FINANCIAL POST

If you want to keep wealth in the family, be careful how you bequeath it

The transfer of wealth to an heir must be exercised with caution, paying particular attention to the structure of the gift or inheritance

Caution must be exercised by recipients in using the inherited or gifted funds once they are received if they don't want it to end up in the hands of a spouse in case of divorce.*Illustration by Chloe Cushman/National Post files*

SPECIAL TO FINANCIAL POST

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As the population ages, baby boomers are preparing to make one of the largest transfers of wealth in history. For many families, the underpinning to the transfer of wealth from one generation to the next is the preservation of that wealth notwithstanding the recipient's marriage. Often times, parents or grandparents will want to ensure that if the recipient's marriage comes to an end, the wealth will remain in the family and, more precisely, not be shared by the recipient's spouse.

Ontario's *Family Law Act* makes clear that an individual's property acquired by gift or inheritance from someone other than the recipient's spouse during the marriage will not be shared between married spouses. Simply put, it is excluded from the recipient spouse's net worth that would otherwise be shared by the spouses. Taking it one step further, the *Family Law Act* goes on to provide that property into which the gift or inheritance can be traced will similarly not be shared. Similar rules exist in provinces across Canada.

To ensure the recipient's spouse does not receive one half of the gift or inheritance in the context of divorce, the transfer of wealth must be exercised with caution, paying particular attention to the structure of the gift or inheritance. Even more caution must be exercised by the recipient in using the inherited or gifted funds once they are received. That is particularly the case when the inheritance or gift is invested in a matrimonial home or a joint bank account.

According to the *Family Law Act*, if a gift or inheritance is invested in a matrimonial home (which is a home in which the spouses ordinarily reside at the time of their separation), it will lose its excluded character. In other words, the spouses will share the gift or inheritance if and when they separate. The Ontario courts have applied a strict interpretation of this provision.

In the 2012 case of *Ward v. Ward*, the wife received a gift from her father of $200,000 during the marriage. Of those funds, $180,000 were invested in the matrimonial home. The husband ended the marriage two months later. While the wife expected the husband to repay those funds to her if they separated, the husband denied any such expectation or agreement existed. The Court of Appeal for Ontario confirmed the loss of the exclusion. However, as a result of the windfall to the husband arising from the substantial gift from her father, the wife successfully claimed the parties' assets should be unequally divided between them. While, in *Ward*, the sharing of the gift or inheritance was avoided to some extent through the court's intervention, such a remedy is discretionary in nature and cannot be relied upon in structuring one's affairs and preserving the exclusion of a gift or inheritance.

In order to protect the inheritance or gift with any degree of certainty when the funds are to be invested in a matrimonial home, the recipient spouse ought to consider either a marriage contract (into which the parties can enter during their marriage) or a mortgage registered on title to the matrimonial home in the recipient spouse's favour. Until such time as either is concluded, the recipient spouse ought to preserve the funds in a segregated bank account in his or her sole name. Doing so will ensure the exclusion if the spouses are unable to agree upon the terms of the marriage contract or mortgage.

While the *Family Law Act* does not expressly address the strength of the exclusion in the event the funds are deposited to a joint bank account, the case law has squarely addressed the issue. In *Townshend v. Townshend*, also in 2012, the husband received a $25,000 gift from his mother during the parties' marriage. The husband deposited those funds into a joint mutual fund account he held with his wife. The wife sought to share in those funds while the husband resisted that claim on the basis of the funds being excluded. The trial court found that the

entirety of the gifted funds were to be shared by the married couple. On appeal, however, the excluded nature of the funds was restored. Writing for the Court of Appeal for Ontario, Justice Simmons stated the following:

“Given that the legislature made clear its intention that gifts used to purchase a matrimonial home lose their excluded character, but did not do the same in relation to monies deposited into a joint account, I discern no legislative intent that the entire amount of the gift should lose its excluded character when deposited into a joint bank account.”

The cost of obtaining this decision from the court likely eclipsed the value of the exclusion itself. With that in mind, beneficiaries of an inter-generational transfer of wealth should take notice of the need to properly plan if the intent is to ensure the funds are not shared in the unfortunate event of a divorce.

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