



Leveraging STEP membership: Building private banking relationships

by **Stewart Lewis**

Editor, STEP INSIDE

For the fourth and final edition of our series on the changes within Canadian financial services due to the demise of the former “four pillars” STEP INSIDE is looking at banking, or more specifically, private banking.

There are some common elements within all financial institutions that offer private banking. They offer integrated services that include normal banking and cash management without the line-ups, tailored credit solutions and access to mutual funds and investment advice — both discretionary and non-discretionary.

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Most clients are worth at least \$500,000, if not \$1 million. Unlike the average bank customer, they aren’t presented with an array of standard products. They’re looking for banking and other services that will be specifically tailored to their needs.

The attraction of private banking for clients, says Lindsay Histrop, partner in the Toronto office of Cassels Brock and Blackwell LLP, “is mainly efficiency.”

Whether the clients want refinancing for their home or an increase in their line of credit, they’re going to get it wherever they go, she says, however, with private banking, one phone call will get them what they need.

“A client will usually have one private banking officer to coordinate all their needs. That one individual will make everything happen for them. They like that.”

Estate planning is also part of the offering within private banking services. To look how that’s done in Canada, STEP INSIDE spoke with representatives from each of the five big banks.

CIBC

At CIBC there are several estate and trust specialists on staff, says Marcia Ball, Toronto-based senior regional director of CIBC Private Wealth Management. One is lawyer Orlando Consoli, a member of STEP Canada who meets with clients directly along with their private banking officers and investment managers.

They regularly review the client’s needs, says Ball, to see what estate planning services are required. It may involve everything from strategizing to protect legacies to setting up wills and powers of attorney.

“Helping clients plan for the future includes estate planning,” says Ball.

While many private banking clients will have lawyers, they may not have a lawyer who specializes in estate matters. If not, Consoli may use his contacts within the trust and estate practice community to refer someone to the client. Similarly, estate

lawyers will come to him to establish a structure, which they have determined is appropriate for the client.

CIBC also has a corporate trust arm, and Consoli can help coordinate use of its services as a trustee or executor.

BMO HARRIS

At BMO Harris Private Bank tax and estate planning is a key part of the services that are offered, says Jean Blacklock, VP and managing director of personal trust services of BMO Harris Private Bank.

In this regard, she says, there may be four or five client meetings and as ideas crystallize, an estate plan is devised.

The bank has tax and estate planners — lawyers or accountants — in all of its offices across the country, however, their goal is not to compete with private practitioners. Instead, the ideas that come out of the client meetings, which combine input from the integrated service-people at BMO, put them “miles ahead of where they would be if they had gone directly to an estate planner.”

However, Blacklock is quick to note that “pretty much all” of the estate planning staff are STEP members, she says. “So our practitioners know private practitioners extremely well. They go to the same update seminars.”

One of the new services that BMO would like STEP members to know about is being unveiled in February 2005. It’s called enCircle, a service for BMO Harris customers who are seniors.

It may include bill payment or travel and medical insurance — items of particular interest to snowbirds, says Blacklock. It also includes provision of information on health and homeowner services in their local community.

In the initial testing of this service BMO Harris got “an excellent response to this service,” says Blacklock. “It provides one relationship manager to get all this done.”

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Divisive reorganization in a complex family business

Two friends John and Frank immigrated to Canada several years ago and have built up a successful rental business. John's family are wealthy Singapore entrepreneurs and he owns 25% of shares of the family's Singapore companies. John and Frank now own eight properties in Canada. Frank's daughter Felicia works in the business as a property manager. Frank's son Fred remained in Singapore to work in the family business. John's two sons Jacob and Justin have their own construction business and don't currently work in the rental business. One of the sons, Justin, plans to expand the construction business in China

and will be moving there within 12 months. John and Frank are the only shareholders in the business. The children want their share of the real estate business when the founders die, but they don't get along with the daughter, Felicia. The founders don't want to see the business split up. What do they do? How would an estate planner help them with the inevitable?



Lorne Saltman is a Partner at Cassels Brock & Blackwell LLP in Toronto and a Member of STEP Toronto

TAX ANALYSIS by Lorne Saltman

While many entrepreneurs wish to bequeath their businesses to their children, this is not always wise or possible.

John and Frank wish to keep their business, Realtyco, intact while they are both alive. They recognize, however, that while Felicia is competent and the right choice for management, John's sons are not in the business and do not get along with Felicia. Therefore, a plan is required that contemplates an eventual transfer of control to Felicia and her buying out the interests of John's family.

Keeping the business intact with eventual exit by sale of shares

Frank should implement an estate freeze in respect of his 50% shareholding in Realtyco ("Frank's Shares"), so that the capital gains tax on his death is fixed at an amount equal to the current value of Frank's Shares. That would also enable Felicia to start participating in the growth of Realtyco, while Frank continues to maintain control over his shares during his lifetime.

This freeze can best be accomplished by having Frank transfer his shares to a new

holding company ("Frankco") in return for fixed-value preference shares in Frankco ("Class A Pref"), on a tax-deferred, rollover basis under the provisions of subsection 85(1) of the *Income Tax Act*.

As the entire value of Frank's Shares will have been taken up in the Class A Pref, Frank would subscribe for nominal value common shares that he would then give to Felicia. The gift may protect Felicia's common shares from a potential claim by her spouse under the applicable family law statute. In addition, Frank would subscribe for nominal value Class B Preference Shares that would provide him with voting control over Frankco. On his death, these shares would be converted into non-voting Class C Preference Shares, thus ensuring that Felicia alone acquires control of Frankco at that time.

John would remain as a direct shareholder in Realtyco and not freeze his shareholding ("John's Shares"), because on his death the shareholders' agreement would require his family to sell John's Shares to Frank or Frankco, if Frank is alive, or to Felicia or Frankco, if Frank has predeceased John. Accordingly, a freeze to defer capital gains tax would not benefit John's heirs.

Other exit strategy: The butterfly reorganization

If Frank and John cannot agree on how to keep Realtyco intact, it is necessary to examine other exit strategies. Because Frank and John deal with each other at arm's length (for purposes of section 55), there is only one avenue available to arrange for a tax-deferred transfer of the assets of Realtyco, and that is the "butterfly" reorganization.

