

Parting ways

Re-establishing financial security at the end of a relationship



With the breakdown of your marriage or common-law relationship, you will want answers about your rights and obligations around crucial issues: spousal/partner support, child support, and property — especially the family home. What impact will relationship breakdown have on your Will, your Powers of Attorney and your beneficiary designations, among other tax and estate-planning issues?

Your TD advisor will be able to provide critical support through this difficult time, in concert with the work you do with your lawyer, and perhaps a tax specialist.

The first steps to renewed financial stability

The **first step** on your new road is establishing your *relationship status*. Are you facing divorce or the end of a common-law relationship? The **second step** will be establishing your province or territory of residence. These two steps will point you in the direction you head next. Here is a general overview of *key legal issues* when it comes to relationship breakdown and building financial stability:

Defining your relationship

- Marriage is defined by federal legislation, but the provinces and territories are given the right to regulate the “solemnization” of marriage (the ceremony; who can marry — based on age, familial connection, and consent).
- Common-law partnerships are regulated by the provinces and territories. Most require cohabitation and a conjugal relationship that has been established between 1 and 3 years, depending on the respective legislation. Many provinces and territories will automatically designate a relationship as common-law if you have a child together. In some jurisdictions, you can register your common-law partnership as an indication of your joint intent to live common-law.

Support

- The federal *Divorce Act* deals with spousal and child support, and provides guidelines for both.

For more information on spousal support, please see: www.justice.gc.ca/eng/fl-df/spousal-epoux/ss-pae.html

For more information on child support, please see: www.justice.gc.ca/eng/fl-df/child-enfant/index.html

Division of family property

- Provincial and territorial statutes deal with the division of property, and how claims for property are handled, depending on the status of your relationship. While there is no legally mandated time within which a spouse has to make an application for spousal support, applications for the division of family property, must usually be made within two years of the date of your divorce.

Consult with your lawyer regarding your obligations and rights regarding support and family property under the family law legislation where you live. Then, speak with your advisor about recalibrating your Wealth Plan as required.

- Family law matters use an “**equalization**” formula to settle both spousal support and asset division between partners. For example, with respect to the **family home**, one spouse may be the only party registered on title. However, the value of the home will become part of the overall calculation regarding how the property will be split between the partners, unless you have a cohabitation agreement which allows you to contract out of this requirement.

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However, not all assets necessarily fall into the “equalization” calculation. For example, if an **inheritance or gift** has not co-mingled with the family property or money such as the family home or a bank account, they will not be part of the equalization calculation. The Court will require that the gift or inheritance is shown to still be in existence at the date of separation. You can ensure neither will be included in the equalization by opening a separate account for the money and depositing it.

Review the assets that will be included in the equalization calculation with your lawyer. Then, your advisor can assist with recalibrating your Wealth Plan as required.

Dissolution of the relationship

- Spouses can separate without a legal separation agreement, and continue to live without pursuing a formal divorce. They can have their own written or spoken agreement, with or without the approval of a Court. A divorce order will not be issued by the Courts until the couple has lived “separate and apart” for at least a year.
- Other than the *Divorce Act*, the key piece of federal legislation affecting your post-relationship status will be the *Income Tax Act (ITA)*. You are required to report the change in your relationship status to the Canada Revenue Agency (CRA).

When a Québec couple separates

Under the *Civil Code of Québec (the Code)*, the rules governing the division of family property, or “the family patrimony”, apply whether the couple has entered into a marriage or a “civil union”.

A “*de facto*” relationship (known as common-law in Canada’s common law provinces) is when a couple has not entered into a marriage or civil union. In Québec the law does not provide *de facto* partners protection for property rights, unless they have signed a cohabitation contract that establishes those rights.

The family patrimony is considered to belong in equal shares by both spouses, regardless of whether only one spouse actually owns the property. The property division rules are applied when separation, annulment, divorce or death occurs.

The following is **considered to be part of the family patrimony**:

- all residences used by the family (e.g., house, condominium, cottage) or the rights which bestow use of them;
- furniture used by the family in the residences;
- motor vehicles used for family transportation;
- benefits accumulated in a pension plan or Registered Retirement Savings Plan (RRSP) during the marriage or civil union;
- earnings registered during the marriage or civil union under a pension plan.

The following property is **not** included in the family patrimony:

- property received by one of the spouses as a gift or inheritance prior to or during the marriage or civil union;
- appreciated value of this property during the marriage or civil union;
- property for the *exclusive use* of one of the spouses (e.g., computer, musical instrument);
- businesses and farms (except their residential portion);
- cash and bank accounts;
- savings bonds, treasury bonds, stocks and other investments.

