TAB 1

Estate Accounting – Navigating the Complex Issues When Preparing and Reviewing Estate Format Accounts

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February 4, 2010

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ESTATE ACCOUNTING
- Navigating The Complex Issues When Preparing And Reviewing Estate Format Accounts

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ESTATE ACCOUNTING
– Navigating the Complex Issues When Preparing and Reviewing Estate Format Accounts

INTRODUCTION

The purpose of this paper is to attempt to analyze and consider some of the more complex aspects of estate administration relating to estate accounting.

ASSETS OF THE ESTATE

In a sense, all personal property of the deceased which is of a saleable nature and may be converted into money is an asset of the estate. This, of course, can include the deceased's right of action or possession.

Pursuant to the *Estates Administration Act,*[1] real and personal property devolves to the deceased's personal representative.

Except in circumstances where there is wilful default, fraud or gross carelessness, ordinarily, trustees are not liable beyond what they actually receive in the context of an estate administration. Some unique assets to consider in the context of preparing estate accounts are as follows:

- a mortgage;
- a lease;
- profits made from continuing the testator's business;
- the benefit of a licence;
- an option;

[1] R.S.O. 1990, c.E.22, s. 2.

- a right of action; and
- any rights to property under the provisions of a domestic contract, such as a marriage contract.

VALUATION, CONTROL AND CUSTODY AND INVENTORY OF THE ASSETS

Taking possession of the assets of the Estate is the Executor's immediate obligation, and if not properly undertaken, can be the subject of an accounting by the beneficiaries. In the course of determining the nature and extent of the assets of the estate, the Executor's obligation is to undertake an inventory of the assets and to do so without delay. The delay is, of course, considered on a case by case basis, and is typically no longer than the Executor's year at a maximum.

It is the obligation of an Executor to bring in all of the assets of the estate, whether specifically bequeathed or otherwise, and the expenses associated with collecting those assets are typically payable out of the general estate unless the will provides otherwise.[2]

The liability of an Executor or Administrator for loss of assets of the estate in his or her hands has been developed through the Courts and subsequently adopted by section 7 of the *Courts of Justice Act*[3]. The Executor's liabilities is typically considered in the context of whether or not the fiduciary has acted for the benefit of the estate, used proper diligence, and acted with ordinary care and circumspection in the discharge of his or her trust. If this is the case, then he or she will not be held answerable for the losses.[4]

STATEMENT OF ORIGINAL ASSETS

It is the Executor's obligation to provide a statement of original inventory or assets of the estate, and this is particularly set out in Rule 74.18 of the *Rules of Civil Procedure*. As a result of *Re:*

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[2] Thériault, C., *Widdifield on Executors and Trustees*, 6th ed., looseleaf (Toronto: Carswell, 2002) at 2-12. [*Widdifield*].
[3] R.S.O. 1990, c.C.43, s. 7.
[4] *Widdifield*, *supra* note 2 at 2-13.

Silver Estate,[5] there is no requirement that an Executor act under exclusively a probated will and, therefore, may be compelled to pass his accounts for both unprobated and probated assets.

Executors may be guilty of negligence or careless administration where they sell or dispose of the assets at less than their value.[6]

SPECIFIC AND UNIQUE ASSETS

Goodwill

The proceeds of the sale of goodwill in the practice or business of the deceased can be an important asset in respect of any estate administration and needs to be properly accounted for when there is still value in the goodwill at the date of death. In the case of a commercial partnership, it is now generally held that, subject to a provision in the partnership agreement to the contrary, the portion of the goodwill is naturally the deceased's asset.[7]

Chose in Action

It is a general assumption that the right of action which survived death will automatically pass to the personal representative. Instances where a chose in action is an asset of the estate include:

- actions against directors of the company;
- claims for a settlement agreement or contract of employment; and
- personal injury claims.

Special attention must be given to section 38 of the *Trustee Act,*[8] which states specifically that there is a limitation period of 2 years for the commencement of actions for tort and damages generally.

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[5] 31 E.T.R. (2d) 256 (Ont.S.C.J.).
[6] *Widdifield, supra* note 2 at 2-14.2.
[7] *Widdifield, supra* note 2 at 2-26 at paras 2.5.1.
[8] R.S.O. 1990, c. T.23, s. 38.

Foreign Assets

It was generally held that an Executor was not obligated to include in the inventory of the estate assets that are in a foreign jurisdiction. However, where an individual is named Executor of the whole estate, wherever situate, he or she cannot completely ignore foreign assets.[9]

Land

Whether chattels attached to a building or land are fixtures is a question of fact depending principally on two considerations: Whether they can be easily removed without injury to them or to the building or land; and whether the object of the annexation was for the permanent and substantial improvement of the dwelling or merely for the temporary purpose and the more complete enjoyment and use of it as a chattel.[10]

Executor's Compensation

There are a series of issues that need to be considered in the context of the calculation of compensation, and these are generally dealt with on a case by case basis. These include:

- distributions in specie;
- accrued interest from the date of death;
- real estate sales;
- fees paid from the estate for legal and accounting costs etc.;
- assets that fall outside of the estate, including insurance policies and RRSP's;
- capital gains and losses;
- book entries;
- compensation division among co-trustees;
- compensation to successive trustees;
- priorities of compensation over other claims and enforcement;
- pretaking compensation;

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[9] *Widdifield supra* note 2 at 2-64.1 at para 2.5.9.
[10] *Widdifield supra* note 2 at 2-68 at para 2.5.12.

- payments to real estate agents and other agents of profession;
- directors fees;
- solicitor's fees;
- payment from the estate to the executor for ongoing administration expenses;
- distributions to ongoing trusts;
- distributions to beneficiaries; and
- risk assumed by the Executor.

CAPITAL AND INCOME ISSUES

Disbursements

Subject to a contrary intention in the will, the decision of *Vallambrosa Rubber Co. v. Farmer (Surveyor of Taxes)*[11] describes the distinction between a capital expenditure and an income expenditure as follows:

> To say that capital expenditure is a thing that is going to be spent once and for all, an income expenditure is a thing that is going to recur every year.

