequest, taken by the testator on the sale of such property, whether such mortgage, charge or other security interest was taken before or after the making of the will,

the devisee or donee of that property takes the right, chose in action, equitable estate or interest, right to insurance proceeds or compensation, or mortgage, charge or other security interest of the testator.

The section above applies only where the deceased has disposed of property and received something in exchange.

Frequently, assets are sold by an attorney pursuant to a general power of attorney for property, sometimes without knowledge of the impact the sale of the assets will have upon the incapacitated testator's testamentary wishes. While a Court appointed guardian is frequently made aware of the fact that the powers of an attorney or guardian do not extend to making a new Will for the incapacitated person or taking action which would affect the rights of any beneficiaries under the Will, this is a common practice and one which frequently leads to challenges.

(iii) Valuation

Finally, where the specific bequest is a gift of stock, the value of that stock may fluctuate sufficiently to be worth much more or much less than the testator had anticipated, thereby "skewing" the percentage benefit intended for that beneficiary. For this reason, the testator should be discouraged from specific bequests of portfolio assets. Rather, he or she should be encouraged to identify dollar amounts (or percentages up to a maximum value) as opposed to assets, when the intention is simply to give a financial benefit. Does the nature of the financial benefit really matter to the testator? Frequently, a specific bequest of stock, particularly if it has appreciated, will benefit the specific beneficiary greatly — once again, at the expense of the residuary beneficiary.

If stock is specifically bequeathed and has appreciated significantly since the date of acquisition, the estate will incur a taxable capital gain on the date of death if the specific legatee is someone other than the spouse. However, the Will will likely provide that all taxes are to be paid out of the general estate, thereby reducing the value of the residue.

Testators are often not advised of the incidence of taxation that may reduce the ultimate benefit to the residuary beneficiary. It is arguably much easier to do as the testator

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[13] For a detailed discussion on the complications that arise with respect to tracing assets and insurance proceeds see *Re Clements Estate*, (2007) N.S.S.C. 168 (CanLII).

instructs. However, a client is often best served by resisting the temptation simply to follow instructions.

The impact of taxation on the residue of the estate can be considerable. Since the residue of the estate is generally left to the individual who is most important to the testator, practitioners ought to carefully review with the testator the net value of the estate, taking into account the incidence of taxation.

(b) Abatement

(i) *Legacies Before Residue*

Legacies are paid in priority to the residue of the estate. The solicitor should point out that legacies may deplete the testator's estate because the residue bears the costs of the estate administration, as well as the taxes and debts. Given the inveterate practice of testators to overstate their assets and understate their liabilities, the net value of the estate available for "planned" gifts is often ambitious. Into this must be factored the testator's lack of knowledge of the costs of administration, including probate fees, legal fees and executor's compensation.

Consequently, a solicitor taking instructions for a Will must be careful to ensure that the testator is aware of the real possibility that those intended to benefit most substantially may not do so. A residuary legatee is entitled to nothing until all the legacies have been paid. Any loss in value of assets after the testator's death will also fall upon the residue.[14]

A more detailed discussion of abatement follows in the next section.

(ii) *Payment of Legacies*

Legacies are paid when the estate is ready to be distributed. At the end of the executor's year, the Court presumes the estate to have been fully administered and ready for distribution.

B. RIGHTS TO INCOME AND INTEREST PENDING PAYMENT OF LEGACIES

1. Income and Expenses Relating to Bequests and Legacies

(a) General

Generally, the cost of administration of an estate (which is generally charged against the general estate) includes costs of gathering all assets and sometimes the payment of duties in any foreign jurisdictions. However, once the asset has been situated, *Theobald* notes that "all costs incurred in perfecting the title" or "transferring stocks and shares must be borne by the specific legatee".[15] These expenses would also include insurance pending transfer and the costs of any safekeeping pending transfer to a

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[14] *Widdifield on Executor's Accounts*, 4th ed. (Toronto; Carswell, 1944), p. 185.

specific legatee. These costs also arise in connection with legal fees and disbursements necessary to transfer title to the specific devisee.

Where a beneficiary requests that cash legacies be paid elsewhere than when the assets are being administered, that legatee must pay the cost of remittance, wire transfers and bear any exchange rate differentials.

(b) Specific Legacies

A specific legacy of stock or other income-producing property, carries with it the dividends or other income which accrue from the date of death.[16] The converse should be true. That is, any carrying charges resulting from, or directly attributable to, the asset which is the subject of the specific legacy should be charged against the income derived from the particular asset.[17]

(c) Charges Against Specific Legacies - Who Bears The Cost?

In an estate involving litigation that went to the Supreme Court of Canada, the administration of the estate was held in abeyance pending the determination of the court. The Will of the deceased provided for certain specific devices of real estate. The estate had virtually no debt. The real estate was mortgage free. However, over the ten year period taken to resolve the litigation, there was no agreement by the competing parties as to the appointment of an administrator pending litigation with the result that the administration of the estate was largely in abeyance. The specifically devised real estate was left unattended. It was not rented or put to use. Taxes were paid periodically on the properties but only when it appeared that the local authority was about to seize the property for non-payment of taxes.

When the letters probate were eventually issued, an issue arose as to what charges were specifically chargeable against the real property. The issue was whether real estate which is the subject of a specific devise should bear the maintenance costs referable to its upkeep. This would involve the obligation to pay property taxes, insurance and maintenance of the property. Are these costs the obligation of the devisee or the residuary beneficiary?

The general rule concerning responsibility for payment of debts for the estate is set out in Section 5 of the *Estates Administration Act*.[18] This provides unless a contrary attention appears from the will or any codicil, the residue of the estate is liable for payment of debts, testamentary expenses and the cost and expenses of administration.[19]

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15 *Theobald*, page 816.

16 *Martin (Re)*, [1901] Ch. 370; *Mullins v. Smith* (1806), 1 Dr. & Sm. 204,62 E.R. 356.

17 *Theobald on Wills*, p. 816.

18 R.S.O. 1990, c.E. 22

19 *Re Grisor* (1979) 26 O.R. 57 where the specific legatees of a deceased son is incorporated business were entitled to have the debts of the business paid out of the residue of the estate.

5. Subject to section 32 of the *Succession Law Reform Act*, the real and personal property of a deceased person comprised in a residuary devise or bequest, except so far as a contrary intention appears from the person's will or any codicil thereto, is applicable rateably, according to their respective values, to the payment of his or her debts, funeral and testamentary expenses and the cost and expenses of administration.

Section 5 is subject to Section 32 of the SLRA, which provides as follows:

32.(1) Where a person dies possessed of, or entitled to, or under a general power of appointment by his or her will disposes of, an interest in freehold or leasehold property which, at the time of his or her death, is subject to a mortgage, and the deceased has not, by will, deed or other document, signified a contrary or other intention,

(a) the interest is, as between the different persons claiming through the deceased, primarily liable for the payment or satisfaction of the mortgage debt; and

(b) every part of the interest, according to its value, bears a proportionate part of the mortgage debt on the whole interest.

The general direction to pay debts does not represent an expression of a contrary intention.[20]

In *Feeney's Canadian Law of Wills*, the author notes that at common law a devisee of mortgage land took the land free and clear of any mortgages or charges.[21] This role has been reversed in Ontario and in most provincial Wills statutes. Section 32 states that where land is subject to a mortgage and the deceased has not, by Will, signified a contrary intention, the land is primarily liable for the payment or satisfaction of the mortgage debt.

In determining whether or not the specific devisee of real estate is responsible for charges and maintenance pending conveyance to the transferee, it is clear that unless the Will specifically provides otherwise, the devisee must take subject to the mortgage. However, subsection 32(4) of the SLRA contains an extended definition of the word "mortgage" and provides as follows:

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[20] Subsection 32 (2) of the SLRA provides as follows:

(2) A testator does not signify a contrary or other intention within subsection (1) by,

(a) a general direction for the payment of debts or of all the debts of the testator out of his or her personal estate, his or her residuary real or personal estate or his or her residuary real estate; or

(b) a charge of debts upon that estate,

unless he or she further signifies that intention by words expressly or by necessary implication referring to all or some part of the mortgage debt.

[21] *Feeney's Canadian Law of Wills*, (3d) Volume 2 at 179

> "mortgage" includes an equitable mortgage, and any charge whatsoever, whether equitable, statutory or of other nature, including a lien or claim upon freehold or leasehold property for unpaid purchase money, and "mortgage debt" has a meaning similarly extended.

Municipal taxes which are unpaid give rise to a lien. The view that a devisee of real property takes subject to unpaid taxes is supported by *Feeney's Canadian Law of Wills*, vol. 2 (3d ed.) at p.180, footnote 23 which reads in part as follows:

> "The SLRA and the *Uniform Wills Act* define a mortgage to include not only unpaid vendor's liens, but also other charges and liens similar in nature to a mortgage. This would appear to include such claims as arrears of taxes or bills for electricity and all other debts for which a statutory lien is created. (Emphasis added).

However where the taxes have been advanced by the estate or by any other person and are no longer owing to the municipality then they no longer constitute a charge against the land, but only a right *in personam* to reimbursement. As such, the amounts advanced on behalf of the beneficiary no longer fall within the purview of s.32 of the SLRA.

In conclusion, to the extent that carrying charges for specifically devised land constitute a "mortgage" for the purposes of s.32 of the SLRA, the real property interest is liable for the payment or satisfaction of the charges.

In the case involving the ten year period preceding the conveyance of the real estate, the specific devisees argued that the unpaid taxes ought to have been borne by the residuary beneficiary (who opposed the appointment of the Estate Trustee Pending Litigation) because the property had not been rented or put to use in the meantime. That is the corollary of a specific devise. That is, that any income earned as a consequence of the rental or production from the real estate is payable to the legatee.

Since the property could not be conveyed to the specific devisee without the payment of the tax arrears to discharge the lien, it transpired that the residuary estate bore the burden of these charges instead of the specific devisee. As a practical matter, however, that appeared to be inappropriate *quid pro quo* for the failure to render the real estate productive during the ten year period.

