Hull on Estate and Succession Planning Podcast #49
Protecting Your Children's Inheritance

Posted on February 27th, 2007

Suzana Popovic-Montag: Hi, and welcome to Hull on Estate and Succession Planning. You are listening to Episode #49 of our podcast on Tuesday, February 27th , 2007.

Welcome to Hull on Estate and Succession Planning, a series of podcasts hosted by Ian Hull and Suzana Popovic-Montag, that will provide information and insights into estate planning in Canada, from the offices of Hull Estate Mediation in Toronto, Ontario, Canada. Here are Ian and Suzana.

Suzana Popovic-Montag: Hi there Jordan.

Jordan Atin: Hi Suzana.

Suzana Popovic-Montag: Thank you very much, Jordan, for joining us today. Although Ian is normally sitting beside me and talking about our estate planning techniques and considerations and things of that sort, unfortunately Ian is not available this week. So I thank Jordan Atin, who is going to be my co-host this week and I look forward to speaking with him about some very interesting ideas about how to protect your kids from blowing basically their inheritances.

Jordan Atin: Well, thanks again Suzana, for inviting me to speak about this topic. I know that when I sit down with my clients who are planning their estates, one of their major concerns is the whole idea that their kids are going to blow their money that they're leaving for them, and that they've protected for them for all these years and now, when they give it over, they are concerned it's either going to be spent unwisely or it's going to end up as part of a divorce settlement or something like that. So I know that certainly that's what they're concerned about.

Suzana Popovic-Montag: And are there some interesting mechanisms or ways that people can plan for these kinds of possibilities, Jordan?

Jordan Atin: Well, for sure. The first sort of common scenario is the idea that if you have children who are under 18, most people don't want their kids to get the inheritance when they turn 18, which would be the default position in Ontario, that as soon as a kid turns 18, they get all their inheritance. Well, when I, I remember back to when I was 18 and although I probably would have liked a huge inheritance, I know that probably wasn't a good idea. So a common technique would be for a parent to say they don't get, their kids don't get the inheritance until they are some older age, for example, 25 or 30 or even, I've had parents who say, I don't want my kids to get anything until they are 40. So that's one technique, and the other part of it is that they may want to stagger the payments, so that if they blow the money in the first time, there is another chance for them to get some money.

Suzana Popovic-Montag: And that, I guess, would be based on an assumption that over time, people will become more and more responsible and fiscally knowledgeable about what they are doing with their finances.

Jordan Atin: Yeah, exactly. And the other thing is it gives them a chance to blow some money at different stages, so for example, let's say the parents say, okay, at age 21 I'm going to give them a quarter of their inheritance. And then if they blow that, you know, I'm going to give them a third of their inheritance later on, when they are 25, and maybe the balance at 30. And there, they've got three shots not to screw up their inheritance.

Suzana Popovic-Montag: And I guess in the meantime, the idea is not that they would have a big entitlement, but that there would be an income flow, which is a much more regularized payment, and much more contained. So that they will have enough to get by but not enough to essentially blow.

Jordan Atin: Exactly. Like you would typically allow the, especially while they are under 18, you would allow the money to be used for their support, would go to their guardian perhaps to, you know, make sure that they are educated and fed and all those necessities of life. But that there wouldn't be a huge capital, you know, lump sum of money that they could go and buy a Ferrari with. And, although a Ferrari probably wouldn't be a bad investment but it may be a Hyundai or something like that, and blow the money that way.

Suzana Popovic-Montag: Well, that's interesting. Well that's a great suggestion and I know that certainly in our practice, we've seen a lot of those kinds of trusts set up. What about some other planning ideas, Jordan?

Jordan Atin: Well, from time immemorial parents have wanted to encourage their kids to be good citizens and not rely on their wealth that they inherit. And so we've created these ideas of what we call incentive trusts, and basically that's a way of saying to your kids after you are gone, look, I want you to still be working, I don't want you to just fall back and rely on the inheritance that I've left you. So we're only going to give you more money out of the inheritance if you can prove that you're employed, for example, or that you are making contributions to society in some other way. Maybe you are doing charitable work, or you are doing work for needy people or those sorts of things. And so you incentivize the beneficiaries to do what the parents consider to be socially responsible activities and then the more they do that, the more money they get from their trust.

Suzana Popovic-Montag: That's a great idea. Do you see a lot of that kind of trust being used in planning?

Jordan Atin: It's certainly bigger in the United States, where it was first developed. They are tricky to work out because you don't know exactly what you want your kids to do and you are leaving it in the hands of usually the trustee to decide what is going to satisfy those requirements. There is also, whenever you use a trust, there's the feeling from the beneficiaries that Mom and Dad are still trying to…

Suzana Popovic-Montag: Control.

Jordan Atin: Control me, exactly Suzana, and still attaching strings and won't, you know, even when they're gone they're still trying to decide what I'm going to do. So one has to be careful about using trusts and the psychological effect that it is going to have on the beneficiaries.