Once the value of the property to be divided is established, the spouse with the highest value must compensate the other spouse for the difference:

- in cash;
- by transferring ownership of property equal in value to the amount owed; the property transferred may come from outside the family patrimony.

These methods of compensation may be combined to settle the division obligations.

Renunciation of property rights

A spouse may not through a marriage or civil union contract renounce their rights to the family patrimony. However, a spouse may make a legal declaration to do so during the course of legal proceedings, or following a judgment, for:

- legal separation;
- annulment of a marriage or civil union;
- dissolution of a civil union, or;
- divorce.

The declaration or judgment must mention the renunciation. To take effect, a renunciation must be entered in the *Register of Personal and Moveable Real Rights* within one year from the time when the right to division of the patrimony arises. If not, the renouncing spouse is deemed to have accepted the division.

Preparing to see your TD advisor

Several documents will help your advisor provide you with solid financial advice:

- If your relationship was *common-law*, did you have a cohabitation agreement? Bring that to your advisor's office. Similarly, if you were married and had a marriage contract, bring it along.
- What about your rights to the *family home*? Bring a copy of the Deed and mortgage to establish ownership, if any, and the rights which ensue.
- What other *assets were purchased in the context of the relationship*? Bring documentation that establishes ownership.
- What are your shared and individual *credit/debt* obligations? Bring your statements.
- Did you and your Partner have private or employer *insurance* policies that may be affected by relationship breakdown? Bring a copy of each policy so you and your advisor can assess your insurance needs going forward, and review whether you wish to change your beneficiary designations.
- Do you have a *Will*? Did you make your Partner a beneficiary? Did you give your Partner *Powers of Attorney* over your personal care and property (should you become incapacitated)? You will likely want to review these documents and make changes as appropriate with your lawyer. Then discuss them with your advisor to work out the impact on your planning.
- You and your Partner may have named Guardians for your children. Are you still comfortable with those choices? This is an issue to address with your lawyer, and may affect your estate planning.
- Going forward you will want to make a new *Wealth Plan* with your advisor. Consider the issues you would like your advisor to address: Perhaps you intend to stay *single* for a while. Perhaps you are heading into another relationship. Are children involved? Will you be doing a new plan that will include a *blended family*?
- In the event that your planning interests may now diverge from your Partner's, your advisor will be able to refer your Partner to another TD advisor, ensuring that both of you are well-served.

Divorce and tax

Tax-efficient transfer of RRSP assets

One of the principal tax issues arising from divorce is the tax-efficient transfer of assets between separating spouses/partners. For example, this is a time when the *ITA* permits transfers from one Partner's RRSP to the other's to settle divorce settlement obligations, without imposing tax. There is no income inclusion for a recipient spouse and no deduction for the transferring spouse. Documents such as a Court order, written separation agreement (ideally, one that has received Court approval) or your divorce decree, along with form T2220, will be required by the CRA to facilitate a tax-free transfer.

Income Attribution Rules

The *ITA's* income attribution rules govern the way income is split between immediate family members (spouses and minor children). Usually, when income-producing property is transferred or loaned to a spouse or minor child, either directly or by means of a trust, the income and capital gains from the property will be attributed back to the transferor and taxed in his or her hands. However, the attribution rules will not apply when spouses are living apart due to relationship breakdown. Moreover, if a joint election is filed with the CRA, the application of the attribution rules can also be avoided. This may help facilitate tax-efficient transfers of assets in the course of facilitating divorce settlement obligations.

Support payments

Periodic spousal-support payments are generally tax-deductible for the payor, and taxable for the recipient. *Lump-sum payments* are generally considered to form part of the equalization and will not be deductible by the transferor or taxable for the recipient. Meanwhile, a lump sum payment made to cover missed periodic payments required by a court order or written agreement, may be considered deductible by the payor and taxable for the recipient.

When it comes to *child support*, payments are generally tax-free for the recipient, and not tax deductible by the payor.

Speak with your lawyer and/or tax specialist about the implications of any of these issues. Then speak with your advisor about recalibrating your Wealth Plan, as required.

Now you will:

- Be able to gather materials you need to meet with your TD advisor and begin the discussion about your wealth planning going forward. These same documents will be useful to you when you meet with your lawyer.
- Have an understanding of some of the tax implications of your relationship breakdown.
- Be better prepared to speak with your advisor about creating a new Wealth Plan.