The real test as between income and capital is a question of fact and often a question of degree.[12] Ultimately, the jurisdiction as to determining whether or not funds of the estate are income or capital lies with the court.[13]

Payment of Expenses of Administration

The general rule is that costs relating to protection of the trust property, including legal proceedings, are paid out of capital; however, if the expense relates exclusively to the life tenant (such as taxes) an income beneficiary pays those expenses.

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[11] [1910] S.C. 519 (Scot. Ct. Sess.)
[12] *Shabro Investment Ltd. v. R.* [1979] C.T.C. 125 (Fed. C.A.).
[13] *Re Bronson* (1958), 14 D.L.R. (2d) 51 (Ont. H.C.).

The following is a list of some of the general allocations of payments divided as between income and capital:

- The cost of appointing new trustees came out of the capital;[14]
- The cost of investing funds were paid out of capital and the fees were seen as a recurrent charge to protect the estate as a whole;[15]
- The charge of all taxes imposed on land were payable by the life tenant.[16] Furthermore the life tenant was held to pay carrying charges on vacant non-productive land.[17]

The Rule in *Allhusen v. Whittell*[18] - Allocation of the Testator's Payment of Debts, Income or Capital, and When?

The *Rule* in *Allhusen v. Whittell* is that the true residue is determined only after funds have been set aside for future liabilities.[19] The question still remains as to whether or not the debt of the testator should be paid out of capital when it becomes due, or whether a fund should be set aside which, with its income accumulated, would be sufficient to pay the debt at the future reported time. Putting the matter in another way, should the income tenant have the benefit of the income from the capital funds until such funds are required for the payment or, in other words, what is the true residue of the estate the income from which is to be paid to the income tenant?[20]

Fortunately, in Ontario, section 49 of the *Trustee Act*[21] resolves the confusion that once surrounded the *Rule*. As was stated by Davey J.A. in *Lotzkar v. Southin*[22] where an amount from capital is set aside to meet debts and liabilities, the life tenant does not collect interest on the sum so set aside. Section 49 of the *Trustee Act*[23] in simplified form provides that any debts at the

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[14] *Carter v. Sebright* (1859), 26 Beav. 374.
[15] *Horlock v. Smith* (1853) 17 Beav. 572. See also *Carver v. Duncan (Inspector of Taxes)* [1985], 2 E.R. 645 H.L. (Eng.).
[16] *Biscoe v. Van Bearle* (1858), 6 Gr. 438 (U.C.Ch.).
[17] *Josephs v. Josephs Estate* (1993), 106 D.L.R. (4th) 384 (Ont. C.A.)., rev'g (1992), 45 E.T.R. 162 (Ont. Div. Ct.).
[18] (1867) L.R.4 Eq. 295.
[19] *Widdifield supra* note 2 at 7-4 at para 7.1.6.
[20] *Ibid.*
[21] R.S.O. 1990, c.T.23, s. 49.
[22] (1965), 50 D.L.R. (2nd) 338 (B.C. C.A.), rev'd, [1966] S.C.R. 69.
[23] *Supra* note 21.

death of the testator are to be satisfied out of capital and the interest on the capital of the estate retains its character unless the capital itself is insufficient to satisfy the disbursements.[24]

In summary, the *Rule* is still very relevant and applicable as a principle of law.[25]

Allocation of Losses between Income and Capital

In Canada, there are essentially two approaches applied to the apportionment of an investment loss as between the life tenant and capital beneficiary, and each approaches the question on the basis of seeking to equitably allocate the actual proceeds realized on the investment.[26] As the authors in Widdifield note,[27] it is likely that the equities involved in each particular case will determine which test is favoured and each case is very much dependant on its facts.

Business Losses

In circumstances where a business is involved, the net losses are born by the life tenant, as are the profits. It should be noted that this *Rule* does not apply where there is no direction to carry on the business in the will, and careful consideration must be given to the terms of the will itself. An example of this allocation was found in the case of *Rose Estate, Re,*[28] where the testator directed in his will that his business was to be continued so long as it should be profitable. The business was sold after a loss was incurred, and the Court applied the principle in *Upton v. Brown*[29] and held that the loss was chargeable as against the income beneficiary and not against the capital.

Mortgage Payments

In situations where the deceased, at the date of death, held real property subject to certain encumbrances, any payments toward the principal owing or on account of any arrears of interest accumulated during the lifetime of the testator are a charge on the capital. The life tenant bears

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[24] *Widdifield supra* note 2 at 7-6 at para 7.1.6.
[25] See *Lotzkar v. Southin* Supra Note 22. (For a contrary view that the *Rule* in *Allhusen v. Whittell* has no applicability in Canada – See G.F. Maclaren in (1959), 2:6 *Can. Bar Journal*, at 399).
[26] *Widdifield, supra* note 2 at 7-7 at para 7.1.7. See *Re Foster; Lloyd v. Carr* (1890), 45 Ch.D. 629 for the first approach. See Also *Moore, Re* (1885), 54 L.J. Ch. 432 for the second approach. (Both of these approaches were later followed by Canadian Courts).
[27] *Widdifield, supra* note 2 at 708 at para 7.1.7. (B).
[28] (1939), [1940] 1 D.L.R. 139 (N.B. Ch.).
[29] (1884), 26 Ch.B. 588 (Eng. Ch. Div.).

only the current interest due under the mortgage, which includes any interest on the accumulated arrears and interest.[30]

The income beneficiary takes all casual profits that accrue during the time of his tenancy for life.[31]

Benefits for Corporations

The normal receipt of the dividend corporation is income. Moreover, if the company sells its assets and distributes the proceeds in the context of a winding up, then it receives capital. This, of course, represents two extremes and problems can arise between them.

