Ontario Court Examines Estate Planning Challenges Posed by Corporate-Structures
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The Estate of John Kaptyn has given rise to a number of court applications. Notably, the issue of testamentary capacity was decided in a 2008 decision of the Ontario Superior Court of Justice (2008 CanLII 53123). Recently, the interpretation of certain aspects of the testamentary documents was the subject of an application by the co-executors for the opinion, advice and direction of the court (2010 ONSC 4293). While there were a number of interesting questions of interpretation, the comments in this article focus solely on certain issues arising from challenges to corporate structure used in fashioning testamentary gifts.

The late John Kaptyn was said to be an astute businessman with an understanding of tax and real estate issues. He left an estate valued in the range of $75 million, largely comprised of real estate. The deceased had two sons (who were the co-executors) and five grandchildren. One son, Simon, had two sons. The other son, Henry, had three children. The deceased disposed of his property by two Wills – a Primary Will and a Secondary Will – which were amended by codicils a few weeks later; all shortly before his death.

Sometime during the year before his death, the deceased had decided to generation-skip. As summarized by the Court in the testamentary capacity action (see above at paragraph 29), the testator wanted his real estate assets to be distributed to his grandchildren. He wanted his wife looked after and to make some charitable donations. The residue would go to his sons. The Court also found that the testator intended that the two sons' families be treated the same and there was to be no shared ownership between them.

The deceased did not own real estate directly. Instead, the real estate was owned by corporations of which he was the sole or controlling shareholder. To achieve his intention of treating each son's family the same, it appeared that he first identified certain real estate to pass to Simon's children. The deceased was the sole shareholder of a numbered company that was a 50% shareholder of a corporation and a 50% partner of a partnership, both of which owned hotels. The other shareholder or partner was a corporation whose sole shareholder was his son, Simon. Presumably the deceased considered it logical to provide that same pass to Simon's children to consolidate the hotel ownership within Simon's family. Then the deceased sought to provide for real estate of equal value for the children of his other son, Henry. However, the identified real estate was not only corporate owned, but owned by a subsidiary named Captain Investments Inc., of a holding corporation which owned other assets too. In addition, the equal treatment of the two families resulted in one property referred to as the Hensin property being identified for Henry's children and another property being 650 Highway 7 East being identified for Simon's children, yet both were owned by a single corporation-West Beaver Creek Management Limited.

On application to the court, some parties advanced the position that the deceased's gifts failed or adeemed because he did not own those assets at death. Specifically, the argument was advanced that the gift of the Hensin property to Henry's children failed because such property was owned by West Beaver Creek Management rather than the deceased.

The same argument was advanced with respect to the gift of 650 Highway 7 East that was also owned by West Beaver Creek Management rather than the deceased. And similarly, it was argued that because the deceased did not own shares of Captain Investments Inc. but rather owned shares of its holding company, the gift of Captain Investments Inc. should also fail.

The Court found that the deceased's intention was "clear and unambiguous" to pass certain assets to certain grandchildren. The Court held that this was not a case where the deceased did not own the assets in question so he could not deal with them.

Somewhat rhetorically, the Court asked " … who else on the face of this earth could gift those assets through a Will?" With respect, this seems to confuse ownership and control. However, on the foregoing basis, the Court held that the sole issue was the adequacy of the language used by John Kaptyn in his Will to implement his intention.

Using the gift to Henry's children as an example, the relevant section of the Will had not merely gifted the real estate by name or address. Rather, the gifting language referred to "… any interest that I may have, including without limitation, my shares of stock, whether common, special or preferred, owned by me in" the Hensin property and Capital Investments Inc. The Hensin property was owned by a corporation that in turn was owned by the deceased.

Captain Investments Inc. was owned by a holding company, Marktur, whose common shares were owned by the deceased. The Court found that the gifts did not fail because of the expansive nature of the phrase "any interest". Further, the Court noted that the extensive powers given to the executors under the Will should enable the executors to take the necessary corporate steps to give effect to the gifts.

During the deceased's lifetime, a tax-deferred reorganization might have been possible to segregate assets into separate single purpose corporations, whose shares could have been gifted to particular grandchildren. This was apparently identified in the last few weeks of John Kaptyn's life but likely too late to implement. In any event, the evidence at that point reflected that he was satisfied that the tax be paid to enable the grandchildren to receive the real estate. The Court held that any resultant tax was to be paid from the residue just as the taxes resultant from the deemed disposition immediately before death were to be paid.

It is axiomatic that a shareholder of a corporation does not own the assets of the corporation. In this case the Court considered that the shareholder (being the testator) had "an interest" in the assets of the corporation and fortuitously, the language of "an interest" was used in the gifting provision. The case serves as a reminder that a testator and the drafter must have a clear understanding of the testator's corporate structure to ensure proper and adequate description of assets and to assess the consequences of corporate ownership of any assets that the testator might wish to deal with on a segregated basis. Better yet, there may be an opportunity to effect a corporate reorganization during the testator's lifetime to facilitate his/her testamentary wishes and thereby avoid triggering more tax and complexity in the aftermath of death.

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