As an exception to the surplus-stripping anti-avoidance rule in subsection 55(2), the butterfly reorganization in paragraph 55(3)(b) provides a method for dividing assets between corporations using the rollover provisions of subsection 85(1) and the deductibility of inter-corporate dividends in subsection 112(1). Briefly stated, a business corporation (the "Distributing Corporation") can transfer on a pro rata basis, each type of its property to one or



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more of its corporate shareholders (the “Transferee Corporation”) on a rollover basis in return for shares having a value equivalent to the shares held by the Transferee in the Distributing Corporation. The cross-shareholdings are redeemed and the proceeds are offset, one against the other, thus severing the connection.

In the case where John and Frank cannot keep the business intact and must agree to separate, they could decide to employ the classic “double-wing” butterfly whereby the interests would be divided between their respective holding corporations.

Alternately, John could implement a single-wing butterfly, which would involve the same transfer of John’s Shares to his holding company as in the double-wing. Similarly, Realtyco would transfer 50% of each type of its property to Johnco for similar preference shares as noted earlier. The same cross-redemption would occur by Johnco and Realtyco, thus severing the connection, leaving the four transferred properties in Johnco and the four retained properties in Realtyco, whose only shareholder is Frank (subject to any estate freeze that Frank may wish to implement).

Planning for departure tax

Upon leaving Canada, Justin will be deemed under subsection 128.1(4) to have disposed of his property, subject to limited exceptions, for proceeds of disposition equal to the then fair market value. Justin will realize accrued capital gains on his shares in the construction company he owns with his brother and, if John has implemented a freeze of Johnco in favour of his sons, any directly owned shares in Johnco.

An advantage of using a Canadian-resident discretionary family trust in an estate freeze such as this is that each beneficiary’s interest is likely to have nominal value on death or departure from Canada. If a family trust held the common shares of Johnco for John’s issue, including Jacob and Justin, there will likely be no capital gains tax payable on Justin’s departure regarding his interest in the trust. He would still continue to be a member of the discretionary class of beneficiaries.

Absent such planning, Justin would be faced with paying the capital gains tax over a maximum of 10 years or lodging acceptable security with the Canada Revenue Agency under subsection 220(4.5) (in proper circumstances, this could include private company shares, such as those in the construction company or in Johnco),

or selling his shareholdings in order to realize the cash with which to pay the tax.



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COMMERCIAL ANALYSIS

by Ann Watterworth

Keeping the business intact with eventual exit sale of shares

The critical commercial issue for this alternative is that John, Frank and Felicia enter into a shareholders’ agreement to deal with both the day-to-day operations of Realtyco and the ultimate disposition of both John and Frank’s shares since the ultimate goal is for Felicia to become the sole shareholder. Similarly, Frank and Felicia will need to enter into a shareholders’ agreement for Frankco.

The Frankco shareholders’ agreement should, as a primary matter, set out a process for making decisions on behalf of Frankco as a shareholder of Realtyco. Depending on the wishes of Frank, Felicia could have a role during his lifetime. Otherwise, the agreement would provide that Frank should be the decision-maker.

The shareholders’ agreement should also deal with the disposition of the Class A Preference shares held by Frank. As the simplest alternative, if Frank has sufficient assets, he can provide in his will that all of the Class A Preference Shares are left to Felicia and provide other equivalent assets to Fred. If this is not feasible and Frank wills half of the shares to Fred, the Frankco shareholders’ agreement must provide for the right of Frankco and/or Felicia as the surviving shareholder to acquire the shares on Frank’s death.

In order to fund the buyout of Fred’s shares, Frank would acquire life insurance payable to Felicia on the death of the survivor of Frank and his wife to enable her to buy out Fred’s one-half interest in Frank’s Shares. Alternatively, insurance could be obtained which is payable to Frankco to enable the shares to be redeemed.

With regard to the Realtyco shareholders’ agreement, the agreement will set out the usual housekeeping matters regarding day-

to-day operations of the company and will probably mirror the terms of any existing pre-reorganization shareholders’ agreement.

To reflect the objective that the ultimate control of Realtyco should rest with Felicia, the shareholders’ agreement should provide that Frankco will have an obligation to acquire the shares held by John at fair market value on John’s death. The agreement must set out the methodology for valuing John’s shares, which can involve any number of options including appointment of a third-party valuator or using a value agreed upon by the parties on a year-to-year basis.

For both the Frankco and Realtyco shareholders’ agreement, consideration also needs to be given to other liquidity events such as incapacity of Frank and John, family law issues and bankruptcy issues. Corollary estate matters that need to be addressed are the entering into of wills and powers of attorney.

Another commercial issue that needs to be dealt with by Realtyco is Felicia’s compensation. This issue is critical both pre- and post-reorganization.

While seemingly straightforward, compensation paid to a family member for working in a family business that does not employ all family members can give rise to ill will and must be carefully thought out and communicated to the other family members.

Conversely, for the person working in the family business, there can be feelings of unfairness if their compensation is less than they would be obtaining if similarly employed elsewhere, which is particularly true if they are not obtaining any other benefit from the employment.

It is preferable to remove the element of discretion from Felicia’s compensation package and, to the extent that she has bonus provisions, to make the bonus provisions formulaic and transparent so that certainty is provided to other family members and to Felicia on a year-to-year basis.

Other exit strategy: The butterfly reorganization

For this alternative, the critical commercial issues revolve around the transfer of the real estate assets. The first step that needs to be taken is to review any contracts and in particular banking arrangements that are in place with Realtyco which contain covenants prohibiting the sale of assets of the company without obtaining the consent of the other contracting parties. Typically any

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lending arrangement would contain such covenants.

It is important that John and Frank keep their lenders and other contracting parties apprised of the reorganization and obtain the appropriate consents. Similarly, since at the end of the day the assets of the company will be split into two separate groups, it is likely that any existing financing will need to be renegotiated and new security registered.

As well, any guarantees that the individual shareholders have entered into of the obligations of Realtyco need to be reviewed. These guarantees will preferably be replaced with new and separate guarantees as appropriate. If the parties are unable to obtain a release of the guarantees, indemnities will need to be entered into to deal with the event that any of the guarantees are called upon.

As a related issue, the parties will need to assess any liability that may flow from any particular asset which is being transferred. If one of the properties has an environmental risk associated with it, it might be appropriate for the party transferring the asset to provide a proportional indemnity for all matters that have arisen prior to the date of the transfer or, in certain circumstances, on an ongoing basis.

