

The TaxLetter®

Vol. 35, No. 6

Your Guide to Tax-Saving Strategies

June 2017

ESTATEPLANNING

Common Law

Uncommon Considerations

Mark Halpern, CFP, TEP

Wedding planners are preparing for busy times ahead. Summer approaches and love is in the air; the return of warmer weather heralds the start of the wedding season for Canadian couples.

Falling in love will never go out of style, but many couples are now waiting longer than ever to get married. A growing number is deciding to live together in a non-marital relationship, like common-law. Few people are aware of the legal, financial and tax-planning implications of common-law relationships that differ from those with marital status. The differences prevail during the time they are living

Mark Halpern is a Certified Financial Planner (CFP), Trust and Estate Practitioner (TEP) and one of Canada's top life insurance advisors. He is CEO of WEALTHinsurance.com® and illnessPROTECTION.com®, with special expertise for business owners, entrepreneurs, medical professionals and high-net worth individuals and their families. He can be reached at 416-364-2929, toll-free at 866-566-2001 or mark@WEALTHinsurance.com.

together and persist long after the relationship ends.

In our continuing series of articles dealing with life-cycle milestones (having a baby, divorce, death), this article examines some of the issues faced by common-law couples that require the help and experience of knowledgeable tax, legal and estate-planning professionals.

Common Law Issues

Recent figures from Statistics Canada confirm that a married couple remains the most common family structure; however, their "market share" is dwindling. The number of common-law couples has risen sharply and now accounts for almost 17 per cent of all family units.

Living together is not just for millennials. Many romantics over the age of 65 are also taking the live-in plunge. Quebec has

the highest proportion of the population living common-law, regardless of age.

Proceed with caution, and before you decide to live together consider the following:

1. Know your provincial regulations

Provincial laws vary and what is common law for insurance or tax purposes might differ from the family-law definition applied by the provinces and territories. Even the language used to describe couples can vary.

In Alberta, for example, common-law couples are legally called "adult interdependent partners," and in Nova Scotia it's a "civil union" or "domestic partnership." In Quebec, a "civil union" is not the same as a couple in a "common-law" relationship.

Unlike married couples, people in common-law relationships in Quebec do not have a right to a division of their property if they separate, nor can one partner ask another for support payments. In La Belle Province, the partners don't automatically inherit from each other if one dies without a will or if one was not named as an heir in the will.

All of this leads to a "wild west" atmosphere for those seeking non-marriage unions, according to my colleague, Jonathan Tucker, CPA, Tucker Professional Corp.

2. Consider the future

Tucker says that regardless of what a non-marriage union is called, many heading into these relationships are blissfully unaware of the financial, legal and taxation issues that may arise in the future. That is a problem. And of course, at the beginning, neither party wants to consider the possibility that the relationship may end. However, that is a distinct possibility which should be addressed in advance rather than left to some future time.

“When speaking with couples who have entered common-law relationships (or who are considering doing so), both parties are often not aware of the tax, financial and legal issues which should be considered and agreed upon in advance, with the advice and assistance of an experienced lawyer and accountant,” says Tucker.

3. Take the time to understand how laws affect you

Many people involved in common-law relationships are young professionals who have been in school for several years, taken on a lot of debt and are now starting to make good money.

They sometimes find themselves in a common-law situation where they have misunderstood the tax and financial implications of being in such a relationship.

Tucker gives the example of a client, a successful young dentist who has been practising for a few years and already owns his own home. Both he and his girlfriend decide she will move in with him. The dentist, who is making \$300,000 a year, continues to pay for the cost of the

house, which is owned in his name. His girlfriend, who is making about \$30,000 a year, contributes about \$500 a month. If that relationship breaks up, who is entitled to what? “With no defined parameters, many mistakenly believe they have the right to be maintained in the lifestyle to which they have grown accustomed. One needs to think about that beforehand,” says Tucker.

Matters may become more complicated if the dentist decides to sell the house. He takes his proceeds from the sale and, with money from his girlfriend, they buy a second house. In a few years, they decide to go their separate ways and sell House #2. How does that get divvied up? In the absence of any written contract, that might well be up in the air.