2. The Executor's Year

The general rule is that where no special time is fixed for payment of a legacy, it carries interest only from the expiration of the executor's year, whether the legacy is vested or not.[22] There are, of course, exceptions to the rule.

3. Exceptions to the General Rule

(a) Interest at an Earlier Date

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[22] *Scadding (Re)* (1902), 4 O.L.R 632, and *Widdifield on Executors' Accounts*, *ibid.*, p. 191.

There are four cases where interest on a general legacy runs from the date of death of a testator rather than from the first anniversary of the date of death:

1. where the legatee is an infant (but not a child of the testator) and the testator is in *loco parentis*;[23].

2. where the legatee is an infant child of the testator, interest is allowed by way of maintenance, unless the testator has otherwise provided for the maintenance of that child;[24]

3. where the legacy is in satisfaction of a debt of the testator,[25] and

4. where the legacies are charged upon land and no time is fixed for payment.[26]

(b) No Interest

In many instances, interest will not run where the testator gives the executor a discretion as to the time for payment of the legacy.[27] The Courts have consistently ruled that the testator can direct displacement of the general rule. Where the estate may comprise assets likely to be difficult to realize, the solicitor should suggest that the testator set a time beyond which the assets *should be considered* to have been converted with the result that the legatee would be entitled to interest.

Further, if the affairs of the testator are complicated and if the estate consists of assets which do not produce income or will not produce income proportionate to the value of the estate, perhaps the legatee ought to forego interest in favour of the life tenant of the residue. In the majority of estates, the testator's spouse is usually the life tenant and will depend upon the income for support. If questioned, the testator would probably prefer that the spouse receive the income generated by the estate before interest is paid on legacies. Since the Court will scrutinize the Will to see if the testator's intentions have displaced the general rule, it should be part of the solicitor's "checklist" to learn the testator's intention. The solicitor should question the testator on two salient issues - when should interest be payable on unpaid legacies and at what rate should that interest be payable? As a practical matter, it is a simple matter for the solicitor to insert a clause providing that no interest shall be payable on any unpaid legacies.

Given that the length of time for the administration of an estate and its ultimate distribution is becoming less accurate to predict given contentious issues arising from "calling in" the estate and determining which assets form part of the estate as a consequence of probate tax avoidance, it would not be unreasonable to provide as a general rule that no interest be payable on unpaid legacies until at least three years after the date of death.

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23 *Daly (Re)* (1926). 58 O.L.R. 301 (C.A.); *Murton (Re)* (1924), 26 O.W.N. 324.

24 *Ibid*.

25 Although this appears to have been alternatively decided on the basis that forgiveness of a debt is a specific legacy: *Wedmore (Re)*, [1907] 2 Ch. 277; *Watt (Re)*, [1958] O.W.N. 418.

26 *Shirt v. Westby*, 16 Ves. Jun. 393, 33 E.R. 1033.

27 See the discussion in *Daly (Re) supra*, footnote 19, discussed *infra*.

The other instance in which interest will not run is derived from the rule that a contingent legacy does not carry interest while it is in suspense.[28]

(c) Trust to Pay Income

When a trust to pay income is established, the right to income arises when the fund has been set aside. Interest is not payable until that time. This rule can be displaced by directions in the Will relating to periodic payments from a fund. Further, income from **a specific fund** will bear interest from the date of death, on the basis that the fund itself is a specific legacy. This was the case in *Nathanson (Re)*,[29] where it was held that income from a specific fund bears interest from the date of death.

In *Nathanson*, the trust arising from an aliquot share of a specific fund was considered to be a specific legacy and therefore subject to the general rule that a specific legacy will carry with it the income earned from the date of death.[30] *Re Nathanson* is an important decision because in that instance, two separate trusts were set aside as the primary vehicles to benefit the testator's spouse and the testator's children. The residue of the estate was to be divided between the spouse and the children as well. However, the decision of the testator to set aside a specific amount in the "spousal trust" and the "family trust" caused these trusts to be categorized as specific legacies. The testator had also provided for numerous other small trusts but they were not so characterized.

It is not clear how or why the trusts in *Re Nathanson* were determined to be a trust arising from an aliquot share of a specific fund. The two trusts provided in part as follows:

> (e) In trust to set aside, invest and keep invested the sum of Two Hundred and Fifty Thousand Dollars ($250,000.00) (hereinafter referred to as "my wife's fund") and to pay the net income thereof to my said wife, Irene Henrietta Nathanson, during the full term of her natural life, and until the said sum is so set aside and invested not longer than one year to pay to my wife out of my general estate interest from the date of my death on so much of the sum of $250,000.00 as is not invested at the rate of 5% per annum...**The setting up and establishment of my wife's fund shall be a first lien and charge upon my whole estate in priority to all other devises and bequests contained in this my will** but upon the setting aside of the same or the allocation of securities therefor the balance of my estate shall be released and discharged from the said lien and charge.
>
> (f) In trust set aside, invest and keep invested the sum of Five Hundred Thousand Dollars ($500,000.00) and until the death of my last surviving child to pay and divide the net income therefrom equally

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[28] *George (Re)* (1877), 5 Ch.D. 837 (CA.). Note, however, that the same rule does not apply to a defeasible interest.

[29] [1946] 3 D.L.R. 603,[1946] O.R. 421, [1946] O.W.N. 477.

[30] See *Page v. Leapingwell, supra*, footnote 6.

between my two daughters, the child or children of any deceased daughter to take its parent's share of such income…

The section noted in bold clearly indicates that the wife's fund was to have priority over all other benefits provided under the Will. As well, the wife's fund specifically addressed the issue of income being paid until the date of investment at the rate of 5%.

No such provision existed with respect to the family trust and yet the Court determined that this trust too would bear interest from the date of death, although at the rate of 4% rather than 5% because this was the rate considered to be appropriate for a trust invested in trustee investments.

(d) Legacies and Trusts for Children

It is not uncommon for grandparents or parents to direct that, before the bulk of the estate is set aside in a spousal trust, that funds be set aside for grandchildren or for children to be held in trust until a specified age. Those trust funds will qualify as a legacy which will bear interest from the date of death rather than from the time the trust is set aside. Usually, the right to income arises where the fund has been set aside and not before. Based on *Re Nathanson*, such funds will qualify as specific legacies and interest will run from the date of death.

Depending on the size of these funds, the interest to be paid until the fund is set aside can be considerable, particularly where the rate to be applied is 5%. For this reason, although such trust funds are generally not considered as legacies by many Will drafters, practitioners should be careful to ensure that language is inserted to direct that no interest or income shall be paid until the fund is set aside. Again, to prevent inordinate delay, after a certain point, interest ought to be payable if the fund has not been set aside after, for example, three years.

4. Procedures Before Payment

In administering an estate, it is necessary to characterize the legacies before determining what rule governs the income rights of the legatee.

Before making distributions, the executor must characterize the legacy and then determine whether interest is payable from the date of death, from the first anniversary of the date of death or from some later date. In some instances, if the Will provides, the Executor, may have a longer period of time than the executor's year, or the testator may direct that no interest be payable at all. This requires an examination of the terms of the Will and a knowledge of the general rules.

Again, it is critical that a solicitor specifically advert to these issues. Executors who pay interest when none is payable risk the possibility that the residuary beneficiary will complain and hold the executors personally liable for that improper payment.

5. The Rate of Interest

It has generally been assumed that interest on legacies in Ontario is payable at the "statutory rate" of 5%.[31] The rate is applied regardless of the actual rate of interest earned by the estate. Indeed, in Canadian jurisprudence there has been little (if any) attempt to link the issue of interest payable on legacies to the amount of income actually earned by the estate during the period when interest was payable to the legatee. In periods of high income, this will represent a windfall to the residuary beneficiary, who will have had the "notional use" of the legatee's money for at least the period of the executor's year. However, where the estate consists of unproductive assets, where the estate has had significant carrying charges or where the residue has been depleted by litigation, the actual rate of return to the estate may be less than the 5% allowed. In that instance, the legatees receive a benefit at the expense of the residuary beneficiaries.[32]

Additionally, where the estate earned a rate of return of less than 5% during a period when the legatees are required to be paid interest at the rate of 5%, the T3 Income Tax Return will be prepared on the basis that all the income is payable to the legatees. The executors may pay, say, $10,000 to the legatees on account of interest, but will issue a T3 Supplementary for only $5,000, being all the income earned. Since the estate will not have earned sufficient income to discharge the obligation to pay interest, the legatees will receive a portion of their interest out of capital, on a tax-free basis. In some instances, where the legacies are not payable until after the death of the life tenant, the legacies and the accrued interest will be paid entirely out of the sale proceeds of the asset charged with payment of the legacies. All the amount characterized as "interest" will be paid out as capital, with no tax consequences to the legatees at all.

This is an additional benefit to the legatees at the expense of the residuary or remainder beneficiaries.

Although perfect equity is impossible, the 5% rule has the benefit of being widely known and, by convention, understood by executors and their solicitors. Consequently, if assets cannot be realized in time to make the payments or if distribution is delayed,[33] investments can be selected to earn the rate known to be payable.

In the last two years, that planning and investment selection may not be possible given that any investments made by the Trustees pending distribution will likely be in the nature of short-term investments or GICs which are currently earning less than 1%.

The judgment in *St. Cyr v. Leitch* has called into question both the time at which interest on a legacy becomes payable and the rate of interest to be applied to compensate that legatee for the delay in payment. In times of high interest, the change in the rule represents a considerable benefit to the unpaid legatees. Now, when interest rates are

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31 For a detailed history and genesis of that convention see Rosanne Rocchi and Michael W. Kerr, *Legacies: A Matter of Some Interest*, (1997) 16 E. & T.J 257 and (1997) 16 E. & T.J. 305

32 The issue of a notional and assumed rate of return of 5% becomes especially fractious in the settlement of estate litigation, particularly when the cause of the delay and the reason for the unproductive state of the estate is occasioned by the same beneficiaries who are insisting on being paid interest.