As a housekeeping matter, to the extent that any of the properties have tenants, the tenants will need to be notified with respect to the new landlord or provided with instructions for payment of rent. Any other commercial agreements that are in place will need to be examined and the impact of the reorganization assessed.



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INSURANCE ANALYSIS

by David Beavis

If Frank and John decide that their children will not continue on together in the business then they can set up buy-sell arrangements so that Frank's family buys out John's family at some point over the next several years or on John's death.

Since Felicia is the only child that is involved in the business it probably makes sense for her, or Frank, to buy out John. With the proper life insurance arrangements in place it is possible that John's family could be bought out on a tax-free basis. They may be just as happy to receive the tax-free proceeds from the sale of John's interest in the business and use the proceeds to make their own real estate investments.

Frank and John may have grandfathered status against the stop-loss rules for corporate-owned life insurance. They may be grandfathered because they had corporate-owned life insurance in place on April 26, 1995 or as a result of an existing buy-sell agreement at that time.

If they are grandfathered then the company can set up a corporate-owned policy on John to fund the tax-free redemption of his shares on his death. If they are grandfathered as a result of existing corporate-owned life insurance they can add additional corporate-owned life insurance to fund the full share value or they can replace the existing insurance and still maintain the grandfathered status. The grandfather provision attaches to the shares not the life insurance.

They will have to be very careful in order to maintain the grandfathered status because even a minor amendment to the existing agreement may result in the loss of grandfathered status.

Even if they are not grandfathered John's estate could still be bought out on a tax-free basis using a roll and redeem strategy. John could set up his will so his shares are transferred to his wife or a spouse trust. Then the corporation can use the life insurance proceeds received at John's death to redeem his shares from his wife or the spouse trust using a tax-free capital dividend from the amount added to the CDA on receipt of the life insurance proceeds.

The stop-loss rules do not apply because no loss is created. John's shares would be rolled over to his wife or a spouse trust so there is no capital gain on the shares in his estate. The buy-sell provisions in the shareholders' agreement between John and Frank would have to be set up properly in order for John's shares to roll over to this wife or the spouse trust.

In order for the rollover to work, the shares have to "vest indefeasibly" with John's wife or the spouse trust. That means the shareholders' agreement cannot contain a mandatory sale of shares on John's death.

The tax-free proceeds from the sale of shares will belong to John's wife or the spouse trust. If John's wife holds his shares directly without a spouse trust then she can distribute the tax-free proceeds from the sale of the shares among her children if she wishes, but that is her choice.

If the shares are held through a spouse trust then she is the only person entitled to the capital from the trust for the balance of her life. In order to distribute any of the proceeds to her children she would first have to receive a capital distribution from the trust and that would depend upon a decision from the trustees. John could also set up his will to leave other non-taxable assets to his children to adjust for the shares transferred to his wife for the tax-free sale.

With the roll and redeem strategy there is also a concern that John's wife will predecease him. In that case, if the corporation redeems John's shares using the proceeds from corporate-owned life insurance on his life under the stop-loss rules only 50% of the loss is denied. In effect the tax in John's estate is reduced to the tax on a taxable dividend on 50% of his shares. This is still a significant tax saving.

John could also use an estate freeze to provide for a tax-free sale of a portion of his shares if he is not grandfathered from the stop-loss rules.

The corporation can insure John for the full value of his family's interest in the business including the common shares held by his children or a trust for his children. On John's death there is no deemed disposition of John's children's shares so the stop-loss rules do not apply. Their shares can be redeemed by the corporation on a tax-free basis with the life insurance proceeds.

If Frank and John decide that Frank will buy John out during his lifetime, John could still "sell" his shares on a tax-free basis using a variation of the corporate-owned life insurance arrangements for the tax-free sale of shares on death. With this arrangement John gets his tax-free cash now for re-investment, Frank takes over the business now and Frank reduces the cost for the purchase of John's shares to the cost for the life insurance to purchase the shares.

Capital gains tax in estate

Frank and John have similar issues to deal with in regard to planning for the tax payable in their estates.

It is very likely that Frank and his family will end up with all or a portion of the rental property business that will be passed on to his children. Frank will need to do some planning to deal with the payment of capital gains tax in his estate.

If Frank has built up sufficient value to provide for himself and his wife he may want to consider, as discussed above, implementing a full or partial estate freeze to limit or stop any further increase in the value of his shares for tax purposes. The assets and family members outside Canada raise additional issues. For example, if Fred was included as a beneficiary of a discretionary family trust there would be an issue to deal with in trying to distribute assets out of the trust on a tax-free rollover basis if Fred was still a non-resident at that time.

Whether Frank does a full or partial estate freeze or doesn't freeze at all he can set up a corporate-owned life insurance policy to fund the payment of the tax liabilities in his estate. The life insurance policy can be a joint last to die policy for Frank and his wife if Frank's estate plan is set up to transfer his shares and other taxable assets to his wife or a spouse trust for his wife. The life insurance proceeds will be received tax-free by the company on the death of the second. The cost of the life insurance on a joint last basis is much less than insuring Frank by himself.

If Frank is grandfathered from the stop-loss rules for corporate-owned life insurance, the insurance can be used to provide the tax-free cash to pay the tax in his estate and reduce it by 20% to 25% depending on the province where he lives. If the tax-free redemption of shares is set up the amount of life insurance that is required to pay the tax on his shares can be reduced.

If Frank is not grandfathered from the stop-loss rules, corporate-owned life insurance could still be used for a significant reduction of the tax payable in his estate. Regardless of whether he is grandfathered, consideration must also be given to any other potentially applicable stop-loss provisions, such as subsection 40(3.6.).

Fred may also want to consider using a life insurance policy to make a charitable gift in his estate to offset the taxes payable in his estate while preserving his business value for his family. It takes a little more life insurance to provide the charitable gift to offset the taxes in his estate but he is also providing a substantial gift to the charity(s) of his choice.

John can undertake similar estate planning steps to provide for the payment of the taxes in his estate.



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CONTINUITY ANALYSIS

by Aron Pervin

Deciding on a continuity plan is a process. Misaligned behaviour, assumptions and beliefs, unrealistic expectations, hostile personalities and poor interpersonal relations can hinder and even sabotage the most carefully planned and brilliantly crafted plan. For a plan to be successful, complex relationship issues must be examined in tandem with the progressive technical and structural legal, tax and financial planning.