4. Contemplate a cohabitation agreement

Tucker strongly suggests that each party seek independent legal advice. A cohabitation agreement may be drafted by a lawyer, much like a pre-nuptial agreement for those contemplating marriage, or a shareholder agreement for those entering business together. Experienced lawyers can give couples the ins and outs of an agreement which will set the boundaries if a relationship breaks up down the road.

If the dentist and his girlfriend continue to live together then they may want to consider some tax-planning strategies. Adding her as a shareholder in the dental practice is a typical tactic used for income splitting, suggests Tucker.

If they decide to go their sep-

arate ways in the future, what happens if the girlfriend wants to keep the shares? Whose obligation is it to pay the taxes?

With no firm agreement, is the dentist on the hook for the taxes? These are questions which may well be decided in court in the absence of an agreement put in place ahead of time.

5. Take a strategic approach

Like anyone else, common-law partners can set up a trust as a tax- and estate- planning tool. From a tax-planning perspective, trusts can be used to facilitate income splitting by spreading income among family members who get taxed at lower marginal tax rates to reduce the family's overall taxes.

When it comes to estate planning, trusts are used to provide control and protection of assets by reducing probate fees.

Should a relationship end, trusts can also be used to set aside certain assets to protect the former partner and children out of that relationship, while creating ongoing income for them in the future.

6. Be aware of federal tax laws

The Canada Revenue Agency website (www.cra-arc.gc.ca) provides some information on what constitutes a common-law relationship for federal tax purposes, says Tucker. Where a couple meets this definition, when tax time rolls around both must include their common-law partner's name, social insurance number and net income, in addition to their own personal information.

Both parties must be consistent on what they declare. One partner can't declare “single” status on their return while the

other declares “common-law”. “If the other person has not put down their net income and whether they are in a relationship, that can flag the CRA to say there are inconsistencies,” says Tucker.

Tax laws are agnostic when it comes to tax credits, so whether you are married or living common-law, couples can, for example, split the age credit (if they’re older than 65), the child tax credit, HST benefits, the disability tax credit, as well as health costs and charitable donations.

7. What happens if you decide to leave?

If a couple splits up, provincial family law legislation is not necessarily the same as for those who are married. In fact, in the absence of a cohabitation agreement, it may be a free for all, says Tucker. “And that’s concerning.”

From a tax perspective, if a couple decides to call it quits they may discover some tax obligations they never even contemplated. If your partner hasn’t paid income tax for the last year – some of those obligations may fall to you as a consequence, under certain provisions of the

Income Tax Act.

Having children in a common-law relationship may cause inheritance issues down the road. Talk to a lawyer before you make the live-in commitment and be sure the two of you know what is expected of you before you share the same address.

8. Who pays for life insurance?

As in any relationship, you may also want to think about getting life insurance. Consult a knowledgeable life insurance advisor, who can explain the differences between separate life insurance policies and joint policies in a common-law relationship. While it’s not something people like to think about, there is always the possibility the two of you will split. If so, what happens? Will the higher-income partner who has helped finance the other person’s life insurance premiums continue to pay, especially if there are children involved?

When it comes to living together - in a marriage, common-law or civil union relationship - there is always a honeymoon period. It is always my sincere hope that a happy and

friendly mood continues, but we all know from experience that unforeseen difficulties arise that can push the partners away from each other.

If you are uncomfortable bringing up the subject of a cohabitation agreement with your partner, ask your financial advisor (in advance) to bring it up the next time you all meet. He or she will explain the laws of the land in your particular jurisdiction, to ensure you both know the ground rules on potential issues. The rest is up to the two of you, happily ever after.

Mark Halpern is a Certified Financial Planner (CFP), Trust and Estate Practitioner (TEP) and one of Canada’s top life insurance advisors. He is CEO of WEALTHinsurance.com® and illnessPROTECTION.com®, with special expertise for business owners, entrepreneurs, medical professionals, high-net worth individuals and their families.

He can be reached at 416-364-2929, toll-free at 1-866-566-2001 or mark@WEALTHinsurance.com
Visit WEALTHinsurance.com
Get your FREE Estate Planning Toolkit at www.WEALTHinsurance.com/toolkits.html

The expanded toolkit now includes:
Estate Directory
Estate Planning Checklist
Executor Duties Checklist
Business Owners Planning Guide

Visit www.MarkHalpernBlog.com and sign up for free updates