33 Usually, pending issuance of a clearance certificate from Canada Revenue Agency

nominal, this change is a welcome relief to Trustees who have not been able to invest funds pending distribution in order to achieve the 5% rate of return.

6. The *St. Cyr* Decision

In *St. Cyr v. Leitch*, Mr Justice Hockin ordered that:[34]

> ... the legatees shall be paid in addition to their respective legacies of $75,000, simple interest at the "bank rate" as defined by s. 127 of the *Courts of Justice Act*, R.S.O. 1990, c. C.43 for the quarter ending June 30, 1992.

This was the first reported decision concerning the payment of interest on a legacy since the 1977 amendments to the *Judicature Act*,[35] which amendments significantly increased the entitlement to prejudgment interest and are continued in a modified form in the *Courts of Justice Act*.[36] Until those amendments, interest was awarded at a fixed rate of 5%, generally thought to be based on the rate specified in the *Interest Act*.

St. Cyr was an application for the advice and direction of the Court in relation to the administration of an estate. The testator died on November 14, 1990 and named his three children as executors. The applicant executors contended that their sister, Marjorie Leitch, refused to participate in the administration of the estate. One of the disputes concerned bequests to St. Peter's Basilica and St. Peter's Seminary Corporation, each in the amount of $75,000. The applicants wanted to pay the bequests but Leitch wanted the legatees to waive payment under the Will, in return for a payment by each of the executors personally out of the portion of the estate to which each of them as beneficiary, was entitled.

This structure would have resulted in the executors personally receiving the tax benefit of a charitable donation.[37] Mr Justice Hockin found no reasonable explanation for the delay in the payment of the legacies after April 28, 1992, some 18 months after the date of death. He found the delay was caused by the position taken by Leitch and ordered that interest was payable from April 28, 1992, by Leitch (the co-executor) personally.

The first issue was the date from which interest was considered to run. As the jurisprudence demonstrates, the general rule is that interest is payable on general legacies from the first anniversary of the date of death. Mr Justice Hockin selected April 28,1992, being the date of correspondence from the charitable legatee rejecting the structure proposed by Leitch. Under application of the general rule, the charity would have been entitled to interest for an additional six months.

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34 *Supra*, footnote 3, at p. 6 of the Judgment.

35 R.S.O. 1970, c. 228, as am. 1977, c. 51, s. 3.

36 R.S.O. 1990, c. C.43, ss. 127 and 128.

37 Presumably, the benefit of the charitable receipt to the deceased had been wholly or partially exhausted and any unutilized credits would not be of any use to the estate. The structure proposed by Leitch would have resulted in greater net tax savings to the beneficiaries and would be neutral to the charitable legatees.

Although the date from which interest was to run was deferred, Mr Justice Hockin ordered that interest be paid pursuant to s. 127 of the *Courts of Justice Act* at the "bank rate" for the quarter ending June 30, 1992. That rate of interest was 7.5% per annum.[38]

Mr Justice Hockin's decision deviated sharply from what was believed to be the rule; namely, that general legatees are entitled to be paid interest on their legacies from the end of one year from the date of the testator's death at the rate of 5% per annum, when no time for payment is fixed by the Will.

7. Is the *Courts Of Justice Act* Restricted to Contentious Proceedings?

The right to prejudgment interest in the *Courts of Justice Act* contemplates the defendant's having wrongfully withheld from the plaintiff funds which have, at least notionally, generated interest at current rates.

However, the *Courts of Justice Act* contemplates both a cause of action having arisen and an action having been commenced, as condition precedent to the entitlement to interest. In most estate administrations, there is no proceeding and the executors are simply administering the estate. It would be bad policy to encourage legatees to commence an action to recover their delayed legacies, principally on the basis that their interest entitlement would be enhanced by the very commencement of that action.

The U.K. has dealt with this issue in part by legislation. Judgments on legacies are treated in a different manner from judgment debts and are subject to a fixed rate of interest. Order 44, Rule 10 of the *Proceedings Under Judgments and Orders: Chancery Division* (Supreme Court Practice, 1995) provides:

> Where an account of legacies is directed by any judgment, then, subject to any directions contained in the will or codicil in question and to any order made by the court, interest shall be allowed on each legacy at the rate of £6 per cent.[sic] per annum beginning at the expiration of one year after the testator's death.[39]

According to *Williams, Mortimer and Sunnucks on Executors, Administrators and Probate*, Rule 10 applies to accounts directed by a judgment, but should obviously be followed in administrations out of court.[40] The editors implicitly support Mr. Justice Hockin's approach in *St. Cyr* by referring to the U.K. prejudgment interest legislation that pre-dated the introduction of Rule 10:[41]

> Until the implementation of Section 15 of the *Administration of Justice Act*, 1982, the courts had no jurisdiction to award interest on claims or debts

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38 Counsel in *St. Cyr* confirm that they did not address the line of cases that hold that interest at 5% per annum is appropriate.

39 There have been no changes since the section was originally enacted in 1995.

40 *Williams, Mortimer and Sunnocks on Executors, Administrators and Probate Williams, Mortimer and Sunnocks on Executors, Administrators and Probate (London, Steven & Sons, 1993), p. 1035.* (London, Steven & Sons, 1993), p. 1035.

41 *Ibid.*

other than judgment debts. There is now wide discretion subject to rules of court.

The rate of interest on judgment debts is regulated by statutory instrument under Section 44 of the *Administration of Justice Act*, 1970 and in the case of County Courts under Section 74 of the *County Courts Act*, 1984, where an estate is being administered in the High Court, it is thought that, the court would now act by analogy to these statutory rates and that therefore **representatives acting in an administration out of court should follow the same or similar rates or the rate received under the Court's short-term investment account.** [Emphasis added.]

It appears, therefore, that in the U.K. there is some doubt as to whether the personal representative should pay interest at the fixed rate of 6% or at a fluctuating rate. *St. Cyr v. Leitch* has not been judicially considered but in the past twelve years, its significance is becoming more relevant. At the time, the interest rate under the *Courts of Justice Act* was 2.5% higher than the 5% rate which is the general rule. Since that time, interest rates have plummeted. Consequently, in 2009, it would be preferable if personal representatives could pay the pre-judgment interest rates which, currently is 0.5%.

Since there is presumably some nexus between the rate set as pre-judgment interest rates and the presumptive rate of return for short-term investments, it is open to argue that the *St. Cyr* decision supports this position.

So, for example, if legatees of unpaid legacies demand the standard 5% rate of interest on unpaid legacies, it is arguable for personal representatives to take the position that, unless the assets which are held pending payment of the legacies are producing a greater rate of return, the rate used should be the rate for pre-judgment interest. Attached as Schedule "A" is the table showing the post-judgment and pre-judgment interest rates under the *Courts of Justice Act* from 1989 to 2009.

We note, however, that another section of the *Courts of Justice Act* relates to monies paid into Court. The rate of interest paid on moneys paid into Court is provided for in R.R.O. 1990, Reg. 190, s.2(4), which provides as follows:

2(4) Money paid or transferred to the Account bears interest on the minimum monthly balance,

(a) in the case of money held for a minor, at the rate of 5.6 per cent per year, compounded semi-annually;

(b) in the case of all other money, at the rate of 2.75 percent per year, compounded semi-annually.

These rates are exceptionally high given current interest rates for short-term investments.[42]

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[42] These rates have not changed in twelve years.

C. ABATEMENT OF LEGACIES

1. Introduction

The concept of abatement is important. It applies where the assets of an estate are insufficient to meet all the debts, taxes and other obligations. In the normal course, a testator is presumed not to anticipate that there will be a deficiency in the estate.[43] Otherwise, a testator would not provide a Will which was bound to be adjusted. However, in the normal course it is difficult to anticipate when assets will be insufficient. Abatement generally occurs where a testator has made a number of bequests and left a very small residue which is insufficient to discharge all the obligations. This will happen if a testator has not reviewed the Will on a regular basis to keep track of the appreciating value of certain assets and the tax consequences that are going to arise on death. While abatement does not often occur, it is becoming more frequent due to the trend to disposing of assets prior to the date of death resulting in significant taxes payable on death with insufficient assets left to be disposed of through the Will.

2. Priority of Abatement

The case of *Re Legge Estate*[44] is often cited as the leading Canadian case for the summary of rules regarding abatement of legacies.[45] The gifts under a Will will abate in the following order:

1. Residuary personalty;

2. Residuary real property;

3. General legacies, which include pecuniary bequests from the residue;

4. Demonstrative legacies, that is bequests from the proceeds of a specific asset or fund not forming party of the residue; [See *Culbertson v. Culbertson* (1967), 62 D.L.R. (2d) 134 (Sask. C.A.).]

5. Specific bequests of personalty; and

6. Specific devises of real property.

Re Legge Estate was a decision of the Nova Scotia Supreme Court in 2001. However, a Saskatchewan Queen's Bench decision in 2000 noted that there is a gloss to be placed on the abatement rules. This represents a change to the third rule relating to general legacies.