When differences are irreconcilable between business families, the best course is probably to sell the business. However, things may not always be what they seem, making it worthwhile to probe the relationship issues. In this case, simply selling the business doesn't address the founders' desire to see the business continue. It would mean the loss of the product of years of hard work, and the loss of the benefits to their families.

Here's one scenario of how this situation could be played out: I met the founders, John and Frank, and they told me that they had come to Canada from Singapore and had chosen each other as partners. They indicated that their Chinese heritage and other cultural similarities and patterns contributed to their collaborative and unified relationship.

They described how they worked together as partners to build a successful income-producing real estate enterprise. John and Frank both took frequent trips back to Singapore to manage their affairs.

They told me that their concern could possibly be the continuity of ownership and management to the next generation in the real estate firm. In addition to the challenge of possible absentee owners, they were concerned that John's children, Justin and Jacob, might not hold Felicia in high regard

and this might affect harmony and decision-making.

As we discussed the situation, they told me that the transfer of the enterprise, in good operational and financial condition, to a next generation who are ready, capable and eager to take over as operators and/or owners was one of their ultimate responsibilities and obligations. It is their legacy.

Experience confirms it is prudent to separate and protect beneficial owners from different owning families who can't get along easily. But depending on the situation you might advise an alternate strategy to sustain the enterprise, mitigate risk, capture opportunity, appreciate legacy and maintain appropriate owner oversight, especially if the business is profitable and the management of the rental firm is done well. Why break up a going concern?

As I listened to John and Frank discuss and appear to agree on their ultimate intentions and dreams for the future of this enterprise, I began to understand their values regarding identity, respect, trust, face, altruism and consensus without conflict. They elaborated on the merit of honour and dignity, and suggested that discipline and order are important attributes in their culture and to them.

They described how business is personal and indicated that a Confucian concept they learned in school suggests that human dignity should never be removed from doing business. They indicated that favours were remembered and that everybody is supposed to win in business — everyone must walk away from the table feeling they have been successful. They indicated that there is no success if you corner someone or try to get him or her over a barrel.

They told me how certain subjects were taboo except in private and others open for public conversation. They explained how this Canadian enterprise was one of their most lucrative businesses, but they maintained a more connected identity to their other overseas family firms.

They asked me to speak to Justin, Jacob and Felicia separately and explore how they envisioned the ongoing ownership and management of the firm.

The result of this series of conversations dispelled their initial fears. Simply put, when John and Frank first started the business, there was little room for additional staff. Therefore, Jacob and Justin were encour-

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aged to establish another business and had worked hard to build it.

They inappropriately assumed that there was no place in the real estate firm for any family member from either family. This assumption was reinforced by Fred staying in Singapore and challenged by Felicia's employment. It had shaped their resentment and distance from Felicia, and contributed to their feeling boxed in and out of control.

They also were concerned how a partnership might work with Frank if their father were to die. To add to the twisted thinking, they never felt able to query their father about what they considered to be a contentious matter; they might appear jealous, greedy, petulant and lacking in trust and respect. So they constructed rational stories to make sense of their tension and anxiety resulting from this misunderstood situation. This appeared to validate their feelings and create the negative messages.

I prepared everyone for a solution-focused discussion. In a private meeting with John and his sons, John explained how Felicia had been asked to join the firm by both founders. The timing was right and she was the only family member available, as everyone else was doing something else. John

and Frank did not think the situation required explanation, so it was never discussed in the regular meetings. They assumed everyone would understand. He indicated that she was doing a good job and had contributed to the growth and profitability of the firm.

Jacob and Justin were surprised by this and explained how they had built a story based on an inappropriate assumption, and were glad to understand their misaligned thinking and change it.

As a result, John and Frank began to construct their continuity plans, and included their wives and children in the process at the appropriate time.

Rather than meet with each professional individually, John and Frank invited all their advisors to a meeting and explained what they were attempting to do, and requested that the advisors construct a logical plan with minimal overlap of service. John and Frank performed some aspects of the work together and some separately, such as their personal estates.

Here are a few examples of outcomes that were planned for completion within the next three years:

- Integrated estate and tax plans (jointly and separately).

- A shareholders' agreement, including helpful exit and liquidity options.
- A family participation plan, including rules for entry, staying, exit and compensation guidelines.
- A leadership plan for the enterprise (family and/or non-family).
- An employment contract for Felicia (and similar contracts were discussed for John and Frank) including performance measures, role assignments, relationships, accountability and other expectations.
- A transition plan for John and Frank.
- A governance plan that stated an advisory board should be established to coincide with the transition of John and/or Frank to a less involved role in the company.
- A shareholder charter setting out the systems of governance structures and processes that shape the relationship the owners have with one another and to the firm and/or assets, such as improving communication in the firm and the family, relations with shareholders, leadership development and methods to keep the peace. ■

Leveraging STEP membership *continued from page 1*

It's also of interest to clients in their 50s with elderly parents, she adds.

TD WATERHOUSE

Private trust services at TD are closely linked with investment counsel services and private banking under the one umbrella of TD Waterhouse. The brand is well known in its capacity as a discount broker, and that may be the door that some clients enter, but the financial services for high net-worth clients are "the second floor" at Waterhouse, says Alan Walker, associate VP of Private Trust, part of TD Waterhouse Private Client Services.

"Our trust officers work closely with the private bankers and portfolio managers." It's a system of cross-referral that helps TD identify clients' needs and fill them. For example, he says it's not uncommon for private bankers to be providing credit management for complex estate freezes or helping to facilitate estate planning transactions that can run to seven or eight figures.

Most of its private trust professionals are STEP members. "One of their responsibilities is to leverage the privilege of STEP membership." TD is a strong believer in the TEP designation, he adds.

BANK OF NOVA SCOTIA

BNS prides itself on its bevy of established multi-generational clientele. "It's old money, extremely well-established families, a 'Who's Who' of Canadian wealth," says James Neate, national director of private banking at the Bank of Nova Scotia.

Like the other four major banks, it has centers in many major urban centers across Canada, and is keeping an eye out for new opportunities where the wealthy are putting down stakes. For example, BNS plans to set up a new private banking center in Barrie, Ont. this year. "As many people flee the city," says Neate, they will be looking for services closer to home.

The same holds true for wealthy clients who already live in smaller cities and towns.

They may not be within quick driving distance to a private banking center. However, says Neate, a lot of their concerns can be dealt with over the phone or via e-mail.

