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Disjointed Rights

Two similar cases, two different rulings. Why can't the courts come together on joint accounts?

COURT REPORT

BY JAMIE GOLOMBEK

An issue which perennially rears its ugly head is the topic of joint ownership of assets, specifically "joint tenants with right of survivorship," or JTWROS for short. Under a JTWROS account, which is available in all provinces other than Quebec, upon the death of one of the joint owners the property in the account simply passes directly to the surviving owner and does not pass through the estate.

It is because of this feature that joint ownership is often suggested as a means to avoid probate tax, which in most provinces is based on the value of the assets that pass under the will. Since joint-account assets pass outside the will, their value does not form part of the estate and may be excluded from the calculation of probate tax, where eligible.

Many articles have been written over the years cautioning advisors and their clients on the dangers of using joint-accounts, specifically highlighting some of the risks, which may include: lack of control by the transferor, a potential income tax liability when transferring appreciated assets into joint names (with anyone other than a spouse or common-law partner) and perhaps most importantly, questions that may arise after the death of the transferor regarding his or her true intent in establishing the joint account.

It is this last concern that forms the subject of two Ontario Court of Appeal decisions that will be making their way to the Supreme Court of Canada in December. What's interesting, and perhaps explains why the Supreme Court granted leave to appeal in both joint-account cases, is that the two decisions contradict each other.

This month we will be discussing the first of the two cases namely, *Pecore v. Pecore* (2005 CanLII 31576 (ON C.A.)). Next month, we will examine the second case *Saylor v. Brooks* (2005 CanLII 39857 (ON C.A.)), in which the appellant court reached the opposite conclusion.

THE FACTS

Michael Pecore was injured in a car accident, which rendered him a quadriplegic. Paula was his caregiver whom he eventually married and lived with for 20 years.

Paula Pecore was the youngest daughter of the late Edwin Hughes. Edwin decided in the context of his estate planning that he would bequeath his entire estate to Paula, as her two elder sisters were financially independent.

Consequently, Paula was named as the beneficiary on his RRSP account and life insurance policy. Hughes also transferred an investment account worth approximately $950,000 into joint name with her.

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When Hughes became ill, he decided to move in with Paula and Michael. Within five months, Hughes' second wife died. Michael became too ill to be cared for by Paula alone and moved into a long-term care facility and, not long after that, Hughes died.

Upon his death, the joint investment account was transferred solely to Paula's name. Approximately two years later, Michael initiated divorce proceedings against Paula, moving out of the long-term care facility into a home with his new fiancée. It is as a result of the division of property under the divorce that Michael sued Paula for a share of the $950,000 from the joint-account, claiming that since he was a residual beneficiary under Hughes' will, if the account was part of the estate, he may be entitled to a portion of it.

THE ISSUE

The issue, therefore, is straightforward: Did a true joint ownership exist between the late Hughes and his daughter Paula? If not, as Michael argued, the joint-account assets should have devolved to the estate and as a result, should be distributed among the beneficiaries

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under the will, which included Michael.

Paula maintained that her father's intention was to indeed make a gift to her, establishing her as a true owner of the account and thus, upon her father's death, the assets passed directly to her, bypassing the estate and thus any entitlement by Michael.

THE ANALYSIS

The appeal court concluded that the preponderance of evidence suggested that a true joint ownership existed. Specifically, Hughes named Paula as the sole beneficiary of his RRSP and insurance policy. Secondly, only after the investment account was registered as JTWROS did he name Michael as a residual beneficiary under his will. Thirdly, there was evidence that during Hughes' lifetime, and with his knowledge, Paula withdrew money from that account for her own personal use. This evidence, taken together, supports an actual intention to give Paula a beneficial interest in the account as opposed to merely a legal interest.

The appeal court made an interesting distinction regarding the use of joint ownership as a tool for estate planning as opposed to a tool of convenience to allow a child to manage funds or pay bills for an elderly parent. The court found that since Hughes also gave his daughter Paula a power of attorney, which provided her with the authority that was needed to pay bills and make investment decisions, this would have negated the need to make the investment account JTWROS unless "Hughes intended something more; to ensure the investments were given to Paula and to avoid probate fees, both entirely legitimate purposes."

TAX CONSEQUENCES

What's most interesting from a tax point of view is that, according to the testimony, at some point, Hughes learned that transferring assets into joint ownership with his daughter could possibly trigger a capital gain. This is consistent with the *Income Tax Act* and the Canada Revenue Agency's longstanding administrative position, articulated through numerous technical interpretations surrounding the consequences of joint ownership.

Hughes therefore obtained some advice and sent a letter directly to the financial institution that held the account that said that the transfer was "made for probate purposes and, accordingly, no changes should be made to the adjusted cost base of the investments because, he said: 'I am the 100% owner of the assets and the funds are not being gifted to Paula.' "

This statement certainly seems at odds with the appeal court's finding that the transfer into joint ownership was legally effective, confirming that, notwithstanding the letter, "the trial judge was satisfied on the evidence that Hughes still intended to gift the investments to Paula."

The testimony also indicated that Hughes continued to pay income tax on the money earned on the investments at a higher rate than would have been the case had the income been taxable in Paula's hands. As the judge summarized, "any improper attempt by Hughes to defer taxes is a matter between his estate and the tax department. It is not a matter that bears on Michael's claim against Paula."

Stay tuned next month in which a different result was reached on very similar facts, in the Saylor v. Brooks decision and keep in mind, that in both cases, the Supreme Court will have the final say when it hears both cases in December. AER

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NEW TAX RELIEF (+ One Increase)

In May, the federal government announced more than $26 billion in tax relief over the next two years. Here's how the first round of tax cuts shakes out as of July 1:

- About 655,000 low-income Canadians became tax exempt.
- The GST was reduced to 6% from 7%.
- The Canada Employment Credit worth up to $500 to help pay for things like uniforms, computers or safety gear came into effect. This jumps to $1,000 next year.
- Canadians who buy monthly transit passes will receive about $150 a year in federal tax relief.

Increasing:

- The lowest personal income tax rate was inched up to 15.5% from 15%.

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