In *Mickler v. Larson-Shorten*[46] the testator provided for a specific devise of a residence to his daughter, Lois and a legacy of $10,000 to Juliette Mickler. In the normal course,

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[43] See discussion on *Mickler v. Larson-Shorten, infra.*

[44] 2001 NSSC 156, 203

[45] *Widdifield on Executors Accounts* contains a summary on page 5-36 paragraph 5.2 regarding abatement of legacies.

a legacy of $10,000 would be considered a general legacy; the gift of the residence would be a specific devise of real property and the last to abate. However, in this Will, the testator had provided clear language that the pecuniary legacy was to take priority over the specific devise. The Court noted as follows:

> General legacies abate *pro rata*, however, there may be circumstances under which a general legacy is given a priority of payment... *Feeney, supra,* at §8.54 outlines circumstances in which a general legacy will be given priority of payment as follows:
>
> > §8.54 Sometimes a general legacy may be given by the will priority of payment over another general legacy or legacies and then of course the *pro rata* rule is displaced by the testator having shown a contrary intention, but this must be absolutely clear. Such words as "to be paid immediately after my decease out of the first moneys belonging to me" will not give a legacy priority and save it from abatement. The reason is that the testator, in the absence of clear and conclusive language to the contrary, must be deemed to have considered that the estate would be sufficient and consequently not to have thought it necessary to provide against a deficiency by giving priority.
>
> The general legacy of $10,000.00 is given priority of payment by the will due to the clear and conclusive language of the testator. In the construction of the Will, the testator identifies the general legacy to Juliette Mickler in clause 2(c) before any other legacies and, in addition, begins clause 2(d) with the preface "subject to clause 2(c) hereof". The ordinary meaning of thee words places the fulfilment of clause 2(c) in priority to clause 2(d). Due to the construction of the will, clause 2(d) intended to place the general legacies to Juliette Mickler in a priority position over the general legacy to Lois Larson.[47]

The entire Will was not detailed in the case but it is noteworthy that the testator can always displace the specific rules of abatement. Nevertheless, as the Court noted, a testator does not assume that there will be insufficient assets and therefore it is often difficult to draft a Will to take account of this possibility.

Mickler v. Larson-Shorten is also notable because the Court directed that the sum of $10,000 be paid to the legatee within sixty days out of the proceeds of sale of a residence. If payment was delayed beyond sixty days, the Court noted that "interest shall accrue at the rate in force pursuant to *The Pre-Judgment Interest Act*". This is consistent with the *St. Cyr* decision discussed above. The testator died on January 27, 1999 and judgment was given on October 13, 2000, some eight months after the

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[46] 2000 SKQB 426 (CanLII)

[47] 2000 SKQB 426 (CanLII), para 11 and 12

anniversary date of death. The anniversary date of death as the commencement date for the running of interest appears to have been ignored.

3. Abatement by Advancement - Presumption Against Double Portions

There is a concept known as the "presumption against double portions" which is sometimes described as "abatement by advancement". We noted earlier that abatement occurs when the assets of the estate are insufficient to discharge all the benefits given under the terms of the Will. Abatement is also thought to occur in some instances where the beneficiary of an estate has been advanced during the testator's lifetime. This concept of abatement by advancement applies in very limited instances. It is described by *Feeney* as follows:

> §15.72 Some authors have expressed the doctrine of ademption by advancement in the form of a presumption, the "presumption against double portions. However expressed, the doctrine is very limited. It amounts to this: if, after making provision by will for the children (including any person to whom the testator stands in *loco parentis*); the testator then makes a substantial and similar gift *inter vivos* to one child equity will take care (in fairness to the other children) to see that the one who has received the *inter vivos* gift – the advancement – does not receive the gift again under the will. **Depending on the extent of the advance, equity presumes that the *inter vivos* gift was an advance of a part or of the whole of the donee's share of the will provision for children generally.** Accordingly, the court will reduce *pro tanto* the will benefit of the child who received the *inter vivos* gift. The notion of advancement, or at least the presumption of advancement, is currently being questioned by the courts.[48] [Emphasis added.]

The rules regarding ademption by advancement or the presumption against double portions are exceptionally complex. *Feeney* notes that the limited relevance of these concepts ought to be reviewed again in the context of the Supreme Court of Canada decision in *Pecore v. Pecore.* Since the *Pecore* decision dealt extensively with the presumption of advancement and the presumption of resulting trust, the concept of ademption by advancement ought to be reviewed. He notes as follows:

> The tendency is to treat the presumption [against double portions] as a basis for examining all evidence to rebut the also so-called presumption of resulting trust. In *Pecore*, the Supreme Court of Canada made it clear the standard of proof to rebut this presumption and the competing presumption of resulting trust is the ordinary civil burden of the balance of probabilities…
>
> On balance, given the emphasis that the decision appears to give to the presumption of resulting trust, it might have been a preferable move to dispense with the presumption of advancement in its entirety.

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[48] *Feeney*'s *Canadian Law of Wills*, at para 15.72.

Given that the concept of the presumption against double portions is related to the presumption of advancement which has been modified extensively by the Supreme Court of Canada, *Feeney* concludes that this presumption which would result in abatement by advancement has little relevance.[49] He notes at paragraph 15.73:

> §15.73 The doctrine is restricted to the above special circumstances, that is, where a will-maker makes a will provision for children and subsequently makes an *inter vivos* advance to one or more of them. It is not, and falls far short of, a general rule preventing a person from claiming additional benefits under a will after having received benefits, however similar, from a will-maker during the latter's lifetime. **Given even the exceptional circumstances in which the doctrine does apply, the presumption is one which is quite easily rebutted**. There will be no ademption if there is sufficient evidence to show that the testator intended the child to receive both benefits. If there is such evidence, then the child who received the additional benefit may keep it and still be entitled to an equal share with the other children under the will.
>
> Specific provisions in wills should prevent the application of the presumption. In *Johnston Estate*, the provision in the will read:
>
> > 10.1 None of my beneficiaries shall be liable to bring into account any money, or the value of property, which I may have transferred to any of them prior to my death, unless I have indicated in writing at the time of the transfer that it is not to be a gift.
>
> The court had no doubt that this provision was effective to oust any application of the presumption.[50]

The view that the presumption against double portions is not relevant in Ontario is echoed by yet another author. In *Oosterhoff on Wills and Succession*, the author notes as follows:[51]

> Sometimes a parent makes a substantial *inter vivos* gift to a child with the intention that the gift shall be taken into account in determining the child's share in the parent's estate. If the parent then dies testate, this will occur if the will provides that the gift be taken into account or be brought into hotchpot or if the rule against double portions applies. If the parent dies intestate, there are statutory provisions contained in section 25 of the *Estates Administration Act*.[52]

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[49] See also the observations of Marni M.K. Whitaker in "Hotchpot Clauses", Estates and Trusts Journal, Volume 12, page 7 in which the author notes that the presumption against double portions may not be relevant in Ontario except cases of intestacy.

[50] *Feeney's Canadian Law of Wills*, para 15.73.

[51] *Oosterhoff on Wills and Succession* (5th Edition), Carswell at p. 87

[52] Section 25 of the Estates Administration Act provides as follows:

The author also examines this issue further at p. 552 as follows:

> It is a rule of equity that if a testator has given a legacy or property of a substantial nature to a child and subsequently transfers the money or the property or the equivalent value to that child, the legacy has been satisfied. This rule, often called the rule against double portions, is really a sub-rule of the doctrine of satisfaction.

In support of this, the author cites the case of *Re Georges Will Trusts*[53]. In that case, Jenkins L.J. cited the principles upon which the rule is based, as stated by Lord Greene M.R. in *In Re Vaux*[54]. Lord Greene M.R. stated as follows:

> The rule against double portions rests upon two hypotheses:
>
> First of all, that under the will the testator has provided a portion and secondly, that by the gift *inter vivos* which is said to operate in ademption of that portion either wholly or *pro tanto* he has again conferred a portion. The conception is that the testator having in his will given to his children that portion of the estate which he decides to give to them, when after making his will he confers upon a child a gift of such a nature as to amount to a portion, then he is not to be presumed to have intended that the child should have both, the gift *inter vivos* being taken as being on account of the portion given by the will. When the word "portion" is used in reference to the gift *inter vivos*, it has a qualitative significance in this sense, that **it is not every gift *inter vivos* that will cause the rule to come into operation. If the testator gives to a child as pure bounty and by way merely of a present a sum of money, that will not have**

Cases of children advanced by settlement, etc.
25.(1) If a child of an intestate has been advanced by the intestate by settlement or portion of real or personal property or both, and the same has been so expressed by the intestate in writing or so acknowledged in writing by the child, the value thereof shall be reckoned, for the purposes of this section only, as part of the real and personal property of the intestate to be distributed under this Act, and if the advancement is equal to or greater than the amount of the share that the child would be entitled to receive of the real and personal property of the intestate, as so reckoned, then the child and his or her descendants shall be excluded from any share in the real and personal property of the intestate.

If advancement is not equal
(2) If the advancement is less than the share, the child and his or her descendants are entitled to so much only of the real and personal property as is sufficient to make all the shares of the children in the real and personal property and advancement to be equal, as nearly as can be estimated.

Value of property advanced, how estimated
(3) The value of any real or personal property so advanced shall be deemed to be that, if any, which has been acknowledged by the child by an instrument in writing, otherwise the value shall be estimated according to the value of the property when given.

53 [1949] Ch. 154 [1948] 2 All E.R. 1004 Chancery Division

54 [1939] Ch. 465 at 481

> **the character to cause the rule to come into operation**. Similarly there may be various reasons why the testator should give property to a child. He may wish to free him from some embarrassment, or something of that kind. In cases of that sort upon the facts a gift may not be apportioned at all, in which case, of course the rule does not apply.

The section noted in bold specifically references the fact that the so-called presumption against double portions has so many exceptions, that it can rarely be relied upon as a rule which will operate to either equalize beneficiaries or claw-back assets into the estate. Indeed, the presumption against double portions which will result in ademption by abatement is, in many respects, simply a method of determining whether property was given to a prospective beneficiary as a gift or as a loan. The concept is further discussed in the section dealing with hotchpot.

4. Adding Back Assets to the Estate – Claw Back Issues

If there is no such concept as a presumption against double portions in Ontario, and if as *Feeney* notes, the whole concept ought to be reviewed in the context of *Pecore v. Pecore*,[55] then a recent Ontario case is helpful to a certain extent in determining when assets will be repatriated into an estate. In this case, there was no discussion about the concept of double portions. Rather, the numerous gifts to various children were examined in the context of the presumptions of resulting trust and the presumption of advancement as discussed in *Pecore v. Pecore*.