Private bankers also coordinate with the bankers in a client's local community to offer them the specialized service that they require. "It simply requires the proper introduction to set up better services," says Neate.

Whether in a larger or smaller center, he says, private banking "is not cookie-cutter stuff."

ROYAL BANK OF CANADA

RBC offers high net-worth clients in Canada and abroad an integrated private banking value proposition, which includes trust and investment services, says Steve Mackey, VP & director of RBC Global Private Banking.

"We see the capability to offer high net-worth clients an international trust service, where appropriate for their needs, as a sig-

nificant strategic advantage in attracting clients. In a time when globalization has made the world a much smaller place, high net-worth clients around the world are now routinely exposed to international planning options by their professional advisers or otherwise,” says Mackey.

RBC considers trust services as a cornerstone of its private banking offering, says Mackey, as trusts involve custom tailored

solutions that encourage a strong relationship between RBC and its high net-worth client base. “Whether the solution required is domestic, international or a combination of the two, RBC has the expertise to understand and implement sophisticated planning structures.”

In Canada, RBC Trust Services is rolling out a unique service directed at both trustees and executors, says Patricia Kennedy, na-

tional VP of private trust services at RBC, part of the bank’s domestic private client group.

With the new agent for executor and agent for trustee services, RBC can take on the role of primary advisor, liaising with outside professionals such as an external investment manager, while the client remains trustee or executor, says Kennedy. “We can assist with administration without handling the whole portfolio.” ■

STEP TECHNICAL COMMITTEE REPORT

Responding to finance, building knowledge and developing key relationships

by Kim G.C. Moody

*Partner, Moody Shikaze Boulet LLP, Calgary;
Chair, STEP Canada Technical Committee*

Your Technical Committee was busy throughout 2004 and has a full slate for the upcoming year.

The 2004 year commenced with welcoming the Department of Finance to Calgary for the branch’s Finance Roundtable. The Technical Committee had a significant hand in posing direct questions to Finance on matters directly affecting the taxation of trusts and estates. The day was both enlightening and encouraging. Finance officials invited STEP to put forward its comments on several technical issues.

On March 11, 2004, the STEP Technical Committee was involved in releasing an open letter to The Right Honorable Paul Martin, Prime Minister of Canada, with respect to the draft legislation on taxation of foreign investment entities and non-resident trusts. This open letter got STEP a fair amount of press. However, the draft legislation still is unchanged. STEP intends to continue its lobby efforts.

In early October, the STEP Technical Committee wrote a letter to Finance to discuss its concerns with respect to the legislative proposals put forward in the March 2004 budget dealing with the concept of trust affiliation. To the extent that such budget proposals would be enacted as proposed, subsection 40(3.6) would be very problematic in many classic estate plans involving shareholders of private corporations given that such proposals would often deny a realized loss.

The Technical Committee is happy to report that on December 6, 2004, Finance responded to our submission by introducing draft legislation that would enable such losses to be

utilized by the deceased estate, thereby solving the problem identified by the committee. This is great news! While there are still problems with subsection 40(3.6) (such as denied losses involving spousal trusts), STEP is pleased with the fact that the Department of Finance recognized the problem and responded appropriately.

In 2005, your Technical Committee will continue to be involved in a number of other activities, including:

1. Reviewing appropriate topics for a study.
2. Ensuring that the next one-day course — Testamentary Estate Issues — is completed and delivered.
3. Considering the content of new one-day courses that STEP can offer in the future.
4. Setting out the technical content of the 2005 STEP National Conference.
5. Continuing to review ongoing draft legislation released by the Department of Finance.
6. Exploring the idea of providing federal and provincial budget commentary on any content that affects trusts and estates.
7. Working with STEP Technical Chairs around the world.
8. Working with the Canadian Tax Foundation to enhance the friendly relationship that STEP currently enjoys with it.

The STEP National Technical Committee held a teleconference call in January with the chairs of technical committees in the branches throughout the country to receive feedback and exchange ideas in order to enhance the role of the STEP Technical Committee.

Meanwhile, should you or your branch wish to be more involved, please feel free to contact Kim Moody at 403-206-0842 or moodyk@taxandestateplanning.com. ■

NS chartered accountants, Ontario do-it-yourself wills, Alberta's AIPs and BC charitable purposes

NEW RULES GOVERNING CONFLICT OF DUTIES FOR NS CHARTERED ACCOUNTANTS

by Catherine Craig

Associate, Baxter Harris Neonakis,
Halifax; Prospective STEP student

Recent amendments to the Rules of Professional Conduct adopted by the Institute of Chartered Accountants of Nova Scotia may prevent a chartered accountant from serving as a trustee of a client's family trust while providing assurance services to that client's operating company.

Rules 204.1 to 204.8 of the ICANS Rules of Professional Conduct came into force on January 1, 2004 but the impact of the rules is just starting to be fully understood. Any accountant who acts as a trustee of an *inter vivos* trust in Nova Scotia should be aware of the amendment and review their practice in light of the new rules.

Specifically, Rule 204 provides that a chartered accountant must be (and appear to be) independent when reporting on the results of specified auditing procedures or any assurance engagement. ICANS adopts the definition of "assurance engagement" from the Canadian Institute of Chartered Accountants' *Handbook*, which is broadly defined as any service that provides a conclusion to the subject matter of interest to a user (Council Interpretations, Rule 204/1). Therefore, the duty of independence is broad reaching in a chartered accountant's scope of practice.

The Canadian Institute of Chartered Accountants has opined that presiding as a trustee of a discretionary trust is "tantamount" to acting as an officer or director of a company (*CICA Standards & Guidance Update*, December 15, 2004). Both positions of trustee and corporate officer or director empower the individual to make managerial decisions on behalf of the entity as well as owing fiduciary duties to the entity. However, problems may arise when a chartered



accountant holds shares of an operating company as trustee of a client's family trust, and also provides assurance services to the operating company as its accountant. As a shareholder, the trustee/member has the legal ability to influence who is appointed as director of the company.

For clarity, Rule 204.4 enumerates "circumstances and activities which members and firms must avoid" because adequate safeguards to the accountant's independence do not exist. There are many circumstances enumerated in Rule 204.4, which reasonably capture an accountant presiding as a trustee of a client's family trust while providing assurance services to the operating company. Among others, the following subsections of Rule 204.4 potentially prohibit an accountant (or other member of the accountant's firm) from acting as both a trustee of a trust and providing assurance services for any companies whose shares are owned by that trust:

- 204.4(13) Close business relationships;
- 204.4(18) Serving as an officer or director of an assurance client;
- 204.4(19) Serving as an officer or director of an audit or review client; and
- 204.4(22) Performance of management functions for an assurance client.

