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## Estate Planning in Turbulent Times

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With more than two-thirds of all Canadians self-isolating in a collective effort to flatten the COVID-19 curve of infection, estate planning is one of a number of planning considerations that are top of mind. Regardless of whether individuals already have a plan in place or have yet to commence the estate-planning process, the current, unprecedented circumstances provide opportunities for effective planning and have made it even more important for professionals and clients alike to reflect on current (or proposed) succession planning.

### Wills, Mandates and Powers of Attorney

**As a preliminary matter, clients and advisors should ensure that any estate-planning documents are up to date.** This analysis may involve assessing the composition and profitability of marketable investments; evaluating fixed assets; determining the recoverability of debts; and ensuring that the testator's estate-planning objectives remain attainable. It will also be important to review the current tax residence and domicile of executors and beneficiaries to ensure that adequate safeguards are put in place to avoid unintended tax consequences, such as U.S. income tax. In this regard, clients should also examine their wills to ensure that executors are provided with sufficient powers to address potential planning issues that can arise after death. Individuals and estates with cross border issues, such as U.S. family members or assets, may require more careful attention in light of current circumstances.

**Clients should also ensure they have up-to-date mandates in the event of incapacity (in Québec) or powers of attorney (in Ontario), both for the administration of one's property and one's health (i.e., a living will).**

As of April 1, 2020, Québec notaries are permitted to notarize documents remotely.<sup>1</sup> Similarly in Ontario, an emergency order was made under the *Emergency Management and Civil Protection Act* to permit the virtual witnessing of wills and powers of attorney over audiovisual communications during the province's state of emergency (which is intended to be revoked on May 6, 2020, unless extended).<sup>2</sup> If Ontario wills are witnessed virtually, one of the witnesses must be a member in good standing of the Law Society of Ontario at the time of the signing.

### Estate Freezes and Refreezes

An estate freeze is commonly implemented by many Canadian business owners to reduce the tax liability arising on death. An estate freeze consists of a corporate reorganization pursuant to which the value of the owner's interest in the business or holding company is *frozen* at a particular point in time and exchanged for fixed-value preferred shares (Freeze Shares). The result is that future growth of the business will accrue to new common shares issued in the course of the reorganization – generally to the owner's children or grandchildren, often through a trust.

**Individuals contemplating an estate freeze can reduce taxes resulting from the deemed disposition of the Freeze Shares on death by freezing the value of their estates at a time when values are suppressed.**

In the event that an estate freeze was previously implemented, the owner's Freeze Shares may have declined to a value that is substantially lower than their redemption amount due to current economic conditions. **Owners should consider whether this would be an appropriate time to *refreeze* their interest in the business at a lower value, thus further reducing gains on death, or alternatively to *thaw* part of the freeze so that they can access additional liquidity.** For example, assume an individual had frozen the company at a time when the shares had a fair market value (FMV) of \$10 million, taking back preferred shares with a fixed value of \$10 million, with future growth accruing to a family trust for the benefit of his or her descendants. If the FMV of the corporation decreases to \$7

million, on a refreeze, the owner would take back preferred shares with a fixed value equal to the lower FMV, so that the gain on death would be based on the \$7 million valuation.

## Loss Carryback Planning

The *Income Tax Act* (Canada) generally deems a taxpayer to have disposed of all of his or her assets on the date of death for proceeds equal to the FMV of such property immediately before death, triggering any unrealized capital gains. **To the extent that the value of the assets has declined in the first taxation year following death, executors should consider crystallizing those losses, which can be carried back to the deceased's terminal return.**<sup>3</sup>

## Contributions to Family Trusts and Gifts: Depreciated Assets

When a taxpayer transfers property to an *inter vivos* trust or makes a gift to related persons, the transfer is generally deemed to have occurred at FMV, triggering any inherent gains. **If the value of an asset has decreased to the extent that there is no longer an inherent material gain, it may be an opportune time to gift such property to children or other family members, or to transfer it to a family trust.**

## Capital Dividend Planning

Dividends paid out of a corporation's capital dividend account can be received free of tax by Canadian resident shareholders. **Owners expecting to incur capital losses should consider paying out the full balance of the capital dividend account (in cash or by way of note) before crystallizing losses,** which could potentially reduce the capital dividend account balance or the ability to pay tax-free capital dividends within a corporate group.

## Canadians Stranded Abroad

Many Canadian "snowbirds" escaping the harsh northern winters avoid U.S. tax residency by carefully monitoring and counting the number of days they are physically present in the United States during any given taxation year. In light of the international travel restrictions imposed by COVID-19, many Canadians may be unable to leave, or feel uncomfortable leaving, the United States, and therefore risk obtaining U.S. tax residency if their physical presence in the United States exceeds 183 days, commonly referred to as the "substantial presence test."<sup>4</sup>

The IRS has issued procedures (Revenue Procedure 2020-20) for eligible individuals to claim a COVID-19 medical condition travel exception for purposes of the substantial presence test, under which **eligible individuals may exclude up to 60 consecutive calendar days from the day count for the purpose of applying the substantial presence test if they intended to leave the United States but were unable to do so because of COVID-19-related travel disruptions.** Read our [bulletin](#) for more about the eligibility requirements.

<sup>1</sup> See Order 2020-010 issued by the Québec Minister of Health and Social Services on March 27, 2020.

<sup>2</sup> O. Reg. 129/20: *Order Under Subsection 7.0.2 (4) of the Act [Emergency Management and Civil Protection Act] – Signatures in Wills and Powers of Attorney*, April 7, 2020. The order was further amended by O. Reg. 164/20, dated April 22, 2020, which confirmed that the requisite signatures for both wills and powers of attorney may be made by signing complete, identical counterpart copies thereof, which together are deemed to constitute the will and/or powers of attorney.

<sup>3</sup> In a webinar with the *Association de planification fiscale et financière* (APFF) on April 14, 2020, both the Canada Revenue Agency and Revenu Québec confirmed that the delay for filing the loss carryback election otherwise due between March 18 and May 31, 2020, has been extended to June 1, 2020.

<sup>4</sup> The substantial presence test determines U.S. residency for the current taxation year by adding together (i) the number of days the individual was present in the United States in the current year; (ii) 1/3 the number of days he or she was present in the United States in the preceding year; and (iii) 1/6 the numbers of days he or she was present in the United States in the second preceding year.

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