Videchak v. Giarratano is a 2009 decision of the Ontario Superior Court[56] which involves the "restitution" of an estate by clawing back assets that had been given away or held in trust by certain beneficiaries.

The case dealt with the Giarratano family which comprised a mother (Christina) and four children, Anna, Nina, Lou and Joe. Three of the children were already actively involved in family matters. The fourth was not. The mother died on August 18, 2003 leaving a Will to be divided among her issue in equal shares per *stirpes*. During her lifetime, she had transferred certain funds to three of the children. The issues to be determined were whether the transfers were gifts or intended as a loan. In determining these issues, the Court relied heavily on the *Pecore v Pecore* decision.

The specific issues and the findings were as follows:

1. Did a mortgage of $56,000.00 in favour of the deceased constitute a gift to Nina or an asset of the estate? The Court found that the mortgage granted in 2001 was a gift to Nina and was her property.

2. Did the sum of $40,000.00 paid Joe constitute a gift, was it held as a resulting trust, or was it an asset of the estate or brought into hotchpot on the distribution of the estate? The advance was made in 1991. The Court found that Joe had failed to meet the burden of proof in rebutting a

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[55] 2007 Supreme Court of Canada 17(CanLII) [2007] 1 S.C.R. 795.

[56] 2009 CanLII 29914 (ON S.C.)

presumption of resulting trust and directed that he pay the "$40,000.00" to the estate.

3. Did a joint bank account between the deceased and Anna pass beneficially by right of survivorship, was it held as a resulting trust or was it held as an asset of the estate? The Court found that there were no bank documents to support the position that there was a gift. Mr. Justice Matheson noted as follows:

   "It is well known that elderly people have a joint bank account in order to make sure that debts are paid on time and to ease the pain of probate. The Courts have said that there is still an onus on the person trying to benefit because of this."[57]

   Justice Matheson then directed that "the amount of funds in the joint account will be part of the residue of the estate." This presumably included any interest that had been earned in the joint account from the date of death to present.

4. Does a GIC jointly held by the deceased and two of the children pass beneficially by right of survivorship, is it held as a resulting trust and/or is it an asset of the estate? The Court distinguished between a bank account and a GIC stating that GIC "is different from a bank account because it is basically a savings item and not to be used to pay ongoing debts. In my opinion, this document speaks for itself and the owners of it at the death of Christina are Nina and Joe."[58]

(a) Interest on Loan or Advance

The decision did not deal with whether or not interest was to be repaid in the case of the $40,000.00 paid to the son and noted in item 2 above. There was no discussion as to whether or not this amount could be traced. As a practical matter, it appears that $40,000.00 was used by the son in his business but the evidence is sketchy on this. However, since the advance was made in 1991 and the decision was made some 18 years later, a direction to return only $40,000.00 would appear to be a benefit to the son. The decision was also made some six years after the date of death so that the absence of any accounting for interest ought to be considered a considerable benefit to the son.

(b) Hotchpot

It is interesting that Justice Matheson questioned whether or not the $40,000.00 advance was to be brought into hotchpot. No such alternative was available for the other three assets considered. This is important because there is no indication as to whether or not the Will contained a hotchpot clause.

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[57] 2009 CanLII 29914 (ON S.C.) at paragraph 47 on page 9

[58] 2009 CanLII 29914 (ON S.C.) at paragraph 49 on page 9

So, for example, despite the fact that the Will provided for the children to be treated equally, one daughter received a mortgage of $56,000.00 and 50% of a GIC, one son received an additional 50% of the same GIC and there was no discussion as to whether or not those amounts ought to be taken into hotchpot.

This case is also important because it points out the expense created by holding property in joint accounts and making advances without addressing the issues in the Will.

D. HOTCHPOT CLAUSES

The concept of a presumption against double portions arose because of the equitable concept of treating beneficiaries equally, particularly where a Will provided for such equal treatment.

It is fair to say that in most instances, parents will wish to treat their children equally. However, clients rarely volunteer information about benefits given to children during their life, unless those benefits are significant. Practitioners should specifically address such issues as they are certain to arise in the context of the estate administration if one child has been significantly "advanced" by the parent.

It appears that unless a testator specifically includes a provision for equalization of children, the so-called "presumption against double portions" will not assist and it is therefore necessary for practitioners to be familiar with the concept of hotchpot.

The word "hotchpot" is used to describe a type of claw-back whereby property belonging to other individuals is aggregated with a view to bring into account the division of estate assets which have been made previously to them.

A knowledge of hotchpot is a concept for which many estates solicitors are familiar only in a general fashion. For a detailed review on the history of hotchpot clauses, there are several articles which address the history of the concept and some of the problems associated with the drafting of a proper hotchpot clause.[59]

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[59] See Marni M.K. Whitaker "Hotchpot Clauses", Estates & Trusts Journal, Volume 12, page 7; Corina S. Weigl, "Hotchpot Clauses – A Primer", 4th Annual LSUC Estates & Trusts Forum, November 20 & 21, 2001; and Anne Werker, "It's a Gift! It's a Loan! It's an Advancement!", the Probater, Hull & Hull, Volume 9, Number 4, November 2005, for detailed discussion and practice advice regarding these issues.

1. Drafting Issues for Hotchpot Clauses

Let us assume that a testator has advanced funds to his children during his life and wishes to have all the children equalized at death. In a simple situation, we will assume that there is no surviving spouse so that the Will simply provides that the residue of the estate be divided equally among the children with a hotchpot clause which directs that all advances and loans should be taken into account whether such advances or loans are made before the date of the Will or after the date of the Will.

This particular clause is the general hotchpot clause but is not sufficiently specific. The word "advances" is vague. Similarly, it is probably not intended that all gifts and loans made to children be included or added back. As a consequence, a hotchpot clause should deal specifically and in detailed fashion with advances that have been made. If possible, it is preferable that the testator either specifically list such advances or provide a detailed list as was the case in *Re Barrett*, noted below.

The complexities of a properly drafted hotchpot clause will also involve consideration being given to the timing of certain advances and whether or not interest is to be applied to those advances.

These issues were considered in the Alberta case of *Re Barrett Estate*[60]. The facts are described as follows:

> The deceased, Dwight Wesley Barrett, died on March 11, 1999. In Clause 6 of his Will (signed on February 7, 1992), he gave his Estate to his three sons (Bernard, Darrell and John Barrett) to be shared equally, "*taking into account amounts lent or given to each of my sons as per the attached list by myself or my wife and adjusted to present value at the date of my death using the Consumer Price Index as an inflation factor*". One list, in the deceased's handwriting, was made before execution of the Will ("Pre-Will List"). Two other lists, one in the deceased's wife's (Bernice Barrett's) handwriting and one in the deceased's handwriting, were made after execution of the Will ("Post-Will Lists"). Due to disagreement among the sons, the Court must resolve which lists of loans and advances are to be considered as forming part of the Will and which lists are to be considered in the distribution of the Estate.[61]

The Will contained a very specific hotpotch clause. It is also worthy of note that the amount to be taken into hotpotch did not include an interest factor but was to be adjusted to take into account inflation. The mechanics of a hotpotch clause are often difficult and issues arise as to whether or not the child who has been advanced ought to account for the early inheritance by way of interest or some other method of rectification. For example, a child who has received an advance by way of mortgage on a residential property may have a significant advantage depending on the real estate market. So, for example, a loan of $200,000.00 to purchase a residence in Toronto in

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[60] 2003 ABQB 986 (CanLII)

[61] at para 44 and 45

1980 would be very different from the provision of such loan for the cost of a house in 1995. As a result, something in the nature of an adjustment that more accurately reflects the purpose of the loan should be considered in a hotpotch clause.

In considering the effect of the hotchpot clause in *Barrett* the Court noted:

> The significance of a hotchpot clause, in identical Wills of a husband and wife, was dealt with by the Ontario High Court of Justice in *Re Prittie*, [1940] O.J. No. 29 (H.C.J.). The Court held that any gift or conveyance by the testator or his wife in their respective lifetimes, to or for the benefit of any child seeking a share of the residue of the testator's estate, must be taken into account. In *Prittie*, the testator divided his estate equally among all his children, but provided that any transfers or gifts made by the testator or his wife to a child, must be taken into account.
>
> The Court's comment at paras. 13 and 16 of *Re Prittie* on hotchpot clauses and the intention to be inferred from them is apt to this case:
>
> > As is the case with every hotchpot clause, the direction to take certain gifts to the testator's children into account in dividing the residue of the estate among them is an attempt to achieve equality ...
> >
> > It seems that, so far as the Will goes, his (the testator's) was plain: to equalize at the period of distribution of his estate, so far as the residue would extend, the shares his children received from their parents.[62]

The other issue to be addressed is the value to be taken into account at the period of distribution. Some hotchpot clauses will provide that the advance be taken into account on the date of death or at the date of distribution. In many instances where there is an intervening life interest, the attempt to achieve equality by having a child "account" for an advance could prove to be ephemeral if the time of distribution is some twenty years after the initial advance. Does the child account for the amount advanced or does interest become payable?

The *Barrett* case is also interesting because the Court found that a four page list which was called the "Pre Will List" was incorporated by reference and all transactions listed as adjusted to the date of death were to be taken into hotpotch. I note however, that the particular hotchpot clause asked for adjustment to the present value at the date of death as opposed to the present value at the date of distribution. The Court noted however that the Post Will List transactions were also to be taken into account and taken into hotpotch. The Court found that the obligation was on the part of the Administrator to establish that the transactions recorded did in fact occur. The Court noted that the Pre Will List could not be challenged because it was incorporated by reference.

2. Equalizing Legacies vs. Hotchpot Clauses

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[62] 2003 ABQB 986 (CanLII)

One of the difficulties with a hotchpot clause is that generally, it will only operate to equalize children where there is sufficient residue in order to permit the equalization. Consequently, if a child has been advanced to a significant extent and it is desirable to equalize that child with, say, two other children, the hotchpot clause will arrange for the initial advance to be brought into the Will, with or without some rate of adjustment to account for the use of the advance before the ultimate distribution of the estate. This adjustment can take the form of interest (but at what rate?) or it can be pegged to a cost of living allowance, as was the case in *Re Barrett*, discussed *supra*.