Independence is measured both "in fact and appearance" as provided in Clause 2 of the ICANS Council Interpretations. Therefore, while the threat to independence may not be the case *in fact*, a perceived threat is equally unacceptable.

Other provinces have recently implemented similar rules related to the indepen-

dence of Chartered Accountants and there is a body established to co-ordinate the Rules of Professional Conduct and Interpretations among the various provincial institutes of chartered accountants known as the Interprovincial Committee to Harmonize the Rules of Professional Conduct.

ONTARIO COURT REVIEWS CHANGES MADE TO DO-IT-YOURSELF WILL

by Mary Louise Dickson

Partner, Dickson MacGregor Appell LLP;
Member, STEP Toronto

Luty v. Magill was a case concerning the interpretation of a do-it-yourself will. The Ontario Court of Justice heard it in September and judgment was rendered in December.

The deceased, Julia Hudson Stark, filled in a Self-Counsel Press Will Form and properly signed her name at the foot or end of her will in the presence of two witnesses, who witnessed the will in the presence of each other. Ms. Stark filled in the blank spaces in her handwriting and made a number of legacies. The will was dated October 26, 1998. She later made certain changes on the face of the will after she signed it, which she initialed. Ms. Stark died on March 16, 2004. The issue before the court was whether any of the changes were valid for the purpose of revoking the bequests previously made.

After reviewing the will in detail, the Court found that to be valid alterations must be made in accordance with the formal requirements of the *Succession Law Reform Act*. Therefore, the alterations that were not dated were found not to be valid alterations to the deceased's will.

The alterations that were initialed and dated, and marked "delete" were found to be valid holograph codicils to the will that were validly made under the SLRA and those bequests and/or legacies were revoked for the purposes of probate of the will.

Based on the wording of will, this resulted in a partial intestacy of the residue of the deceased's estate.

Mandatory mediation in some parts of Ontario

Mediation is now mandatory in estate matters in Toronto, the Regional Municipality of Ottawa-Carleton and the County of Essex in Ontario. This move by the Ontario government was preceded by a pilot project in Toronto and Ottawa-Carleton. It has now been made permanent in these jurisdictions and extended to the County of Essex.

Some changes have been made to the mediation forms effective January 1, 2005 by virtue of an amendment to Rule 75.1.02 (1)(a). The main changes are the following:

- Names of the testator or the deceased person: Forms 74.1, 74.2, 74.3, 74.4, 74.4.1, 74.5, 74.5.1, 74.14, 74.15, 74.20.1, 74.21, 74.24, 74.27, 74.30 and 75.1 were amended to deal with problems occurring in court offices relating to the name of the testator or the deceased person. The manner in which the name is set out has been changed with the hope the information will be set out with more clarity.
- Regional or Metropolitan Municipalities: Forms 74.4, 74.4.1, 74.5, 74.5.1, 74.14, 74.15, 74.20.1 and 74.30 are amended by deleting "Regional or Metropolitan Municipality" from the address box of the deceased and from the "Place of Death" box because regional or metropolitan municipalities no longer apply. The boxes now refer to "city or town; county or district."
- Grants limited to assets referred to in will: Because a number of testators make multiple wills, most of which will not be probated, Forms 74.4.1 and 74.5.1 are amended to attach the particular will as exhibit "A" to the Application so the Application will refer to the specific will.
- Notices of applications and affidavits of service: Notices of the Application of Appointment of Estate Trustees, Forms 74.7 and 74.1.7 and Affidavits of Service, Forms 74.6 and 74.1.6 are amended to show a list of persons who may be entitled to be served but have not been served and set out the reason they were not served. The court offices were requiring this information, but there was no place on the forms for it.

SERVING NOTICE ON AIPS

by Nancy L. Golding

Partner, Borden Ladner Gervais LLP;
Member, STEP Calgary

Alberta's new legislation dealing with adult interdependent partners could present practitioners with potential difficulties when trying to get probate granted.

In *Tsang Estate (Re)* (2004), counsel for the executor of an estate made an application for a grant of probate without having to serve notice on an "adult interdependent partner" pursuant to the *Dependents Relief Act*.

The relationship of the deceased and the AIP lasted from 1941 to 1977. The AIP had been the deceased's former common-law wife. Their relationship existed between 1941 and 1977. They had children. Mr. Tsang died in 2004 leaving an estate worth over one million dollars in cash alone.

The Alberta trial division judge involved in hearing the application issued an order from chambers directing that Tsang's former wife be served with notice so she could pursue any claim pursuant to the Act.

The decision stands as a caution to practitioners to fully uncover their client's past relationships, even those that ended almost 30 years before the death.

New Public Trustee Act and Minors' Property Act

The Alberta government has passed amendments to these two Acts, which came into effect on January 1, 2004.

Some of the more important changes to the new *Public Trustee Act*:

- The Public Trustee now only has a duty to monitor a trustee of a minor's trust if directed by a trust creator or courts to do so.
- The Public Trustee does not have to consent to the appointment by the trust creator, which is an exception to the general rule that the Public Trustee must consent to any appointment.
- There will be a prescribed fee for the Public Trustee to act, which will be on an hourly basis.
- The Public Trustee will have broad discretion to make expenditures out of funds held for a minor, for the minor's benefit. Such discretion does not depend on the amount held in trust and no court authority is required.
- An interested party may apply to the court to order the Public Trustee to make an expenditure.

- A new investment regulation will be finalized once the legislation comes into effect.
- The Public Trustee can, under certain circumstances, give an election to administer an estate instead of applying for a grant of probate. This can be used whether the deceased died testate or intestate and the value of the estate must now be under \$50,000.00.