The problem is outlined in *Waters, the Law of Trusts in Canada*, and the learned author queries whether or not, when the trustees are allocating the receipt, they are doing it in accordance with the form and label of the benefit, or whether the particular fund within the company for which the benefit is drawn, is determinative.[32] Some of the considerations to address when determining this issue are:

- The recipient of the monies paid out is of no concern to the limited company and therefore if monies are paid to a trustee it had no bearing on the characterization of the payment as between income and capital;[33]
- The limited company, not in liquidation, can make no payment by way of return of capital to its shareholders except in authorized reduction of capital. Whether the payment is called "dividend" or "bonus" or any other name, it still must remain a payment on division of profits;[34]
- There is little doubt that almost every distribution of money must be treated as income in the hands of the shareholders, unless it is either a distribution in a liquidation, a repayment in respect of production of capital, or an issue of bonus shares or bonus debentures;[35]
- In large part, there has been significant debate within the Canadian Courts as to the impact of the form "Rule" established in *Hill v. Permanent Trustee Co. of New South*

[30] *Widdifield, supra* note 2 at 7-8 & 7-9 at para 7.1.8.
[31] *Brigstocke v. Brigstocke* (1878), A.Ch.D.357 at 363.
[32] D.W.M. Waters, *Law of Trusts in Canada,* 2nd ed. (Toronto: Carswell, 1984) .
[33] *Hill v. Permanent Trustee Co. of New South Wales,* [1930] A.C. 720 (New South Wales P.C.).
[34] *Ibid.*
[35] *Rae (Inspector of Taxes) v. Lazard Investment Co. Ltd.*, [1963] 1 W.L.R. 555 (H.L.).

Wales, and to a great extent the determination is consummately based on the facts in "form".

21 YEAR RULE

Careful attention needs to be given to the rules of accumulation commonly known as the 21 year rule. An accumulation arises when income from a fund is earned and not distributed but is simply added to the capital.

In Ontario, the Accumulations Act[36] imposes certain statutory restrictions on the accumulation of income. The most commonly applicable one provides that income cannot be accumulated for more than 21 years from the death of the testator.

FIDUCIARY CLAIMS – UNJUST ENRICHMENT

There are three traditional classifications of fiduciaries.

The typical person who is considered a fiduciary is a trustee. It is someone who holds or manages property on behalf of another.

The second classification of a fiduciary comes from the principle of the law of agency and the third category is an advisor.[37]

The concept of seeking a remedy or relief against a fiduciary is one that is firmly entrenched in the statues and the common law.

The purpose of this paper is to explore some of the types of remedies and relief, in the context of constructive trust claims, that can be sought and obtained against a fiduciary, and to comment on the procedural and practical aspects of seeking such relief.

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[36] R.S.O. 1990, c.A.5.
[37] J.C Shepherd. *The Law of Fiduciaries*, (Toronto: Carswell, 1981), at 21-22.

Unjust Enrichment - Historical Background

When seeking relief against a fiduciary, one avenue to consider is the remedy of unjust enrichment. The basic principle is that the Courts will act in a manner that ultimately will not permit the unjust enrichment of one over another. Simply stated:

> "A person who has been unjustly enriched at the expense of another is required to make restitution to the other[38]."

Based on the general principle of unjust enrichment, as described above, the Courts in Canada have adopted and developed a framework that assists in explaining the concept of unjust enrichment. Beginning with *Deglman v. Guaranty Trust Co. of Canada*[39], the Supreme Court of Canada set the parameters for the contractual theory of quasi-contract and its relationship to unjust enrichment.

In *Deglman v. Guaranty Trust Co. of Canada*[40], a nephew had provided certain services for his aunt in return for an oral promise that she would leave certain property to him in her will. The services were provided by the nephew as requested and, at the time of the aunt's death, she had not provided for him in her will.

The Court held that the nephew was entitled to relief in quantum meruit for value of the services rendered by him on behalf of the aunt.

Cartwright J. stated that:[41]

> "When the Statute of Frauds was pleaded, the express contract was thereby rendered unenforceable, but, the deceased having received the benefits of the full performance of the contract by the respondent, the law imposed upon her, and so on her estate, the obligation to pay the fair value of the services rendered to her."

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[38] American Law Institute, *Restatement of the Law of Restitution*, Quasi-Contracts and Constructive Trusts (St. Paul: ALI, 1937) at 5.
[39] [1954] S.C.R. 725, [1954] 3 D.L.R. 785.
[40] *Ibid.*
[41] *Ibid* at 735.

Since the *Deglman* case, a series of decisions have firmly developed the concept and implementation of unjust enrichment, and have also set out when it is the appropriate theoretical basis for a claim of quasi-contract.[42]

Most authorities, but not all, recognize that an action for unjust enrichment is subject to the existence of the following conditions:

- an enrichment;
- an impoverishment;
- a correlation between the enrichment and the impoverishment;
- the absence of justification;
- the absence of evasion of the law; and
- the absence of any other remedy.

As noted above, the general concept is that one must not reap the benefit of another's labours. Another aspect of unjust enrichment is that a person shall not be permitted to profit from his or her breach of the fiduciary duty owed. Meaning, the Court will look to the offending party (i.e. the fiduciary) to disgorge any assets or profits obtained by their wrongful conduct.

In *Canadian Aero Service Ltd. v. O'Malley,*[43] the Supreme Court of Canada stated that:

> "Liability of [the defendants] for breach of fiduciary duty does not depend upon proof by Canaero [the plaintiff] that, but for their intervention, it would have obtained the ...contract; nor is it a condition of recovery of damages that Canaero establish what its profits would have been or what it has lost by failing to realize the corporate opportunity in question. It is entitled to compel the faithless fiduciaries to answer for their default according to their gain."

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[42] J.D McCamus & P.D Maddaugh,*The Law of Restitution*: *Canada Law Book* (Aurora, 1990) at 18. (For a comprehensive review of the historical case law developments since the *Deglman* decision, see 16-18.).

[43] [1974] S.C.R. 592 at 621-622.

Even though the defendant's enrichment has not been obtained at the plaintiff's expense in the sense that it was a benefit the plaintiff would otherwise have enjoyed, the enrichment is held to be unjust and recoverable simply for the reason that it was obtained through the defendant's wrongful breach of a duty owed to the plaintiff.

As noted above, the components of proving unjust enrichment are if the plaintiff can show the existence of an enrichment or benefit in the defendant's hands, a corresponding deprivation or expense on the part of the plaintiff, and the absence of any juristic reason for the enrichment.

CONSTRUCTIVE TRUST CLAIMS

Introduction

Most trust relationships are developed from an express trust deed or document that the parties can look to in an effort to define the terms of the trust and to define the relationships of the parties.