Because each "advance" will be different and the form of adjustment should be appropriate for each specific advance, it is best from a practitioner's perspective to recommend an equalizing legacy along with a hotchpot clause in order to use a belts and suspenders approach.

By using an equalizing legacy rather than simply a hotchpot clause, the testator ensures that he or she addresses in specific terms the precise amounts advanced to each child or those anticipated to be advanced. That will more precisely focus the testator's attention on benefits given to each child in an effort to equalize the children. Set out below is a form of "equalizing legacy" where a parent has advanced funds for the provision of a residential and a recreational property. The proposed clause has not been used and is a suggested draft for discussion purposes only.[63]

In the clause below, it should be noted that the legacy involves a forgiveness of a mortgage. A forgiveness of debt operates as a legacy and this is another issue to be taken into account in drafting advance and forgiveness clauses. In the clause noted below, it was noted that to avoid excessive matrimonial equalization, a mortgage had been given by the parents equal to the purchase price of the property.

In this fact situation, parents have advanced to a daughter sufficient funds to purchase both a residential property and a recreational property. They have taken a mortgage for the full amount. In the case of the two sons, the parents have not yet advanced any funds but have used the sum of $1.5 million as the benchmark for the equalization legacy on the basis that this was the amount used to fund the purchase of the daughter's residential property and recreational property.

1. I hereby declare that I or my said wife have either alone or together with one another granted or advanced to one or more of our children from time to time certain funds to permit such child to acquire an interest in a residential property or recreational property. It is our intention to ensure that each of our children has both a residential and recreational home. If my said wife predeceases me, I direct my Trustees to pay a legacy or legacies to one or more of my children in the following manner.

2. As to my son, A, my Trustees shall satisfy such legacy by:

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[63] The author specifically notes that any precedents provided ought to be used without guarantee and there is no representation that the clauses actually perform the function for which they were intended but are provided as guidance and for discussion purposes only.

(i) Paying to him a legacy in the amount which is calculated to be the difference between:

(A) the sum of $1,500,000.00; and

(B) the amount determined by my Trustees to be the value of his principal residential property at the date of my death; and

(ii) Forgiving any amounts due under any mortgage securing his principal residential property in favour of me or my said wife and by discharging such mortgage.

3. As to my daughter, B, my Trustees shall satisfy such legacy by:

(i) Forgiving any amounts due under any mortgage securing her principal residential property and recreational property in favour of me or my said wife and by discharging such mortgage.

4. As to my son, C, my Trustees shall satisfy such legacy by:

(i) Paying to him a legacy in the amount which is calculated to be the difference between:

(A) the sum of $1,500,000.00; and

(B) the amount determined by my Trustees to be the value of his principal residential property at the date of my death; and

(ii) Forgiving any amounts due under any mortgage securing him principal residential property in favour of me or my said wife and by discharging such mortgage;

5. (i) In calculating the value of any principal residential property, my Trustees shall include for each child the full value of any property owned by such child jointly or as tenants in common or by such child's spouse alone as if such child were the absolute owner of such property, if such property were acquired by such child or spouse with property acquired by gift, bequest, inheritance, loan or other advance provided by me or my said wife or any property from which such gift, bequest, inheritance, loan or advance can be traced.

(ii) The legacies hereinbefore provided in paragraphs 2, 3 and 4 shall be paid at such time or times as my Trustees consider advisable having regard to the needs of my estate and available funds to discharge such legacies. Such legacies shall not bear interest unless they or any part remains unpaid on the second (2nd) anniversary of the date of my death, in which case, such legacies or the amount thereof unpaid shall bear interest at the

rate of five per cent (5%) per annum from the second (2nd) anniversary of the date of my death to the date of payment.

6. If any of my children has predeceased me leaving issue him or her surviving and alive on the date of my death, I direct that the valuations be effected and the calculations be made as if such child had survived me and the legacy that would have been payable to such deceased child had he or she survived me shall be divided among such deceased child's issue in equal shares *per stirpes* and held upon the trusts, terms and conditions set out in this my Will.

7. It is my intention that, as between this my Will and my said wife's Will (the latter of which contains a provision analogous to this provision), the aggregate of the legacies received under both Wills shall not exceed the amounts set out above. If my said wife and I should die at the same time or in circumstances rendering it uncertain which of us survived the other, I declare that for the purposes of this paragraph of this my Will, my said Wife shall be deemed to have survived me and the legacies herein provided shall lapse and be of no effect to the extent that such legacies are fully discharged and paid out of the estate of my said Wife.

The precedent noted above contains some problems which may obviate against complete equality between and among the children. Because the benchmark of $1.5 million was the amount advanced for the daughter, cost of living and inflation will erode the value of that benchmark amount. To achieve more precise equality, the benchmark amount should be tied to a cost of living allowance or a consumer price index specifically related to real property.

Additionally, it is anticipated that in some instances, the fair market value of the property owned may exceed the proposed bequest. For example, if the daughter's real estate has appreciated in value so that it is now worth $2.5 million, the benchmark of $1.5 million allowed for the sons is significantly below the value of the daughter's. There is nothing in this particular clause that requires the daughter to "account" for the extra $1 million value by reducing her share of the residue by such amount.

This Will will need to be amended fairly regularly to take account of any changes in the children's circumstances so that if one has acquired a residential property and a recreational property, the legacy clauses can be adjusted accordingly. As well, the clauses may not be sufficient in and of themselves to account for complete equalization. With that in mind, a hotchpot clause should also be added in order to ensure as equal treatment as possible.

I have not dealt at all with some of the other issues that arise in the context of a hotchpot clause.

A hotchpot clause generally requires equalization at the time of distribution of the residue of the estate. Where there is an intervening spousal trust, it means that the children will have to wait until the death of a parent until equalization occurs. During

that period, the child who has been the beneficiary of the advance and who has knowledge of the fact that he or she will have to account at some point in the future, should give some thought to the type of equalization that will have to be made if the hotchpot clause includes a provision to account not only for the principal amount advanced but for any notional rate of return in the nature of interest or consumer price index increase.

Finally, hotchpot clauses are notoriously difficult in terms of equalization where a child in whose favour the advance has been made is no longer alive. This may work to the disadvantage of the deceased's child's issue if the funds advanced were used to purchase a residential property which is owned by the surviving spouse of the deceased and whose children have no guarantee that they will benefit eventually from the portion of their parents' estate that was left to the surviving spouse. For this reason, where clients have made advancements to children in significant amounts and where it is desirable to include a hotchpot clause, solicitors should give careful thought and spend considerable time on the details required to effect as precise an equalization as possible. If, after reviewing all the issues that needs to be taken into account in effecting that equalization, it may appear that the testator should consider advancing all children equally in his lifetime. In large estates this ought not to be a problem. However, in the vast majority of cases, *inter vivos* equalization will not be possible and therefore specific hotchpot clauses or equalization legacies will be necessary.

3. Avoiding Duplicate Legacies in Mirror Wills

You will see that the clause noted above also contains in paragraph 7 a clause designed to prevent multiple legacies.

4. Hotchpot Clauses and Trust Interests

It should be noted that if a testator has established an *inter vivos* trust and if some of the children are going to be benefiting under that *inter vivos* trust, a general hotchpot clause will not work to equalize these distributions for the following reasons:

1. A hotchpot ordinarily operates only on advances made by the testator or the testator and spouse if that is specifically referenced in the hotchpot clause. It will not operate on gifts or advances under an *inter vivos* trust unless the hotchpot clause specifically addresses this.

2. Even if a hotchpot clause is included to effect equalization between benefits given under the Will and benefits given under the *inter vivos* trust, there may be different distribution dates and timing issues which will complicate matters. For example, it is entirely likely that the assets under the Will might be distributed in advance of the assets in the *inter vivos* trust. Since the testator will not be able to impose any type of equalization regime on the Trustees of the *inter vivos* trust, this will create a conundrum for the Executors and Trustees of the Will under which distribution is directed to be equalized. Careful drafting is required where it is necessary to create these adjustments.

3. In any instance where there has been an estate freeze, particularly of a family business and where the common shares are held in a family trust, there will be instances in which it may be necessary for the practitioner to offer guidance to the testator who wants to treat the children more or less equally.

As a practice tip, practitioners should always ask about equalization of the children, not only through advances made *inter vivos* either by the testator, the spouse or through a family trust, but also through a family trust which is designed to be distributed either coincident with the distribution of the Will or after the distribution of the Will.

E. DISSECTING MULTIPLE WILLS – LEGACIES AND RESIDUE

1. General

In multiple Wills, each Will has the attributes of a complete Will. Each Will has a power of sale and power to pay debts clause; it may provide for bequests and legacies. Each Will will have a residue clause. However, unless the Wills are carefully drafted, issues will arise as to whether or not some gifts which appear to be residuary gifts are actually legacies. The significance of this is that, in the case of an abatement, legacies abate after residue. Consequently, it is necessary to determine in multiple Will situations whether or not one of the Wills actually operates as a separate fund rather than an estate. In other words, it is possible that the residue of one Will may not be a true residue but rather a legacy.

The possibility of abatement cannot be overstated. Because of the tendency to engage in probate avoidance techniques, a testator may transfer property to one or more family members when it appears that death will occur shortly. These transfers will often result in deemed dispositions which will be taxable in the year in which the transfer was made. Where death occurs in the same year and where assets have been transferred to family members outside the terms of the Will, the residue will frequently be far less than anticipated. The entire scheme of the Will can be unintentionally perverted by *inter vivos* transfers effected without legal advice and a review of the impact of these transfers on the testamentary dispositions.