Some of the more important changes to the new *Minors' Property Act* include:

- If the value of a minor's share is not over the prescribed amount (\$5,000.00) the executor may discharge their obligation by delivering the money or property to a guardian of the minor with responsibility for making day-to-day decisions regarding the minor. The Public Trustee does not need to consent.
- The executor of the estate would need to obtain an acknowledgment of responsibility in the prescribed form from the guardian, and the executor could rely on representations in the acknowledgment.
- An executor may also discharge its duty if a gift is under the prescribed amount (\$5,000.00) by delivering the money to the Public Trustee if the Public Trustee is willing to accept it.
- The court may now appoint a trustee of particular property or all of a minor's property.
- The order may have limitations such as the type of investment allowed in it and there will be a presumption that a bond or other security will be required.
- The court can now confirm a contract that has been entered into by a minor or by the minor's guardian on the minor's behalf if it is in the best interests of the minor.
- The Public Trustee must be served with notice of any application under the MPA or any other application in which "the existence, extent, nature or disposition of a minor's or unborn person's interest in property is in issue."

BC MOVES TO PROTECT CHARITABLE PURPOSES

by Genevieve N. Taylor

Associate, Legacy Tax + Trust Lawyers,
Vancouver; Member, STEP Vancouver

Gifts to benefit charities or charitable purposes have historically received preferred
In the headlines, page 10

In the headlines continued from page 9

treatment by the common law of trust. The British Columbia Legislature has now given charitable purposes a further preference by way of the *Charitable Purposes Preservation Act*, S.B.C. 2004, c. 59, which augments — but does not replace — the common law.

The Act received Royal Assent on October 21, 2004, but has not yet been brought into force by regulation. The provisions of the Act will be retroactive.

Under the scheme of the Act, a charity holding “discrete purpose charitable prop-

erty” is essentially the trustee of that property. A charity holding discrete purpose charitable property has no beneficial interest in the property. That means the property may not be seized to satisfy a debt or liability of the charity except to the extent that the debt or liability was incurred by the charity in advancing or in attempting to advance the discrete purpose for the property.

For the purpose of the Act, a “charitable purpose” is defined as being recognized at law as being charitable, and includes the payment of debts or liabilities arising from the actual, intended or purported advancement of that purpose. Property is “discrete purpose charitable property” if:

1. a donor makes a gift to a charity for a specified charitable purpose, whether or not the property is given in trust;
2. the donor has either expressly or through some formula identified with certainty what property is given to that purpose; and
3. the donor’s intention is expressly stated to be, or is by necessary implication, that the property be kept and administered separately from the charity’s other property and used exclusively to advance the specified charitable purpose rather than to assist or support the charity generally or in advancing any of its goals, purposes or objects.

Such property remains “discrete purpose charitable property” as long as it is kept, administered and used in accordance with the donor’s intention. Money and other fungible property retains its discrete purpose charitable property status so long as the charity’s records allow for the discrete purpose for the property to be identified and the property that is kept for that discrete purpose can be quantified.

The law of British Columbia with respect to trusts and entities holding trust property will apply to such “discrete purpose charitable property” and to the charity holding it. From a planned giving perspective, clients may wish to consider structuring gifts to charity in a manner that meets the test for “discrete purpose charitable property” instead of giving directly to charitable entities.

The settlement arising from the claims against the Christian Brothers of Ireland in Canada and their operation of the Mount Cashel Orphanage is expressly exempt from the application of the Act except to the extent that it creates “discrete purpose

BRANCHING OUT

Winter programs

VANCOUVER

FEBRUARY 16, 2005

Topic: Understanding family business governance structures

Place: UBC Robson Square
800 Robson St.
Vancouver

Speaker: Dr. Dennis Jaffe

MARCH 3, 2005

Topic: Addressing conflict in the family enterprise

Place: UBC Robson Square
800 Robson St.
Vancouver

Speaker: Dr. Tom Knight

MARCH 18, 2005

Topic: Women in business leadership

Place: UBC Robson Square
800 Robson St.
Vancouver

Speaker: Dr. Nancy Langton

CALGARY

FEBRUARY 16, 2005

Topic: Top 10 cases of 2004

Place: Bankers Hall Auditorium,
Calgary

Speakers: Christopher Thomas, McLeod & Company;
Jane C. Carstairs, McKinnon Carstairs;
Roy Boettger, Field Law

MARCH 15, 2005,

Topic: Estate litigation: Potential claims on an estate

Place: Bankers Hall Auditorium

Speakers: Cherrilynn Kelly,
Parlee McLaws LLP;
Nancy Golding, Borden
Ladner Gervais LLP

OTTAWA

MARCH 2, 2005

Topic: Post-mortem planning issues

Place: Ginsberg, Gluzman,
Fage & Levitz
287 Richmond Road
Ottawa

Speaker: TBA

TORONTO

FEBRUARY 23, 2005

Topic: Planning for the elderly

Place: Metro Toronto
Convention Centre,
North Building
225 Front Street West
Toronto

Speaker: TBA

JUNE 6-7, 2005

Register Early!

Topic: 7th Canadian National
Conference

Place: Metro Toronto
Convention Centre

Speakers: TBA

charitable property.” Given this explicit reference it seems the impetus for the Act was a concern arising from the bankruptcy of the Christian Brothers of Ireland in Canada.

The Mount Cashel Orphanage abuse claims against the Christian Brothers and the ensuing settlement caused the bankruptcy of the Christian Brothers. The insolvency resulted in a claim that the property held by the Christian Brothers for Vancouver College Limited and St. Thomas More Collegiate Ltd., two private schools in the greater Vancouver area, was available for satisfaction of the settlement.

The Act provides the courts with broad discretion, including the ability to order that “discrete purpose charitable property” be transferred to a new charity, if the original charity is no longer able or willing to advance the property for the discrete charitable purpose. The courts can also order that the property be used to advance another charitable purpose that the court considers to be consistent with the originally intended discrete purpose.

If the original charity is bankrupt or wound up, and the trustee in bankruptcy, liquidator or receiver is unwilling or unable

to hold the property for the intended discrete purpose, the court — if it is satisfied that the purpose can be advanced — must issue an order making the necessary administrative arrangements so the property is kept, administered and used to advance that purpose.

If in the court’s view the purpose cannot be advanced by another charity, then upon bankruptcy or windup the court must identify another charitable purpose that is consistent with the discrete purpose and make whatever administrative order necessary. ■

EDITORIAL

Strengthening pre-nups: SCC provides welcome assurance

The idea that pre-nups are unassailable is the stuff of popular misconception, often spread by Hollywood. Just look at the notion of the notorious “Massey contract” in the recent movie *Cruel Intentions* starring George Clooney and Catherine Zeta-Jones, where a divorce lawyer is undermined by his own pre-nup!