A constructive trust is a remedy that can be imposed by the Court that may result in an award of an interest in the property to a non-registered party. It is clear that the registration of an asset in the testator's name alone is not sufficient to prevent the spouse or the common law spouse, or any other person who claims to have contributed to the ownership of an asset from making a claim to an asset such as the matrimonial home, the business operations of the testator, or other similar assets.

If the spouse or common law spouse or any other person can prove participation in the payment for the house or other asset, or show contribution via domestic services or participation in the business, the personal representatives of the testator may be held to be the constructive trustees of the property to the extent of the claimant's interest as determined by the Court.

The principle of a constructive trust is a natural extension of the unjust enrichment concept that has been developed through a series of decisions of the Supreme Court of Canada[44]. In many

[44] *Murdoch v. Murdoch*, [1975] 1 S.C.R. 423, 41 D.L.R. (3d) 367, *Rathwell v. Rathwell* [1978] 2 S.C.R. 436, 83 D.L.R. (3d) 289 and *Pettkus v. Becker*, [1980] 2 S.C.R. 834, 117 D.L.R. (3d) 257.

respects, this series of decisions sets the stage for the entrenchment of the concept of a constructive trust in the Canadian Courts.

In the first of those decisions, *Murdoch v. Murdoch*[45], the dissent of Laskin J. first dealt with the concept that relief may be made available on the basis of a constructive trust [as opposed to an express trust, which does not depend on evidence of intention] and one which would be awarded in order to avoid the unjust enrichment of the husband.[46] The dissent of Justice Laskin was considered by the Court in *Rathwell v. Rathwell*[47]:

> "The constructive trust amounts to a third head of obligation, quite distinct from contract and tort, in which the Court subjects "a person holding title to property...to an equitable duty to convey it to another on the ground that he would be unjustly enriched if he were permitted to retain it"... the constructive trust is an obligation of great elasticity and generality."[48]

The creation of a constructive trust usually depends upon the intention of the settlor to establish a trust situation. However, this is not always the case in certain transactions and, as such, the law will impose a fiduciary relationship on a person even though the original owner of the property does not or cannot (as a result of death or otherwise) intend this to be the case and may not even know the "trustee" in question.

The constructive trust is really the imposition of fiduciary duties on a person by a Court of Equity. A constructive trust is a relationship created and imposed by operation of law and in the interests of good conscience.[49]

Constructive Trust: Cause of Action or Remedy?

The constructive trust claim has been viewed by the Canadian Courts as a remedy available to prevent unjust enrichment and a cause of action.[50]

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[45] [1975] 1 S.C.R. 423, 41 D.L.R. (3d) 367.
[46] *Ibid* at 454 and 457.
[47] [1978] 2 S.C.R. 436, 83 D.L.R. (3d) 289.
[48] *Ibid* at 454, (For a comprehensive analysis of the principle of constructive trust see B. Hovius and T.G. Youdan *The Law of Family Property* (Carswell, 1991) at 121.
[49] E. Gillese, *The Law of Trusts* (Irwin Law, 1997) at 106.

It has been suggested that the constructive trust is tied to the fiduciary relationship and arises in five circumstances:

1. As an extension of an existing trust;

2. On receipt of trust property by a stranger;

3. Profit from trust;

4. A surplus from a mortgage sale; and

5. Where a vendor is a constructive trustee of land for a purchaser on specific performance.[51]

In terms of classifications of trusts and the interrelationship of constructive trusts to other forms of trust claims or remedies, the different classifications show a continuum based upon the level of intention. At one end are express trusts, where an expression of intention is required, and at the other end are constructive trusts, where no intention is required. The midpoint is a resulting trust, where presumptive resulting trusts at least are based on presumption of intention.[52]

Limits of Constructive Trust Claims

When examining the limitations of constructive trusts claims and the protections and defences available in such circumstances, consideration should be given to the nature of the constructive trust remedy itself.

The constructive trust arises in respect of certain gains made by fiduciaries. The constructive trust remedy is sometimes the appropriate claim, as it can make a fiduciary accountable to a principal for a gain made in circumstances which make it improper to retain the gain itself.

Therefore, the constructive trust remedy arises in situations where a person is in a fiduciary relationship and has had an opportunity to make a gain by use of his or her position as a fiduciary. One should consider if the circumstances exist where there is a possibility of conflict

[50] *Ibid* at 109-110.
[51] *Ibid* at 110.
[52] *The Law of Family Property*, *Supra* note 51 at 33.

between the duty as a fiduciary and the fiduciary's own interest, whether or not the gain has been made without the informed consent of the principal or the approval of the Court. In such circumstances, a person will be accountable for the gain to the principal.

A fundamental aspect of any successful constructive trust claim is that the parties are in a fiduciary relationship and a fiduciary relationship exists where:

(a) one person, the fiduciary, has undertaken to act in the interests of another person, the principal, or in the interests of the fiduciary and another person;

(b) as part of the arrangement between the fiduciary and the principal, the fiduciary has a power or discretion capable of being used to affect the interests of the principal in a legal or practical sense;

(c) the principal is vulnerable to abuse by the fiduciary of his or her position; and

(d) the principal has not agreed, as a person of full capacity who is fully informed, to allow the fiduciary to use the power or discretion solely in his or her own interests.[53]

Other considerations in respect of defending constructive trust claims can be developed through a review of the applicable statutory limitation period, the doctrine of laches and acquiescence.

The statutory considerations in respect of the *Limitations Act*[54] are sections 42, 43, 44 and 47, and these subsections provide the statutory framework.

The *Trustee Act* Case Law Developments

Pursuant to section 38 of the *Trustee Act*, actions by estates for torts for injuries to the person or property of the deceased, or actions against estates for wrongs committed by the deceased, must be commenced within two years from the date of death.

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[53] H.A.J. Ford and W.A. Lee, *Principles of the Law of Trusts*, 2d Ed., (Sydney: The Law Book Company Limited, 1990) at 1002.

[54] R.S.O. 1990 ch. L.15.

While there is certainly some debate as to the extent of the provisions of this section, careful consideration must be given to the fact that section 38(1) limits the range of actions by an Estate Trustee to "an action for all torts or injuries", and further expands the range of actions of an Estate Trustee to include "a wrong" committed by the deceased.

