Divorce and discretionary trusts: what can be divided between spouses? – Cottrell v Cottrell, 2022 BCSC 1607

October 28, 2022

The Supreme Court of British Columbia has released an important decision relating to the treatment of a spouse's interest in a discretionary trust within the context of family law proceedings. In *Cottrell v Cottrell*, 2022 BCSC 1607 (12 September 2022, Brongers J.), the Court interpreted provisions in Part 5 of the *Family Law Act*, S.B.C. 2011, c. 25, (FLA) to mean that, when considering the proper division of family property, the court must focus on whether there has been any increase in the value of a spouse's "beneficial interest" in such a trust, and not an increase in the value of the underlying property of the discretionary trust. The Court in *Cottrell* held it had not been proven that there had been any increase in the value of the spouse's beneficial interest and, in consequence, there was no basis for ordering any division of the property.

The claimant Joanne Cottrell was a beneficiary of two discretionary trusts settled by her parents: a joint spousal trust, as well as a family trust that had been settled to manage lottery winnings. Joanne's beneficial interest in both trusts fell within the meaning of "excluded property" under s. 85(1)(*f*) of the FLA because she did not contribute to or settle either trust. Excluded property is not "family property" that is subject to division between spouses. However, s. 84(2)(*g*) of the FLA provides that "family property" includes the amount by which the value of excluded property has increased since the beginning of the spousal relationship or when the excluded property was acquired. When ss. 84(2)(*g*) and 85(1)(*f*) are read conjunctively, the increase in value of Joanne's beneficial interest in the two trusts would be considered "family property" and *prima facie* subject to an equal division with her former spouse Paul.

Joanne argued that it was not possible to quantify any increase in the value of her beneficial interest in the trusts. She cited the conceptual difficulties that are inherent in valuing the interests of objects of discretionary trusts. In contrast, Paul argued that it was possible for the Court to determine a value of the increase in value of Joanne's beneficial interest in the trusts, and this amount would be caught by ss. 84(2)(*g*) of the FLA. He claimed that the post-tax value of the increase exceeded $2.6 million, based on Joanne being one of three remaining beneficiaries of the trusts and the underlying trust property increasing by $12 million during the marriage. In consequence, his undivided half-interest would be $1.3 million.

Justice Brongers confirmed that only the increase in the value of Joanne's "beneficial interest" in the trusts would be considered family property; this analysis does not involve the value of the underlying trust property. Paul had the onus of proving the increase in value of Joanne's beneficial interest, and the Court held that Paul had not met this burden. The Court agreed with Joanne that her "contingent beneficial interest" in the trusts was uncertain, given that she did not have the ability to compel a distribution, and there was no reliable assurance that she would receive a distribution in the future. As a result, Justice Brongers was not satisfied that there was an increase in the value of Joanne's beneficial interest in the trusts. Further, even if Paul was correct that the underlying trust property had increased in value by $12 million, that does not demonstrate an increase in the value of Joanne's beneficial interest.

The Court's analysis in *Cottrell* of valuing a spouse's interest in a discretionary trust is a marked contrast from previous B.C. law on this issue. The B.C. Supreme Court had never endorsed the trust law principle, found in cases like *Gartside v. I.R.C.*, [1968] 1 All E.R. 121 (H.L.), that the interest of an object of a discretionary trust is not "property" and therefore could not be a family asset. The former *Family Relations Act*, R.S.B.C. 1996, c. 128 explicitly provided that a "family asset" may include an "interest in the trust" that is "owned" by one spouse, if the trust owns property that would be considered a family asset if it were owned by the spouse. The Court would first ask whether the spouse's interest was ordinarily used for a family purpose and, therefore, constituted a "family asset": *MacDonald v. MacDonald*, 2002 BCSC 1453, aff'd 2005 BCCA 23. If that hurdle was cleared, the Court confronted the complex issue of valuation. In some cases, the Court would reapportion family assets to take into account the likelihood that the beneficiary spouse would receive trust property in the future: *McCarlie v. Bogoch*, 2004 BCSC 147. In other cases, the Court took an "if and when" approach, and imposed a constructive trust on any property distributed to the beneficiary spouse: *Fulton v. Gunn*, 2008 BCSC 1159. Without a proper valuation, however, the exercise of reapportionment was a shot in the dark.

The Court's decision in *Cottrell* is more consistent with trust law principles about the nature of a beneficiary's interest in a discretionary trust. The beneficiary has no right to compel any property, and the value of the beneficiary's interest may be nil. Justice Brongers avoided the "shot in the dark" approach of valuation and reapportionment based on a guess of what Joanne may one day receive from the trusts. The *Cottrell* decision is clearly in accord with the intention of the Legislature when it amended Part 5 of the FLA in 2014.It should be noted, however, that Brongers J. was careful to state that his decision was based on the evidence before him, and that a different result could arise in another trial. He cautioned that his findings should not be taken as a conclusion of law that it is impossible to make a family property claim under the FLA in respect of a spouse's beneficial interest in a discretionary trust. The *Cottrell* decision will likely not be the final word on this issue.

By

Scott Kerwin, Les Honywill

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Centennial Place, East Tower
520 3rd Avenue S.W.
Calgary, AB, Canada
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T 403.232.9500
F 403.266.1395

Ottawa

World Exchange Plaza
100 Queen Street
Ottawa, ON, Canada
K1P 1J9

T 613.237.5160
F 613.230.8842

Vancouver

1200 Waterfront Centre
200 Burrard Street
Vancouver, BC, Canada
V7X 1T2

T 604.687.5744
F 604.687.1415

Montréal

1000 De La Gauchetière Street West
Suite 900
Montréal, QC, Canada
H3B 5H4

T 514.954.2555
F 514.879.9015

Toronto

Bay Adelaide Centre, East Tower
22 Adelaide Street West
Toronto, ON, Canada
M5H 4E3

T 416.367.6000
F 416.367.6749