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Avoid Second Home Surprises

Before buying a dream home in Arizona, a ski chalet in British Columbia, or pied-à-terre in Paris, speak to your estate planner. No, it's not as exciting as talking to a real estate agent, but owning property in a foreign country or a different province than your permanent residence can profoundly affect your estate plan.

There's a simple reason for this. Real property—meaning the land and buildings permanently affixed to that land—is always governed by the legal jurisdiction and laws of its location.

The laws regarding inheritance, marriage rights, taxation, and even the validity of your will, can differ vastly from the laws of your home province. Purchase property beyond those borders and you expose your estate to a different legal and taxation regime. Those differences require careful planning or they can be costly in many ways.

We'll highlight the differences using the locations mentioned above. We chose those closer to home as they're popular real estate destinations for Canadians looking for recreational or retirement options. We selected France as it shows some of the estate planning pitfalls related to owning property in Europe. Other jurisdictions across Canada or around the world require equally careful planning.¹

The Problem of Probate

First, a brief word about probate as it's fundamental to understanding the unique challenges of our "foreign" ownership examples or any destination you might choose.

Probate is the process where a court verifies the validity of a deceased person's will, and grants legal authority to the personal representative ("executor," "liquidator" or "estate trustee" depending upon the province) of the estate to perform their duties, including dealing with any real property in accordance with the will terms.

To deal with your house, investments, bank accounts and other personal property, your personal representative will almost certainly need to obtain probate in your permanent residence province. Owning real estate outside your home province means your representative must obtain probate again in the legal

jurisdiction where the real estate is located. Real estate can almost never be transferred without the formality of probate.

Within Canada, probate obtained in one province can often be "re-sealed" in another province relatively simply. Obtaining probate in a foreign jurisdiction can be altogether another matter. Consider the following issues that can arise when obtaining probate in another jurisdiction:

- First and foremost, be certain your last will and testament will be valid in the jurisdiction of the real property. For example, many places in the world do not recognize a holograph, or handwritten will. Requirements for impartial witnesses can also vary. Often, creating a separate will to deal with foreign real estate is recommended.
- Your personal representative will probably require legal advice in the foreign jurisdiction, adding to estate expenses.
- Your estate, or at least the portion represented by the real estate in the other jurisdiction, will be subject to the tax regime of that jurisdiction, which could include probate tax, gift or estate tax, or property transfer tax.

The complications and expenses of dealing with "foreign" property in your estate might wind up being disproportionate to the value of the real property. However, your personal representative may have few options to reduce those expenses. Many people accept such costs as part of the price of enjoying a home away from home, but ensure you understand the potential costs before rushing into a purchase.

In British Columbia

Who can argue with the beauty of British Columbia? It's a natural draw for a summer or winter retreat. However, remember owning

1. This article isn't intended, nor should it be construed as, legal, estate planning or investment advice. Individuals should not act on the basis of this information without consulting their respective legal, estate planning or investment advisors.

B.C. real estate exposes your estate to the vagaries of B.C. law upon your death. Here are three examples of issues that should be considered by your estate planner:

- B.C. charges a probate tax of approximately 1.4% upon the market value of all assets declared for probate. This tax is approximately \$7,000 on a property worth \$500,000.
- B.C. also charges a property transfer tax of 1.0% on the first \$200,000 of real estate value, and 2.0% on the portion of market value greater than \$200,000. For a \$500,000 property this tax is \$8,000.
- The B.C. “Wills, Estates and Succession Act” permits the court to amend the terms of a deceased person’s will if the court decides insufficient provision has been made for a spouse or child of the deceased. This Act may concern individuals who wish to reduce or exclude one or more children from their estate. The excluded child may be able to successfully challenge the will in B.C. courts. This type of challenge may be impossible in the deceased’s home province but owning real estate in B.C. exposes that property to such challenges.

Planning techniques exist to mitigate some of the issues arising from these B.C. laws. However, this isn’t a “do it yourself” area and we believe expert legal guidance is essential.

In the United States

Many Canadians purchase second homes in vacation and retirement hotspots like Florida and Arizona. They should be aware of the following pitfalls before buying:

- The US legal system is very different from Canada’s. Further, estate laws vary widely from state to state so it is critical to receive state-specific legal advice. For example, Louisiana has “forced heirship” laws (which we will discuss in our France example below) that will seem strange to most Canadians.
- Owning US real estate means your estate will be subject to the US gift tax and estate tax regime. This is a very complex subject and the tax rules have changed frequently for several years. Unless you have a very large estate or the value of your US home is very high, your estate will probably not have to pay estate tax because current exclusion rates mean the tax only applies to very large estates. However, one thing is fairly certain. If your estate owns US real estate, whether tax is payable or not, your personal representative will be required to file a US estate tax return, and this will probably require professional advice.

We recommend anyone considering purchasing real estate in the US speak to an experienced cross-border tax or estate planner before signing any contracts. To be effective, many planning strategies, such as owning US real estate in a Canadian trust, require advance work.

In France

The food, the wine, the romance—who hasn’t dreamed of owning a home in a quaint French village? Before rushing into anything, think about this:

- France, like many other European countries, has “forced heirship” laws. These laws—derived from feudal laws designed to keep land in the hands of a certain class of landowners—may strike us as archaic, but nonetheless they’re fact. In France, landowners don’t have the right to give their land to whomever they wish. Children have what are known as “entrenched inheritance rights.” No will made in, or outside of, France, can override these entrenched inheritance rights. Without careful planning, this can lead to problems for people who have remarried and have children from a prior marriage, or people who are estranged from one or more of their children.
- Beginning in 2012, France created a new law that applies to any trust, located anywhere in the world, that owns French real estate. For example, a Canadian with minor children might create a trust under their will to hold a French vacation home until the children reach the age of majority. The trustee must now report annually to the French tax authorities the market value of assets held by the trust. Failure to file these reports may trigger onerous penalties and many Canadian trustees could fail to file the reports simply because they’re unaware of this complication.

Choosing to own a vacation retirement property outside Canada or even in an adjacent province may fulfill a lifetime goal. Or maybe it seems like a wise investment. However, in our experience many Canadians decide to buy foreign property unaware of the implications for their estate plan.

Our advice, as always, is to seek competent professional advice before making such a major decision. There are planning strategies, both simple and complex, which can reduce or eliminate negative consequences that might arise upon the death of the property owner.



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