In *Edwards v. Law Society of Upper Canada*[55], the Ontario Court of Appeal considered whether or not sections 43 and 44 of the *Limitations Act* override the two-year limitation requirement in section 38(3) of the *Trustee Act*. In its decision[56], the Ontario Court of Appeal overturned the Motion Judge's decision, and has now left open the question as to whether or not the discoverability rule applies to the limitation period or, in the alternative, the Court left open the question as to whether or not the claim against or by a trustee must be commenced within two years of the date of death.

Out of an abundance of caution, any constructive trust claim should now probably be commenced within the two-year limitation period, if possible.

Laches and Acquiescence

After exhausting the *Limitations Act*, which may limit any constructive trust claim to a period of six years by virtue of section 45(1)(g), and considering the case law, the doctrine of laches and acquiescence may be important to consider.

The basic idea of laches is that it "consists of a substantial lapse of time, coupled with the existence of circumstances which make it inequitable to enforce the claim".[57] The doctrine of laches is not composed of a body of rules; rather, it is a flexible doctrine which simply creates a framework for the existence of judicial discretion.[58]

As to the doctrine of acquiescence, this defence is traditionally based on three elements:

(a) knowledge of the facts by the person alleged to have acquiesced;

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[55] (1998) 39 O.R. (3d)10 (Gen. Div.).
[56] (2000) 48 O.R. (3d) 321 (C.A.).
[57] John McGhee, *Snell's Equity*, 13th ed. (London: Street & Maxwell, 2000) at 3-19.
[58] *The Law of Family Property, supra* note 51 at 166.

(b) some positive acts, as opposed to mere inactivity, by the person alleged to have acquiesced; and

(c) prejudice to the other party caused by reliance on the acquiescence.[59]

ACCOUNTING REMEDIES

Another remedy available in equity against a fiduciary is the obligation of a fiduciary to account. In the context of fiduciary obligations, the accounting remedy is imposed for the purpose of requiring the fiduciary to disgorge any benefit obtained through breach of the duty of loyalty.

Special Accounting Duties of a Fiduciary

Some of the duties and obligations of a fiduciary in relation to accounting to beneficiaries are as follows:

1. To keep proper accounts of the trust estate which should be clear and accurate and rendered at appropriate intervals to the beneficiaries;

2. The accounts must be kept distinct from other accounts;

3. Receipts or cancelled cheques and vouchers must be preserved to support entries on both the credit and debit side of the accounts; and

4. To produce to any beneficiary the accounts when reasonably requested.

In the case of income or revenue beneficiaries, accounts must be rendered at reasonable intervals without being requested by the beneficiaries entitled to such income or revenue. In the case of residuary beneficiaries, accounts should be presented when the interest falls into possession.

These beneficiaries are entitled to inspect and investigate the accounts, vouchers and other documents of the trust estate, including the will or trust deed. They are also entitled to such full and accurate information regarding the state of the trust property and the administration generally as is or ought to be within the knowledge of the Trustee.

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[59] *The Law of Family Property*, *supra* note 51 at 168-169.

Thus the accounts must be kept in such a manner that they will clearly show how all the monies or assets received have been disbursed or otherwise disposed of, and the ultimate distribution among the beneficiaries of the available estate.

It goes without saying, of course, that beneficiaries who are given general or specific bequests or devises and who have received these bequests in full are not entitled to any further accounting.

If, for any reason, the Trustee cannot keep the accounts herself, she is under a duty to employ a competent person to do so, and these costs will generally be chargeable out of her compensation, as it is her duty to keep the accounts.

Further duties and obligations imposed upon trustees include:

5. To make all beneficiaries fully acquainted with their rights;

6. To disclose any and all breaches of trust;

7. To allow all beneficiaries sufficient time to investigate the accounts;

8. To ensure that all beneficiaries have competent and independent advice in their investigation of the accounts; and

9. To notify all beneficiaries interested of any Court audit.

In general terms, the accounts should provide all essential information to all persons interested or entitled to an accounting in the estate or trust in a manner that is capable of being understood by a person of average intelligence, literate in English, and familiar with basic financial terms, who has read the trust document with care and attention. Accordingly, a fiduciary preparing her accounts should be careful to avoid technical terms such as "debit" and "credit," which are generally not known to persons who are not familiar with bookkeeping and accounting practices.

Rescission

The equitable remedy of rescission involves the setting aside of a transaction and the granting of such incidental relief as will restore the parties to their previous position.

This equitable remedy or damages in lieu, is available on a passing of the accounts of an Executor.[60]

The position is the same on the passing of the accounts of an Attorney.[61]

There is, of course, a limit as to the availability of rescissionary relief. For instance, relief will not be allowed if the impugned transaction has been affirmed, if there has been laches or undue delay in seeking relief, or if third party rights have intervened.

Tracing

There are circumstances where a fiduciary's misconduct may result in the necessity to go beyond specific recovery of the unjust enrichment. For example, if the property in question cannot be recovered in its original form.

In order to successfully obtain a tracing order, one must first prove legal ownership of the property. Problems of identifying the property may arise, and the process of tracing the property itself can be cumbersome.

An illustration of a problem that can arise with respect to identifying a property is where two chattels are merged into one and each one's identity is lost in the other. For example, where a car is purchased under a conditional sales agreement and value is thereafter added to the car by way of new tires or equipment.

The answer to the question of whether the property can be identified is not an easy one and, of course, may depend on the terms of the contract itself. Furthermore, the general law of accession applies, and the Court will look at whether or not the item in question has become sufficiently annexed to the vehicle to constitute an accession.

The definition of accession has been set out in the decision of *Dawson v. Floyd Dunford Ltd.,*[62] as follows:

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[60] *Estates Act,* R.S.O. 1990, c. E. 21, s. 49(3).
[61] *Substitute Decisions Act*, S.O. 1992 c. 30, s. 42(6).
[62] [1961] O.W.N. 225 (Co. Ct.) at 227.