2. Nomenclature - The Primary Will and the Secondary Will

There are varieties of nomenclature for multiple Wills. Some practitioners will refer to them as "Primary Wills" and "Secondary Wills". Others will refer to them as a "Residual Will" and "Special Will". Nomenclature could be important in determining the characterization of the gifts granted under each Will.[64]

3. Structuring to Avoid Gaps

It is far more complicated to draft a multiple Will than a single Will. Because there has been virtually no jurisprudence on the interaction of the two Wills or the interpretation of multiple Wills which contain conflicts or confusion, a practitioner must take special care to anticipate problems that can arise.

One of the issues that arises is how to define the assets that are to fall into each Will and how to ensure that there is no hiatus caused by conflicting inclusionary/exclusionary language.

Consider the following definitions for a Primary Will and a Secondary Will. The precedents set out below are not mine but it are good and very extensive:

> **"Primary Estate"** means the whole of my property of every nature and kind whatsoever and wheresoever situate, including any property over which I may have a general power of appointment, **but excluding my property comprising my Secondary Estate as defined in this Will;**

Note that the definition of the Primary Estate is very simple. It is to include everything except property that comprises the Secondary Estate. This is a preferred technique to have one Will operate as the "everything except" Will. The reason for this will become apparent.

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[64] Generally, it is considered that titles are not important and practitioners will include a statement in the Will to the effect that headings and titles are not to be construed as impacting upon the terms of the Will. However, if terms such as "Special Will" and "Residual Will" are used, it may be helpful in a Will interpretation in determining whether or not certain assets are to fall into one Will or the other. The fact that one Will is entitled "Residual Will" suggests that anything not otherwise disposed of ought to be disposed of through the "Residual Will".

"Secondary Estate" means:

(a) my shares, if any, in the capital of any corporation or corporations whose shares are not publicly traded and for which my Trustees determine a grant of authority by a court of competent jurisdiction is not required for the transfer, disposition or realization thereof (in this Will collectively referred to as the "Corporations"), those of my assets, if any, which are held in trust for me by any one or more of the Corporations, and all amounts owing to me from any of the Corporations;

(b) any interest I have in any partnership or joint venture for which my Trustees determine a grant of authority to my Trustees by a court of competent jurisdiction is not required for the transfer, disposition or realization thereof (in this Will collectively referred to as the "Partnerships"), those of my assets, if any, which are held in trust for me by any one or more of the Partnerships, and all amounts owing to me from any of the Partnerships;

(c) any beneficial interest I have in any trust for which my Trustees determine a grant of authority to my Trustees by a court of competent jurisdiction is not required for the transfer, disposition or realization thereof;

(d) any interest I have in any real property for which my Trustees determine a grant of authority to my Trustees by a court of competent jurisdiction is not required for the transfer, disposition or realization thereof;

(e) all articles of personal, domestic, household and garden use or ornament owned by me at my death wherever the same may be situate for which my Trustees determine a grant of authority by a court of competent jurisdiction is not required for the transfer, disposition or realization thereof;

(f)all unsecured amounts owing to me from any of my children, more remote issue or any other beneficiary named in this Will; and

(g) any other of my assets for which my Trustees determine a grant of authority by a court of competent jurisdiction is not required for the transfer, disposition or realization thereof.

It is my intention to include these assets and none other in my Secondary Estate;

In this particular format, the Primary Will is the "Probate Will". This is the Will for which a Certificate of Appointment of Estate Trustee will be sought and will probably deal with Ontario real estate and bank accounts and brokerage accounts for which the financial institution in question will require a Certificate of Appointment of Estate Trustee. The

Secondary Will clearly disposes of assets that need not be subject to probate and lists all those components of the testator's property that can be transferred without the need for probate.

Other forms of Will are more specific and therefore careful scrutiny of the language is needed.

Before moving on to the significance of legacies in the context of multiple Wills, I note two drafting points that should be clarified here.

(a) Broad vs. Specific Drafting

In the precedent noted above, the Primary Estate is what I would describe as "the general estate" and is very non-specific. It will include everything other than those assets which comprise the Secondary Estate.

The Secondary Estate is specific in that it includes only those assets enumerated and no others. The Secondary Will specifically states that it is to be a "limited" estate.

This is to be contrasted with other forms of multiple Wills which specifically exclude "named" assets from the Primary Will. The exclusion is significant. If the terms of the Primary Will and the Secondary Will are not identical, then the exclusion of certain assets can be problematic.

In the example set out above, the Primary Will contains no detail other than excluding everything that falls into the Secondary Will. It is therefore the Primary Will which receives everything else. If on the other hand very specific definitions are used (other than references to a Primary Estate and Secondary Estate), there is a possibility that there could be a hiatus between the definitions excluded in the Primary Will and the definitions included in the Secondary Will, resulting in an intestacy for assets which will fall into neither.

As a practical matter, it is unlikely that a Court would ever find that there would be an intestacy in a situation where a testator has not only gone to the trouble of making a Will but making multiple Wills. Nevertheless, in such circumstances, it is easy to make an error and it may be necessary to bring a motion for construction in order to determine which asset falls into which Will.

(b) Discretionary Issues and Identical Beneficiaries

The other point to note with this form of multiple Will precedents is the attempt is to exclude from the Primary Will almost everything that can be passed on without probate. For example, in paragraph (g) there is a catch-all clause. In this type of Will, because there is so much fluidity between the Primary Will and the Secondary Will, it would be dangerous to provide for different beneficiaries under each Will because it is unclear to which Will the assets will flow. As noted, paragraph (g) is a general catch-all definition and will very much depend upon the negotiations that the Executors might have with entities or institutions which would ordinarily require probate.

How does all this relate to legacies? As noted above, where one Will is clearly identified as a Residual Will and the other is identified as a limited or a Specific Will, it is likely that, depending on the other terms of the Will, any benefits given under the Specific Will will be considered legacies and any benefits given under the Residual Will will be considered "residue". Benefits received under the Specific Will will be considered legacies and not residue. The rules relating to interest and abatement will apply.

4. Payment of Debts and Taxes

Another stumbling block in the use of multiple Wills is the extent to which the burden of debts and taxes is thrown upon the assets of each Will. Set out below is the form of the power to pay debts and taxes which appears in the Primary Will used in the precedent above:

> Payment of Debts:
>
> (a) I direct my Trustees to pay out of and charge to the capital of **my general Primary Estate, my debts, funeral and testamentary expenses** and all succession duties and estate, inheritance and death taxes, whether imposed by or pursuant to the law of this or any other jurisdiction whatsoever, or income taxes which may be payable under the *Income Tax Act* or any similar legislation of any province or other jurisdiction in force from time to time, that may be payable as a consequence of my death or in connection with any property passing on my death (but not including any property transferred to or acquired by a purchaser or transferee upon or after my death pursuant to any agreement with respect to such property) and including any property which does not actually pass on my death but is merely deemed so to pass by any governing law (except as may be provided in this Will to the contrary) or in connection with any insurance or annuities on my life or any gift or benefit given or conferred by me either during my lifetime, survivorship, or by this Will, and whether such duties and taxes are payable in respect of estates or interests which fall into possession at my death or at any subsequent time. The income taxes payable out of my general Primary Estate do not include those payable as a result of an actual or deemed disposition of an asset of a separate trust, fund, part, or share of my Primary Estate after such separate trust, fund, part, or share of my Primary Estate has been set aside. Those income taxes are to be paid from the separate trust, fund, part, or share of my Primary Estate. Without limiting the generality of the foregoing, the income taxes payable as a result of the actual or deemed disposition after my death of any asset which had an accrued gain, the taxation of which was deferred by transferring it to my Spouse or by its vesting in a trust described in subsection 70(6)(b) of the *Income Tax Act*, shall be paid by my Spouse or out of the trust containing the asset, as the case may be. I hereby authorize my Trustees in their discretion to commute or

prepay any such taxes or duties. Any duties or taxes so paid shall be treated as an ordinary debt of my Primary Estate.

(b) I wish to advise my Trustees that I intend to include a similar provision in my Secondary Will and that **it is not my intention that my debts, including taxes, funeral and testamentary expenses which are to be paid as ordinary debts of my estate be paid twice**. Accordingly, subject to the provisions set forth in this Paragraph, **I direct my Trustees to determine, along with the Trustees of my Secondary Estate how my debts, including taxes, funeral and testamentary expenses which are to be paid as ordinary debts of my estate shall be allocated between my Primary Estate and my Secondary Estate. In the event the aggregate residue of my Primary Estate and my Secondary Estate is insufficient to pay all of my debts, including taxes, funeral and testamentary expenses, which are to be paid as ordinary debts of my estate, then in determining the order of abatement of my estate, I direct my Trustees, along with the Trustees of my Secondary Estate, to treat the gifts made by me in both this Primary Will and my Secondary Will which I intend to make, as gifts made in one Will and to establish the order of abatement of such gifts in accordance with the applicable law in the Province of Ontario**.

Paragraph (b) of this particular precedent is important because it clearly states that if the general estate for both the Primary and Secondary Estates are insufficient to pay all debts, then the two Wills are to be aggregated and treated as one Will. Without this provision, it is fair to say that confusion would result. I noted earlier that where one Will operates as disposing of the general estate and the other Will is limited, it is likely that any benefits given under the Specific Will will be legacies and the residue under the general estate will be considered to be the true residue. The result of that is that the residue under the general Will will abate first. In the clause noted above, the drafter has specifically stated that the two residue clauses are to be considered as true residue clauses and all legacies are to be aggregated and to abate in accordance with the usual rule as if the multiple Wills constituted one Will.

In the Wills anticipated by these precedents, the Executors are given broad latitude. However, in such a circumstances, it is absolutely critical that the beneficiaries of each Will be identical. Otherwise, the discretion to allocate not only assets but also expenses could result in the diminution of one estate to the detriment of the beneficiaries of the other.