Suzana Popovic-Montag: How about from a family law perspective, Jordan, once individuals get married, is there anything that parents can do to sort of protect a child's inheritance from perhaps that spouse inheriting it or taking it or benefiting from it at the expense of the child?

Jordan Atin: Yeah, that's another major concern of most parents that they don't want their child's spouse to get their hands on the money if the marriage should break down. It depends really on where you live. In Ontario, for example, inheritances are not included when you are dividing property after you separate or divorce. So, for example Suzana, if you and I were married and I inherited money from my parents and then we separate, you wouldn't get a share of that inheritance. Now that's the general rule, but there are exceptions.

Suzana Popovic-Montag: Can you tell us about some of those exceptions?

Jordan Atin: Yeah, sure. For example, if, in Ontario again, this depends on where you live but in Ontario if you take the money that I inherited. Let's use that same example where you and I are married and it would be my pleasure, Suzana. And you, although I am married already so I think that's illegal but…

Suzana Popovic-Montag: Well, we'll have to be careful about that.

Jordan Atin: We won't tell anybody. So basically, if I took that inheritance that I got from my parents, for example, and put it into the matrimonial home. For example, I paid off the mortgage or I used that money to buy a matrimonial home, then I would lose that exclusion of the inheritance and if we got separated, then you would be still entitled to half of the matrimonial home, for example. And then automatically basically, you would be getting part of my inheritance because it was in the matrimonial home. Similarly, with joint accounts. If I took all that money and put it in a joint account with you, I lose that exemption that's provided for inheritances.

Suzana Popovic-Montag: You know, those are interesting comments because it sort of brings to mind the fact that, you know, once you suddenly come into perhaps a big share of money, you may want to seek some form of maybe legal advice in terms of protecting that yourself and how to, in addition to the financial advice that people will often times seek, you may want to also consider what and how to protect that down the road if need be.

Jordan Atin: I think that's an area that a lot of people overlook as beneficiaries. That they are not, when you are a beneficiary, you have legal rights and there are obviously areas where you should be getting advice, because you could really, really screw up your situation if you don't go out and get some advice. It's something that we encourage beneficiaries to get.

Suzana Popovic-Montag: And sooner rather than later, too, I think.

Jordan Atin: Absolutely.

Suzana Popovic-Montag: Do you have any other thoughts, Jordan, from the planning perspective, of what parents can do, for instance, to protect children and what they are going to come into, particularly in those situations where there is going to be a very large inheritance.

Jordan Atin: Yeah, well there is a lot of material on the Web certainly about these advisors. Advisors for beneficiaries because you are in a whole new, I mean a beneficiary comes into a large sum of money is in a whole new ballpark. And they may not be familiar with investments or any of that stuff. If it's not in a trust, then they are going to be the ones responsible for investing that money, for deciding how to spend it and how to donate it if that's their choice, and things like that. And so beneficiaries are wise to get, not only legal advice on what they are going to do about their money, but also to get investment advice and to speak with professionals who can help plan the best tax efficient way of dealing with that, but also how it's going to affect their lifestyle.

Suzana Popovic-Montag: Just before we wrap up, Jordan, I was wondering if you could just take a few minutes to consider maybe some charitable giving techniques or things that people might want to do in these circumstances, that might also be beneficial.

Jordan Atin: Right, well, I mean it depends on where you live of course. There are all kinds of tax benefits to setting up trusts for charitable purposes. There are donation credits, there are tax credits that one gets if they donate money. So, for example, if you have a large tax obligation when you were to pass away, one way of alleviating some of that tax burden is to make charitable bequests right in your Will. And they have to be done in a certain form and way but if you do it correctly, you can use that money that you are donating to credit against the tax that you would ordinarily owe.

Suzana Popovic-Montag: Well, that's great. And have you had a lot of experience with people using charitable foundations in their estate planning?

Jordan Atin: Well we are seeing more of that, certainly as there is more and more wealth. But the idea, of course, behind a charitable foundation is that there is some discretion, generally. For example, if I had $5,000,000 and I wanted to set up a charitable foundation, I would, either in my Will or just while I am alive, I would set up a trust. It's basically a trust, although it can be done through a corporation, and you are saying to your trustees, I'd like you to take this money, invest it and then use the income to benefit different charities. And so there is discretion and you can guide the trustees on where you want that money to go, it's flexible and there are all kinds of regulations, of course. But that's one way, certainly, of, and you can get tax benefits while you are alive if you set it up during your lifetime. So that's one way of doing good for society and doing good for your own tax position.

Suzana Popovic-Montag: And that's always a good thing. Well, Jordan, thank you very much for taking the time to join us here today. I think you did a great job filling Ian's shoes and thank you for your expertise.

Jordan Atin: It was my great pleasure, thanks Suzana. Bye-bye.

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