> Accession, strictly speaking, is where a thing which belongs to one person becomes the property of someone else by reason of its becoming added to or incorporated with a thing belonging to the latter.[63]

Another consideration of the law of tracing relates to circumstances where the property of someone is transformed by the labour of another into a new form of property. The key question here, of course, is whether or not the title to the transformed property belongs to the owner of the original property, or has passed to the person who had performed the labour and thus transformed it.

As to the tracing of money, in general, money can be traced so long as it can be identified and has not been mingled with other money. However, if money becomes indistinguishably mixed with that of another, the right to trace those funds may be lost.

In *Clarke v. Shee and Johnson,*[64] the Court expressed the rule as follows:

> Where money or notes are paid bona fide, and upon a valuable consideration, they never shall be brought back to the true owner; but where they come mala fide into a person's hands, they are in the nature of specific property; and if their identity can be traced and ascertained, the party has a right to recover. It is of public benefit and example that he should: but otherwise, if they cannot be followed and identified, because there it might be inconvenient and open a door to fraud.

In *McTaggart v. Boffo,*[65] the Court described the doctrine of tracing money in this fashion:

> Tracing is only possible so long as the fund can be followed in a true sense, i.e., so long as, whether mixed or unmixed, it can be located and identified. It presupposes the continued existence of the money either as a separate fund or as a part of a mixed fund or as latent in property acquired by the means of such a fund. Simply put, two things will absolutely prevent the tracing of trust monies:

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[63] W.J. Byrne, *A Dictionary of English Law* (London: Sweet & Maxwell, 1923) at 8.
[64] (1774)1 Cowp.197 at 200, 98 E.R. 1041.
[65] (1975), 10 O.R. (2d) 733 (H.C.J.), 64 D.L.R. (3d) 441 at 458.

(a) if, on the fact of any individual case, such continued existence of the identifiable trust fund is not established, equity is helpless to trace it;

(b) the chain for tracing is also broken where the trust fund either in its initial form or a converted form has found its way into the hands of a third person purchaser for value without notice.

Onus and Evidentiary Considerations

In matters involving a fiduciary, the question of gifts received by the fiduciary is often raised. An *inter vivos* gift is a gratuitous transfer of property from its owner to another person with the intention that the transfer have a present effect and the title of the property passes to the donee. There are two major components to this process (a) the transfer is gratuitous, and (b) there is an intention to pass title to the donee.

The onus is on the donee to prove that there is an intention on the part of the donor to transfer the beneficial ownership as well as the legal title.

The onus of proof is on the defendant to prove a valid gift *inter vivos*.

The presumption arising upon a voluntary transfer of property is that of a resulting trust to the donor, and the burden is on those asserting a beneficial transfer to establish that fact.

The presumption of a resulting trust can only be met by providing the same convincing and unimpeachable evidence that is required for an *inter vivos* gift.

Where undue influence is alleged, consideration must be given to whether there was potential for domination given the nature of the relationship between the parties. The test embraces those relationships which equity has already recognized as giving rise to the presumption, such as a solicitor and client relationship, parent and child, guardian and ward, as well as other relationships of dependency which defy easy categorization[66].

[66] *Geffen v. Goodman Estate*, [1991] 2 S.C.R. 353. [*Goodman*].

If the evidence is clear that the donor was in a relationship of dependency to the donee at the time that she granted the donee a Power of Attorney, then, there is not a relationship of equals. While there may or may not be sufficient evidence to make a finding on the mental capacity of the donor at any point in time, clearly if she was in a weakened condition, both mentally and physically, throughout the period of time the gifting is alleged to have occurred, then any gifts by the donor are subject to review.

As to the issue of the presumption of undue influence, an *inter vivos* disposition of property may give rise to the presumption in cases of gifts to persons standing in a fiduciary relationship or some other relationship, whereby the donee was in a position to overbear the donor. In these cases, such persons must show that they did not influence the donor in making the gift[67].

In such a case there is a presumption of undue influence,[68] and the onus on a beneficiary who attempts to discharge the presumption is a heavy one even when the sale is done at fair market value. The onus on the fiduciary is much heavier when the transaction is a gift.[69]

When an executor or a beneficiary acquires property of an estate without an order of the Court, or fails to rebut the presumption of undue influence, the other party is entitled to a rescission, or when that is not possible, to damages.[70]

In circumstances where there is a challenge to an *inter vivos* gift which does not involve an attorney or a beneficiary, the onus is on the recipient of the gift to provide convincing and unimpeachable evidence that the donor intended to make the gift.[71] The onus is on the recipient (plaintiff) to show that the transaction was a gift; and that must be established by proving a clear and unmistakable intention on the part of the donor to make a gift of money to the plaintiff.

In weighing the conflicting evidence it is not sufficient that the preponderance of evidence may turn the scale slightly in favour of a gift. The preponderance must be such as to leave no

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[67] Feeney, Thomas G. & Jim Mackenzie. *Feeney's Canadian Law of Wills*, 4th ed., looseleaf (Toronto: Butterworths, 2000).at 42. [*Feeney*].
[68] *Goodman supra* note 75 *at* 114-115.
[69] *Re: Taerk*, [1957] O.R. 482 (C.A.), *See also Goodman supra* note 75 at 114-115.
[70] *Treadwell v. Martin* (1976) 67, D.L.R. 3rd 493 (N.B.A.D). *Cheese v. Thomas*, [1994] 1 All E.R. 135 (C.A.).
[71] *Dell'Aquila Estate v. Mellof*, [1996] 6 W.W.R. 445 p. 454 (Sask. Q.B.), *Johnston v. Johnston* (1913), 12 D.L.R. 537 p.539 (Ont. C. A.).

reasonable room for doubt as to the donor's intentions. If it falls short of going that far, then the contention of a gift fails.

In *Halsbury's Law of England*,[72] it is stated:

> A gift alleged to have been made by a deceased person cannot, as a general rule, be established without some corroboration ... there is no hard and fast rule that the alleged donee must be disbelieved if uncorroborated. It must be examined with scrupulous care, even with suspicion, but if it brings conviction to the tribunal which has to try the case, that conviction will be acted on.

