

Hidden Traps: Defending Novel Claims Against an Estate

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In the course of advising an estate trustee as to his or her duties, two primary tasks come to mind: (i) identifying and paying the debts of the estate and (ii) distributing the balance of the estate to the beneficiaries.

While creditors of the estate will often consist of liquidated claims, such as credit card debts, lines of credit or utility bills, it is often a more complicated exercise to identify and defend more complex claims against the estate. Some of the more novel claims that are asserted may be news to an estate trustee who was not privy to the personal circumstances of the testator during his or her lifetime.

Such claims may be founded upon information that was within the knowledge of the estate trustee and the claimant but not always documented. The challenges posed to any creditor advancing such a claim and the estate trustee defending the claim are the same: the key witness is dead and the issue becomes whether the claim can otherwise be proven or defended in such circumstances. Examples of such proceedings are claims predicated upon: (i) equitable mortgage, (ii) fraudulent conveyance, and (iii) claims against insurance proceeds.

Equitable Mortgage

The requirements of an equitable mortgage are set out in *Elios Markets Ltd., Re* (2006 CANLI 31904 (ONCA)). In that case, the court held that an equitable mortgage is distinct from a legal mortgage: “An equitable mortgage is one that does not transfer the legal estate in the property to the mortgagee but creates an equity of charge upon the property ... In essence, the concept of an equitable mortgage seeks to enforce a common intention of the mortgagor and mortgagee to secure property for either a past debt or future advances where that common intention is unenforceable under the strict demands of the common law.”

The case law is clear that an equitable mortgage is a contract evidenced by an agreement between the parties which creates in equity a charge upon real property but does not pass the legal estate to the mortgagee.

In the context of the role of an estate trustee, it may be that a disappointed creditor will assert an argument against the estate on the basis that an equitable mortgage was created between the deceased in his/her lifetime and the person who lent him or her money. If a claim is asserted, the estate trustee will need to compile and assemble any evidence in defence of any such claim and this can complicate the role of the estate trustee.

Fraudulent Conveyance

A fraudulent conveyance is commonly understood to be a conveyance which is made with the intention not to benefit the recipient of the transfer but, rather, to defeat the creditors of the transferor.

Estates are particularly vulnerable to allegations of fraudulent conveyance because it may be that a testator, contemplating his or her imminent demise due to a terminal disease or otherwise, takes steps to transfer assets out of his hands so that his estate will not be left to creditors but to family members who he needs to support.

It is compelling to try and take the position that the needs of family members should triumph over those of creditors but this is not a simple exercise. Support claimants may gain some standing as creditors but it can be a difficult position to argue that such support claimants should take priority over creditors, especially creditors who have made loans to the deceased based upon representations as to the value of their assets and, in particular, the ownership of real property.

In recent years, the “estate planning defence” has been frequently asserted against a claim of fraudulent conveyance. In the most recent example, *RBC v. Scarborough* (2019 ONSC 3369), the defendant common law spouse of the deceased argued that estate planning steps initiated 2 years prior to his death (and well before any debt was accumulated) militated in favour of a finding that the intent of the conveyance was not to defeat creditors. Other factors in favour of this argument were that: (i) the testator had transferred his house into joint ownership with his long-term common law spouse consistent with the terms of his Will, (ii) there was an acknowledgment by the deceased that the debt was owing, and (iii) the deceased was actively taking steps to seek employment while the claim was asserted against him.

Notwithstanding the evidence in favour of the suggestion that the intention was not to defeat creditors but rather to benefit family members pursuant to an estate plan, the court held that the “badges of fraud” that were present nonetheless were overwhelming and found against the estate planning defence.

Life Insurance Claims

Life insurance proceeds are a concern if the estate receives the proceeds of insurance to assist in the payment of creditors. When advising a testator regarding his or her estate plan, life insurance can play an important role in providing for the payment of debts or the support of dependants (the latter often pursuant to a Separation Agreement). As such, an irrevocable beneficiary designation of a family member may be in place. However, as we have detailed in a prior issue of *The Probater*, the recent decision of the Supreme Court of Canada in *Moore v. Sweet* stands for the proposition that, if there is a prior contractual right to be a beneficiary of an insurance policy, it is not a juristic reason for a new beneficiary to be appointed in the face of such a claim.

In our experience, it would appear that claims relating to insurance proceeds are increasingly being advanced and it is prudent to advise a testator that any designation of beneficiaries must be made with a view towards whether there is any other person who has a prior legal entitlement to receipt of the proceeds. If that inquiry is not undertaken and if a beneficiary designation is vulnerable to attack, this can complicate any well-intentioned estate plan.

Summary

The bottom line is that debts of the estate can include not only liquidated debts (commonly identified by an advertisement for creditors), but more complicated claims often framed in the context of civil litigation by way of statement of claim or notice of application. In furtherance of the duty to maximize the estate for the beneficiaries, the estate trustee must carefully scrutinize with appropriate legal advice and marshal any evidence in defence of any claim that calls into question transactions alleged to have been entered into by the deceased.