5. Allocating Debts and Taxes to Each Will

Where there are multiple Wills with different beneficiaries, the power to pay debts and taxes can take a different form, with one Will operating as the "general estate" and another Will acting purely as a special estate, which is more in the nature of a specific Will providing for very specific and identifiable assets.

In certain cases, the power to pay debts and taxes clause provides that taxes payable as a result of the actual or deemed disposition on death should be paid by the estate into which asset falls. Set out below is another clause which sometimes appears in multiple Wills. In this instance, the clause throws upon each Will the obligation to pay taxes from any deemed dispositions on each specific asset.

> To pay out of the capital of my general Secondary Estate my **just debts (including any indebtedness for taxes,** interest and penalties under the provisions of the Income Tax Act (Canada) or of any Province, and all estate, legacy, succession and inheritance taxes and duties (all of which duties and inheritance taxes are hereinafter collectively referred to as "Death Taxes"), imposed by the law of any domestic or foreign jurisdiction whatsoever **that may be payable in connection with any property passing (or deemed to pass by any governing law) on my death with respect to my Secondary Estate**. In the event that my just debts and taxes that may fall due through my Primary Will are unpaid by reason of there being insufficient assets that devolve through such Primary Will to pay same, I authorize my Executors to pay such just debts and taxes from my Secondary Estate and include the same in the direction contained in this my Secondary Will in the foregoing direction to pay.

This particular precedent is a shorter form of precedent which attempts to throw onto the Secondary Estate only debts and taxes referable to the assets flowing through the Secondary Estate.

(a) Debts

If an asset falling into the Secondary Estate is encumbered and the debt is secured by an asset that would otherwise fall into the Primary Estate, the issue arises as to whether or not that asset also falls into the Secondary Estate. Debts relative to an asset which falls into the Secondary Estate (such as a line of credit specifically reserved for that particular asset) will also be charged against that asset. If the debt exceeds the assets, the other assets in the Secondary Estate are responsible for the debt. However, if that line of credit is secured by an asset which would otherwise fall into the Primary Estate, that asset does not become an asset of the Secondary Estate simply by virtue of the fact that it supports the debt referable to that asset.

We noted earlier that legacies and specific assets are generally transferred to a beneficiary on an unencumbered basis except for real estate. In a multiple Will situation, where debts, taxes and other expenses are allocated between Wills and based on whether or not an asset falls into one Will or another, an issue arises as to whether or not that specific bequest of an asset is a gift of the asset itself or the net value of the asset after the deduction of debts, taxes and expenses.

The general rule is that the general power to pay debts and taxes is not a sufficient intention demonstrated by the testator that the specific legacy is to be subject to a burden. In the precedent noted above, the allocation of debts and taxes based on an

asset-by-asset basis is simply an identification step. In each instance, the debts and taxes are to be paid out of the capital of "the general Secondary Estate".

(b) Taxes

In many multiple Will precedents, taxes referable to property passing through each estate are to be paid out of that particular estate. This suggests that taxes should be "allocated" between the various Wills. But how is that tax calculated for each Will? Does each Will notionally claim a proportionate share of the deductions?

It should be noted that all the Executors of the multiple Wills are required to file the T1 Terminal Return as well as perhaps a special Rights and Things Return.[65] In some instances, testators provide for different Executors and Trustees of multiple Wills. In my view, it is likely to be a tedious, time-consuming and very complicated task to file a single T1 Terminal Return and allocate precisely the cost of the taxes due on each specific asset.

Again, this will be critical where there are different beneficiaries for the various Wills and where the residue of each Will bears the cost of such taxes.

6. Legacy vs. Residue

As noted, where multiple Wills do not provide that the Wills are to be treated as one Will for purposes of abatement, it is likely that any residuary bequest in a Special Will (as opposed to the Will which is to be the Residual Will) will be considered as legacies and will therefore abate after the true residue which will be found in the Will which is to be designated as the true Residual Will into which all assets not specifically disposed of will fall.

These issues may not be problematic if the beneficiaries of both Wills are identical. However, many testators will dispose of probate property differently from that which does not require probate. This will particularly be the case where a non-probate Will involves shares of a private business. These shares will fall into the non-probate Will which is generally the Will which has the greatest value.

As a practical matter, I find that drafting multiple Wills is a process fraught with concern for the drafter of the Will who needs to be very careful to ensure that the use of two Wills does not result in applications of rules which have an unintended result.

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[65] Under paragraphs 150(1)(b) and 150(1)(d) of the Act, the obligation to file the terminal year income tax return for a deceased taxpayer is imposed upon the individual's "legal representatives", which is defined in subsection 248(1) of the Act to include an executor, administrator or trustee, or any other "like person ... administering, winding up, controlling or otherwise dealing in a representative or fiduciary capacity with the property that belongs or belonged to, or that is held for the benefit of, the taxpayer or the taxpayer's estate".

All the executors under each of the multiple Wills are responsible, as the legal representative of the deceased taxpayer, to file the T1 terminal return.

Since it is possible for the testator to change the rule regarding abatement, we strongly recommended that each time a multiple Will is drafted, a clause be included to ensure that the testator provides detailed instructions for the order of abatement or priority between the beneficiaries of each of the Wills.

CONCLUSION

The discussions above indicate that the new techniques used for probate tax avoidance have complicated the drafting of Wills considerably. It has also thrown an extra burden upon an estate practitioner who now has to be even more careful in drafting Wills. Multiple Wills continue to be a challenge for many practitioners and will continue to be challenge until there has been some further experience in the administration of estates which have multiple Wills.

It is no surprise that the non-Will techniques used to avoid probate complicate matters even further. The implementation of a prohibitive probate tax has simply resulted in most practitioners drafting multiple Wills or engaging in other planning techniques to avoid the type of revenue that the province might anticipate from large estates.

For the average person without access to lawyers or those who simply choose to take the self-help route and transfer property into joint tenancy or into the name or another, the result is the same in terms of the avoidance of probate tax on smaller estates. However, these techniques continue to be the most fruitful source of litigation and contentious proceedings. To anticipate and avoid these problems, solicitors must exercise extra diligence and it is more clear than ever that preparation of a cost-effective Will for the average individual is becoming more and more of a challenge.

Schedule "A"

Courts of Justice Act, s.127

Postjudgment and Prejudgment Interest Rates

Please note that effective October 1, 2007, postjudgment and prejudgment interest rates will be published on the Ministry's website pursuant to O. Reg. 339/07.

1. Postjudgment interest rates (and prejudgment interest rates for causes of action arising on or before October 23, 1989) are as follow:

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
1985	12.0%	13.0%	11.0%	11.0%
1986	11.0%	13.0%	10.0%	10.0%
1987	10.0%	9.0%	10.0%	11.0%
1988	10.0%	10.0%	11.0%	12.0%
1989	13.0%	13.0%	14.0%	14.0%
1990	14.0%	15.0%	15.0%	14.0%
1991	14.0%	11.0%	11.0%	10.0%
1992	9.0%	9.0%	8.0%	7.0%
1993	10.0%	8.0%	7.0%	6.0%
1994	6.0%	6.0%	8.0%	7.0%
1995	8.0%	10.0%	9.0%	8.0%
1996	8.0%	7.0%	6.0%	6.0%
1997	5.0%	5.0%	5.0%	5.0%
1998	5.0%	6.0%	6.0%	7.0%
1999	7.0%	7.0%	6.0%	6.0%
2000	6.0%	7.0%	7.0%	7.0%
2001	7.0%	7.0%	6.0%	6.0%
2002	4.0%	4.0%	4.0%	4.0%
2003	4.0%	4.0%	5.0%	5.0%
2004	4.0%	4.0%	4.0%	4.0%
2005	4.0%	4.0%	4.0%	4.0%
2006	5.0%	5.0%	6.0%	6.0%
2007	6.0%	6.0%	6.0%	6.0%
2008	6.0%	6.0%	5.0%	5.0%
2009	4.0%	3.0%	2.0%	2.0%

This table shows the postjudgment interest rates for orders made in the quarters indicated. This table also shows the prejudgment interest rates for actions commenced in the quarters indicated in respect of causes of action arising on or before October 23, 1989.

For proceedings commenced before January 1, 1985, the postjudgment interest rate is the prime bank rate, which is published in the Bank of Canada Review. The rate can be found from either the back copies of the Bank of Canada Review or by calling the Bank of Canada. The rates are also reproduced in the 1987 to 1991 editions of Carthy Millar Cowan's *Ontario Annual Practice* (published by Canada Law Book Inc.) or in the 1985-1990 editions of Watson and McGowan's *Supreme and District Court Practice* (published by Thomson Carswell) following the text of section 138 of the *Judicature Act*.

2. Prejudgment interest rates for causes of action arising after October 23, 1989 are as follows:

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
1989				12.4%
1990	12.5%	13.5%	13.9%	12.9%
1991	12.3%	10%	9.1%	8.8%
1992	7.7%	7.5%	6.3%	5.1%
1993	8.3%	6.1%	5.1%	5.0%
1994	4.3%	4.1%	6.6%	5.6%
1995	6.0%	8.0%	7.6%	6.6%
1996	6.1%	5.6%	5.0%	4.3%
1997	3.3%	3.3%	3.3%	3.5%
1998	4.0%	5.0%	5.0%	6.0%
1999	5.3%	5.3%	4.8%	4.8%
2000	5.0%	5.3%	6.0%	6.0%
2001	6.0%	5.8%	4.8%	4.3%
2002	2.5%	2.3%	2.5%	3.0%
2003	3.0%	3.0%	3.5%	3.3%
2004	3.0%	2.8%	2.3%	2.3%
2005	2.8%	2.8%	2.8%	2.8%
2006	3.3%	3.8%	4.5%	4.5%
2007	4.5%	4.5%	4.5%	4.8%
2008	4.8%	4.3%	3.3%	3.3%
2009	2.5%	1.3%	0.5%	0.5%

This table shows the prejudgment interest rates for actions commenced in the quarters indicated in respect of causes of action arising after October 23, 1989.

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