In addition, it should be noted that the *Ontario Evidence Act*[73] makes it clear that corroborative evidence is required when dealing with actions by or against the heirs of an estate. Section 13 of *Ontario Evidence Act* provides as follows[74]:

> **13.** In an action by or against the heirs, next of kin, executors, administrators or assigns of a deceased person, an opposite or interested party shall not obtain a verdict, judgment or decision on his or her own evidence in respect of any matter occurring before the death of the deceased person, unless such evidence is corroborated by some other material evidence.

FIDUCIARY ACCOUNTING OBLIGATIONS – CASELAW REVIEW

Introduction

Litigation involving fiduciary accounting is often contentious, time-consuming and costly. With parameters set out in the *Trustee Act* and the *Substitute Decisions Act,* the focus on fiduciary accounting has changed fairly dramatically. While the obligations and responsibilities have not significantly been altered there has been a change in the nature of the litigation and the volume of complaints, problems and litigation arising from these circumstances, has increased.

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[72] (4th) Vol. 20 at 15.
[73] R.S.O. 1990, c.E.23.
[74] R.S.O. 1900, c.E. 23, See also B. A. Schnurr, *Estate Litigation – Requirement of Corroboration* 5 E.T.Q. 42.

Attorney's Accounts

There is clear statutory and common law authority for the proposition that a fiduciary or attorney has a duty to account[75].

Section 42 of the *Substitute Decisions Act* provides as follows:

(1) **Passing of Accounts**. – The court may, on application, order that all or a specified part of the accounts of an attorney or guardian of property be passed.

(2) **Attorney's Accounts**. – An attorney, the grantor or any of the persons listed in subsection (4) may apply to pass the attorney's accounts.

(3) **Guardian's Accounts** – A guardian of property, the incapable person or any of the persons listed in subsection (4) may apply to pass the accounts of the guardian of property.

(4) **Others entitled to apply** – The following persons may also apply:

a) The grantor's or incapable person's guardian of the person or attorney for personal care.

b) A dependant of the grantor or incapable person.

c) The Public Guardian and Trustee.

d) The Children's Lawyer.

e) A judgment creditor of the grantor or incapable person.

f) Any other person, with leave of the court.

(5) **P.G.T. a party** – If the Public Guardian and Trustee is the applicant or the respondent, the court shall grant the application, unless it is satisfied that the application is frivolous or vexatious.

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[75] See *Re Taerk supra* note 78, See also *Re Warsh* (26 August, 1994) Toronto, Sheard J. O.J. No. 3234/93 and Rule 74 of the *Rules of Civil Procedure.*

(6) **Filing of accounts**. – The accounts shall be filed in the court office and the procedure in the passing of accounts is the same and has the same effect as in the passing of executors' and administrator's accounts.

(7) **Powers of court**. – In an application for the passing of an attorney's accounts the court may, on motion or on its own initiative,

a) direct the Public Guardian and Trustee to bring an application for guardianship of property;

b) suspend the power of attorney pending the determination of the application;

c) appoint the Public Guardian and Trustee or another person to act as guardian of property pending the determination of the application;

d) order an assessment of the grantor of the power of attorney under section 79 to determine his or her capacity; or

e) order that the power of attorney be terminated.

(8) **Same. -** In an application for the passing of the accounts of a guardian of property the court may, on motion or on its own initiative,

a) adjust the guardian's compensation in accordance with the value of the services performed;

b) suspend the guardianship pending the determination of the application;

c) appoint the Public Guardian and Trustee or another person to act as guardian of property pending the determination of the application; or

d) order that the guardianship be terminated.

This provision is further expanded by section 49(3) of the *Estates Act,*[76] which provides:

> The judge, on passing any accounts under this section, has power to inquire into any complaint or claim by any person interested in the taking of the accounts of misconduct, neglect, or default on the part of the executor, administrator or trustee occasioning financial loss to the estate or trust fund and the judge, on proof of such claim, may order the executor, administrator or trustee, to pay such sum by way of damages or otherwise as the judge considers proper and just to the estate or trust fund, and any order made under this subsection is subject to appeal.

As to the common law authority, the Ontario Court of Appeal in *Re: Taerk*[77] stated:

> It is plain to me that after the amendment to the *Surrogate Courts Act*, as now found in s.772(3), *supra*, a Judge on passing the accounts of an executor, administrator or such a trustee, has jurisdiction to enter into and make full inquiry and accounting of and concerning two classes of property, namely: (the numbering is mine) (1) The property which the deceased was possessed of at the time of his death. (2) The property which the deceased was entitled to at the time of his death. For the purpose of making such inquiry and accounting, a Judge is expressly empowered to "decide all disputed matters arising in such accounting subject to appeal". The scope of the inquiry and accounting which may be lawfully made by a Judge of the Surrogate Court is not limited to the property in possession of the deceased at the time of this death. It extends to and includes property which the deceased was entitled to at that time, and the Judge may decide all disputed matters arising in such accounting in respect of the title to such property. Thus, in my opinion, it was within the scope of s. 72(3) and the jurisdiction of a Judge of the Surrogate Court acting thereunder to enter into and make full inquiry concerning the rights of the deceased at the time of his death to the money, bonds and coupons owned by him in his lifetime and which during his lifetime had passed into the possession of the defendants, or the defendant

[76] R.S.O. 1990, c.E.21.
[77] *Re Taerk, supra* note 78.

> Alexander J, Turk, as the case might be. If, upon such an inquiry, a Judge decided that the deceased was entitled to such money, bonds or coupons or any part of them, he had power under the subsection to compel the executors to make an accounting thereof.

Silver Estate

In Re Silver Estate,[78] the executors of the deceased's estate, where the deceased had prepared primary and secondary wills, were required to pass the accounts under both wills.

Initially, Cullity J. heard the matter on a uncontested basis and held that the application required adjudication on the question of whether or not accounts can be passed where probate has not been granted.

Justice Haley held that there was no requirement that an executor acting under an unprobated will (i.e. the secondary will) who wishes to pass his accounts before the Court, must first apply to obtain probate. Furthermore, the Court held (at paragraph 40) that the executor can be compelled to pass his accounts without probate and on that passing all accounts must be served upon all those with a financial interest in the assets of the unprobated will in question.

The Court held that it is within the Court's inherent jurisdiction that it may supervise executors without probate as well as executors with probate.

