Family Law Considerations for Intergenerational Transfers

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Family lawyers and real estate lawyers tend to act for the same clients. After all, families need homes to live in. Family members are often financially interdependent and intermingle their assets and incomes without regard to legal forms or obligations. Motivations shift over time along with family dynamics. While there is a temptation to shy away from addressing the awkward possibility that spousal relationships between family members may both be formed and come to fail over time, it makes good sense to consider family law repercussions and, where possible, protect against unwelcome outcomes. This paper addresses some key family law principles to keep in mind when acting on intergenerational transactions.

Family Property Law

In Ontario married spouses have a right to share in wealth generated during a marriage, with certain restrictions.[1] This right may be exercised at separation or at death. The three equalization provisions that come up most frequently in real property transactions are the exclusion of assets gifted or inherited during the marriage, the deduction of the value of assets brought into the marriage,

[1] Part I of the *Family Law Act,* R.S.O. 1990, c. F.3

and the special treatment of the matrimonial home. Spouses may contract out of equalization rights by marriage contract but such agreements are only enforceable if scrupulously negotiated with full financial disclosure, and, preferably, independent legal advice for both spouses.

(i) Exclusions and Deductions

Equalization creates a debt obligation between the spouses as of the separation date (or the day before death). Each spouse's net family property is calculated by deducting the net worth at the date of marriage from the net worth at the date of separation. The spouse with the greater net family property owes an equalization payment to the other spouse calculated as half the difference between their respective net family property. If a spouse owns a property at the date of marriage he or she receives a deduction for the value of it as of that date. The growth (or decline) in value is then shared with the other spouse through equalization. However, if a spouse receives an asset by gift or inheritance during the marriage and that asset still exists at the date of separation or is traceable to another asset at the date of separation, then the value is excluded from equalization. The interplay of these provisions creates an anomaly. If a spouse owns an asset at the date of marriage, the deduction is fixed and all increases in value during the marriage are shared through equalization. This is so even if the spouse had received that asset as a gift before marriage. If a spouse receives an identical asset by gift after the day of marriage then the full value of that asset at the time of separation or death will be excluded. The outcome may differ enormously by the happenstance of the timing of the gift.

(ii) *Matrimonial home*

A matrimonial home is a defined term under the legislation. It is a property in which a spouse has an interest and which was ordinarily occupied as a family residence at the time of separation.[2] During the marriage, spouses have possessory rights to a matrimonial home which cannot be taken away by contract. Both spouses must consent to any encumbrance or sale of a matrimonial home. The character of a property may change over the course of a marriage. The possessory rights and rights against alienation are ongoing during the marriage. The special treatment of matrimonial homes in equalization, however, concerns only those properties which meet the definition as of the date of separation or at death. For these homes, a spouse may not claim a deduction for the value as of the date of marriage, nor may he or she claim an exclusion for the property or any funds traced into the property.

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[2] *Family Law Act, s18 (1) Matrimonial home – Every property in which a person has an interest and that is, or if the spouses have separated, was at the time of separation ordinarily occupied by the person and his or her spouse as their family residence is their matrimonial home.*

The legislation extends the definition of matrimonial homes to properties held within a corporation in which a spouse owns shares.[3] Properties held within a trust do not fall within the definition of matrimonial home, however. The Ontario Court of Appeal has held that a home occupied by a spouse and her family as their family residence is not a matrimonial home where the property was held by a trust of which the spouse is both beneficiary and trustee.[4]

Couples may have any number of matrimonial homes including recreational properties such as cottages and ski chalets. Whether a property is a matrimonial home or not depends on whether it has been used by the spouses and, if so, whether it has been used as a family residence. Using a cottage or chalet on weekends or holidays will be sufficient to meet this test.[5]

Family Wealth Transfers

The technical rules related to family property law usually come into play at the end of a spousal relationship. During the marriage family members may transfer assets or funds to children or grandchildren without giving much thought as to the form or even substance of the transfer. Whether it

[3] *Family Law Act, s. 18(2)*
[4] *Spencer v. Riesberry* 2012 ONCA 418
[5] *MacFarland v. MacFarland* 2009 CarswellOnt 2949 (Ont.S.C.)

is intended to be a gift or a loan may be unclear to the parties even at the time. Years later seen through the partisan lens of a failed marriage, it may be difficult to determine whether a transaction was a gift or a loan. Decisions made without regard to whether a property is, or may become, a matrimonial home may lead to unwelcome consequences. Whether a transfer was a gift, a property was retained on a resulting trust or a loan is often a point of dispute.

(i) *When is a transfer a gift?*

A valid gift has the following requirements: (a) an intention by the donor to make a gift, without consideration or expectation of remuneration; (b) an acceptance of the gift by the donee; and (c) a sufficient act of delivery or transfer of the property to complete the transaction.[6] A written deed of gift is not essential but is of enormous value if the nature of the transaction must be proven at a later date. In the context of equalization claims a spouse may need to prove a gift to obtain the benefit of the exclusion and there may even be a dispute about whether the gift was to one of the spouses or to both.

(ii) *When is a property held on resulting trust?*

In the context of a divorce, a spouse may argue that an asset held in his or her name is actually for the benefit of the transferor. For example, if a mother transfers a home to her adult son without consideration, was this intended as a gift or is the property held by the son for his parent on a resulting trust? This may be of great significance if the property was

[6] *McNamee v. McNamee* 2011 ONCA 533

transferred before marriage and has increased in value significantly or if the property were a family cottage falling within the definition of a matrimonial home. Where an asset is transferred without consideration equity presumes a resulting trust.[7]

(iii) When is a family loan valid and enforceable?

Payments by family members to spouses during marriages may not be clearly identified at the time of the advance. Post – separation one spouse may have a strong incentive to characterize payments as a gift, while the other wishes to characterize the payments as a loan. The relevant factors to deciding whether a payment was a gift or a loan are:

- Whether there were any contemporaneous documents evidencing a loan;
- Whether the manner for repayment is specified;
- Whether there is security held for the loan;
- Whether there are advances to one child and not to others, or, on the contrary equal advances;
- Whether there has been any partial repayment; and,
- Whether there was an expectation or likelihood of repayment. [8]

[7] *Pecore v. Pecore* 2007 SCC 17
[8] *Barber v. Magee*2015 ONSC 8054 at para 24

Even if found to be a loan, there may be a question of enforceability. Family loans in the form of a demand on which neither payments nor acknowledgement have been made over two years after the demand has been made will fall afoul of the *Limitations Act*. [9]

How to Avoid Trouble

Keeping the above legal principles in mind at the time that family financial arrangements are made will minimize future problems. The nature of a transaction needs to be understood and, preferably, properly documented. If transfers are made to a child then whether that child is married or not, the impact of a future marriage needs to be considered and steps taken to protect and warn against obvious pitfalls. If a property that is or may be a matrimonial home is involved in the transaction then the adult child may need to consider entering into a marriage contract if that is possible. If an advance is intended to be a loan, that intention should be made clear, in writing, and that loan should be properly managed, not ignored until years later when family conflict has arisen. The family law implications of intergenerational transfers may at times be unavoidable but, at least, they should not come as a surprise to those involved. Real estate and family lawyers ideally should work together to plan and advise the family members as to how best to achieve their goals.

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[9] *Limitations Act, 2002*, S.O. 2002, c. 24, Sched. B, as am. s. 5(3) and (4)

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