In the matrimonial sphere, there is greater judicial oversight and intervention than in commercial matters. This shouldn’t be surprising, considering the historic economic imbalance in many traditional marriages where there is a financial heavy-weight breadwinner and an economically vulnerable stay-at-home spouse. Two lovers working out a financial arrangement in case their marriage fails are in a far different position from two business people negotiating a contract, including the fall-out for breaching it.

However, when should the courts interfere with pre-nups? If you make your own bed, do you always have to sleep in it? What is the escape threshold? What can you say to assure a client who asks, “How bullet-proof is this contract?” “When is a deal a deal?”

Family law legislation in Canada allows couples to negotiate their own pre-nuptial contracts, including how their property will be divided and what support, if any, will be paid. If they don’t make a contract, provincial law imposes a mandatory scheme.

Provincial schemes generally work for most people — those who fit into the square box of a first marriage with each party having minimal assets at the date of marriage. Otherwise, pre-nups are an especially important part of estate planning, in particular for people embarking on second marriages that may include children and financial obligations from prior marriages, as well as significant assets.

Fortunately, the Supreme Court of Canada provided guiding principles for advisors and clients in its 2004 decision, *Hartshorne v. Hartshorne*, regarding when the courts will in-

tervene. The majority upheld the ability of parties to make their own deal over the ability of the courts to *post facto* undo the deal because it is objectively “unfair,” provided certain requirements are met such as a fair bargaining process.

The majority of the SCC said a pre-nup contract should be respected. When considering whether a pre-nup should be set aside two factors must be considered: what the parties could realistically have contemplated when they made their agreement and whether the circumstances at the time of the marriage breakdown are vastly different from what was anticipated when the contract was made. The minority took the view that the court should determine whether the agreement is unfair on an objective basis and if so override it.

In *Hartshorne*, the couple were both lawyers and had independent legal advice in entering into their contract. It provided that upon divorce the property they brought into the marriage would remain their own. The husband was previously divorced and wanted to ensure his property would not be subject to further division if the second marriage failed. He made this clear throughout the couple’s relationship. The parties co-habited for 12 years, including nine years while married.

The agreement included a support provision giving the wife an interest of 3% in the matrimonial home for each year of marriage. The pre-nup gave the wife the right to property worth \$280,000, and the husband the right to property worth \$1.2 million.

Based on *Hartshorne*, what is fair will depend on whether the two people were independently advised and made an “eyes wide open” arrangement, examining at the time the possible outcomes.

The ability of parties to make their own arrangements without fear of judicial intervention has been strengthened. We as advisors have better assurance in planning our clients’ affairs. This we should laud. ■

Chair's Message



by Paul LeBreux

Chair, STEP Canada

Each year in late November, STEP Worldwide hosts the STEP Winter Conference and Branch Chair's Assembly in London.

Since STEP Canada's inception in 1998, Canada, as a regional center, has always been very well represented in London. This year was no different.

Eighteen Canadian delegates, including representatives from each of Canada's eight STEP branches (seven branch chairs) attended the two-day conference. STEP Canada hosted its annual Chinese dinner on the Friday night — an event that now boasts an annual waiting list.

The annual Branch Chairmen's Assembly has, in my mind, always been the perfect venue to truly get the pulse on the Society, and take a moment to gaze into the future of STEP in its role in supporting global trust and estate practitioners. Like the song says: "The Future's So Bright I Gotta Wear Shades."

Being in London with STEP representatives from all over the world is the best indicator of the global strength and recognition of the TEP designation. It comes as no surprise that STEP members from the legal, accounting, corporate trust, banking, insurance and related professions now represent approximately 3,000,000 high net-worth individuals and families with a combined net-worth well into the trillions of dollars.

With approximately 11,000 members and 68 branches spanning 48 jurisdictions across the globe, the question is no longer "Why become a STEP member?" Instead it's: "How can you afford not to be a STEP member?" This speaks volumes for the global profile of the Society; however, the true measure of the Society's strength will come when a client looks no further than to a professional with the TEP designation for advice or direction on matters involving domestic and international trust and estate planning.

STEP CANADA'S 2005 PLANS

As in past years, STEP Canada took the opportunity of being together in London to hold its final Board of Directors meeting of the year — a time to review 2004 and plan for 2005.

Following are just some of the things that we will focus on in 2005:

1. A membership drive for experienced practitioners (practitioners/academics with 10 years or more experience in

trusts and/or estates — available only until December 31, 2005) and qualified practitioners (holders of recognized professional qualifications with 5 years or more experience in trusts and/or estates and have submitted three papers demonstrating a level of knowledge acceptable to the Society);

2. The implementation of an education and examination system designed to maintain the integrity and quality of the TEP brand and to ensure the STEP Canada branches maintain a strong and growing membership;
3. A public relations initiative aimed at increasing the TEP profile in Canada and ensuring that STEP Canada, the STEP Canada branches and their membership continue to be recognized and accepted by the public and private sector as the principal professional body for trust, estate and tax practitioners worldwide.

THANKS TO CLARE COLACICCHI

This year's conference marked the end of Clare Colacicchi's two-year term as Chair, STEP Worldwide, and what a remarkable two years it has been. Under Clare's expert tutelage, STEP emerged as a true global player, known to governments, regulatory bodies, related professional bodies and associations, and last but not least, members of the public at large. On behalf of STEP Canada and its near 2,000 members, I would like to thank Clare for all she has done for the Society and will no doubt continue to do into the future.

MICHAEL CADESKY AWARD

It is often easy to overlook the fact that individuals such as Clare Colacicchi, and all the people who take an active role in STEP acting as branch chairmen and board directors or chairing and participating as members on executive committees, do so on a strictly volunteer basis. These volunteers will always be the backbone of the Society and should never go unnoticed. For this reason, STEP Canada has established the *Michael Cadesky Award*, which will be awarded annually at the STEP National Conference to the Canadian member of STEP who best demonstrates magnanimous voluntary contribution of his or her time towards STEP.

Although there will always be the concern that "too few are doing too much," there is also the inevitable adage that "if you want to get something done, give it to a busy person." Based on the latter maxim, STEP Worldwide should see a flurry of positive activity during the next two years, as Canada's own Michael Cadesky assumes the reins as Chair. ■

Write to us! Do you have a story idea for *STEP INSIDE*? Do you have a comment about something that appears in these pages? Perhaps you would like to express an opinion on something that's going on in the industry. Well, please don't hesitate to write us with your concerns and ideas. You can e-mail us at: news@step.ca. ■