Roger Estate v. Leung

In *Roger Estate v. Leung,*[79] the Court considered an application for an order requiring the attorney to account for his actions taken under power of attorney, even though no incapacity of the grantor existed from the date of the grant to the date of death.

The Court held that an attorney has a duty to keep accounts of all transactions that he undertook, and must be ready upon request to produce those accounts. This duty is an ongoing obligation and should not be considered an imposition if an attorney failed in that duty over a long period of time. The attorney's obligation to account is simply that of a fiduciary.

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[78] (1999) 31 E.T.R. (2d) 256.
[79] [2001] O.J.No.2171.

Fair v. Campbell

An important further development in the law in respect to the passing of accounts was dealt with in the decision of *Fair v. Campbell Estate*[80]. In this case, there was an action commenced for an accounting against an attorney and there were allegations of incapacity on the part of the grantor. Allegations of undue influence and fraud were also made. At trial, the Court held that there was no evidence found to support either allegation and, accordingly, held that the attorneys had no duty to account in these circumstances. The Court held that the applicants did not possess sufficient standing to require an accounting and the discretion of the Court to oppose such accounting was refused.

The Court made it clear that an attorney is in fact a fiduciary; however, pursuant to the provisions of the *Substitute Decisions Act*, different duties to account depended upon the capacity of the donor. The Court indicated that a *sui juris* donor was not obliged to involve an attorney in all decisions and therefore the attorney was not required to account for decisions over which he had no influence and for transactions that he did not implement in whole or in part.

As noted above, section 42(1) of the *Substitute Decisions Act* gives the Court the general discretion to order that all or part of an attorney's accounts be passed. The *Substitute Decisions Act* goes on to provide that, outside the enumerated list of parties who can apply, others can also seek leave of the Court to compel a passing of accounts.

Section 42(4)(6) of the *Substitute Decisions Act* provide as follows:

> **42.(4) Others entitled to apply**
>
> The following persons may also apply:
>
> 1. The grantor's or incapable person's guardian of the person or attorney for personal care.
>
> 2. A dependant of the grantor or incapable person.
>
> 3. The Public Guardian and Trustee.

[80] 2002 3 E.T.R. (3d) 67, Langdon J.

4. The Children's Lawyer.

5. A judgment creditor of the grantor or incapable person.

6. Any other person, with leave of the court. 1992, c. 30, s. 42 (4); 1994, c. 27, s. 43 (2).

Filing of accounts

42.(6) The accounts shall be filed in the court office and the procedure in the passing of the accounts is the same and has the same effect as in the passing of executors' and administrators' accounts. 1992, c. 30, s. 42 (6).

Cornacchia v. Cornacchia

In *Cornacchia v. Cornacchia,*[81] the Court held that a person need not be a personal representative of the deceased to compel an attorney to pass accounts, nor does the fact that the person challenging the transaction might benefit personally from doing so preclude them from obtaining an accounting.

Furthermore, the *Rules of Civil Procedure* in Ontario (Rule 74.15)(1)(h)) allows for a person having a financial interest in the deceased's estate to apply to the Court to compel an estate trustee to pass his or her accounts. The Rule defines an estate trustee as "an executor, administrator or administrator with the will annexed," and the term "executor" is not limited to an executor named under a will.

Stickells Estate v. Fuller

In *Stickells Estate* v. *Fuller,*[82] Justice Lack heard an application to compel a passing of accounts from the date of the appointment of the attorney which commenced prior to incapacity. There were concerns and suspicions arising out of the attorney's dealings as there were substantial cheques written to the attorney by the grantor during this period.

The Court ordered the attorney to pass its accounts from April 3, 1995, (the date the *Substitute Decisions Act* came into force), even though the grantor was not then incapable.

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[81] [2007] O.J.No.157 (S.C. J.) at paras17, 20 & 30.
[82] [1998] O.J.No.2940 Ont. Ct. J. (Gen. Div.).

Lack J. notes (at paragraph 13) that s. 42(1) of the *Substitute Decisions Act* does not restrict a grantor, with capacity, to request a passing of accounts. Further, that by natural extension the estate trustee of the grantor, may also request the passing.

Fareed v. Wood

In the decision of *Fareed v. Wood,*[83] the Court continued to consider the issue of the duty of an attorney for property to account.

In *Fareed v. Wood,* a solicitor who was also acting as attorney for property had represented his client for many years. In 1987, the client had made a Will appointing him as Estate Trustee and, in 1992, at 83 years of age, she granted a power of attorney for property to Mr. Wood. The client died in 1999, and Mr. Wood was asked to pass his accounts.

The Court held that an attorney has a duty to account for all transactions during the time of the attorney's involvement, including the time that the grantor may have undertaken transactions herself. Justice Gordon noted:

> It is not uncommon for a grantor to retain the ability to attend to some functions while directing the Attorney to perform others. In some respects, it allows for a transition period as the grantor adjusts to changes in life resulting from age. The separation of responsibilities can co-exist, however, the Attorney assumes full responsibility of all financial activities once he or she assumes some duties. In my view, the Attorney cannot avoid liability by simply saying the grantor paid or transferred her own funds to another.

Executor De Son Tort

Someone who intermeddles in the estate of another may be deemed to be an executor *de son tort.*

It should be noted that an executor may renounce his position at any time, although this right is usually exercised before applying for probate, and the courts are typically reluctant to allow an executor to renounce after having intermeddled in the estate or after having applied for probate.[84]

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[83] 2005 WL 1460361 (Ont. S.C.J.), See also Nimali D. Gamage "Case Comment: Fareed v. Wood 2005 WL 1460361 (Ont. S.C.J.)" (2006) 24:2 Deadbeat 18 (Ontario Bar Association Publication).

As long as the person renounces the office before performing acts that amount to an acceptance of the office, he or she may freely renounce and the Court will then simply appoint an administrator.[85]

However, slight acts of intermeddling, such as paying the deceased's debts, are not typically held to be enough to make a person an executor; they must have the character of an assumption of authority to the office of a personal representative.[86]

[84] *Stordy v. McGregor* (1986), 42 Man. R.(2nd) 237 (Man.Q.B.).
[85] *Feeney, supra* note 76 at 8.2.
[86] *Feeney, supra* note 76 at 8.1.