

How to protect an inheritance from the risk of divorce

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SPECIAL TO THE GLOBE AND MAIL

PUBLISHED YESTERDAY

UPDATED 2 HOURS AGO

A substantial and growing share of first-time homebuyers are now relying on early inheritances and gifts from family to bolster their down payments. And that is creating new complications for parents seeking to ensure that family money remains in their children's hands in the event of a marital dissolution, according to financial advisers and lawyers.

“It’s definitely a topic of discussion when it comes to gifting,” says Jason Heath, managing director and certified financial planner at Objective Financial Partners in Markham, Ont. “When a partner is involved, it’s important to consider the implications. When you give money, particularly if it’s commingled with other money or used to purchase a matrimonial home, in the event of a future relationship breakdown, oftentimes half of that money ends up being lost in a divorce.”

Morgan Ulmer, certified financial planner at Caring for Clients in Calgary, notes this issue raises an important question parents need to consider: how much control they want to exert over their adult children. “That aspect to it also provides complications, both logistically but emotionally with your child,” she says.

Almost one-third (31 per cent) of first-time homebuyers received financial help from family members in 2024, according to a June report from Canadian Imperial Bank of Commerce economists, up substantially from only 20 per cent in 2015 and continuing to climb even amid the recent decrease in home prices. The average gift amount was \$115,000 this year, 73 per cent higher than 2019 levels.

Twelve per cent of “mover-uppers” received gifts from family for the purchase of a larger home, with the average gift for those buyers sitting at \$167,000.

Family law across Canada generally treats inheritances as exempt from the division of assets during a divorce proceeding, though the growth in value on those assets over the course of the marriage is subject to the equalization process. However, inheritance funds that are commingled with joint assets – such as using part of an inheritance to purchase a matrimonial home, pay down a shared mortgage or other shared debt – are considered family property to be evenly divided.

The exception is British Columbia, which introduced an amendment last year to clarify that inheritances remain excluded property even when transferred to a joint asset or account. However, any increase in value of the inherited assets is split evenly between spouses. The amendment also applies to early inheritances, says Emma Ferguson, associate counsel in the wills, estates and trust practice at Alexander Holburn Beaudin and Lang LLP in Vancouver.

Ms. Ulmer says one of the strongest tools parents have around early inheritance gifts is encouraging their children to enter marriage or post-nuptial contracts, or co-habitation agreements with their partner. “That would have the strongest chance of protecting [inheritance equity in] a marital home.”

Ms. Ferguson says many parents have begun giving money in the form of a loan rather than a gift, documented with a loan agreement or promissory note and ideally secured with a mortgage against the child’s home. In the event of a marital breakdown, parents can call the loan and the value of the matrimonial home decreases by that much. However, she says that banks generally take issue with a second mortgage registered against the title, and this may not work in all cases.

Mr. Heath notes that some parents may have the instinct to make the gift a zero-per-cent loan with no repayment schedule, but case law in Ontario has started to question whether those terms constitute a legitimate loan. “There can be risks if you do things informally like that.”

Parents who only plan to pass their assets on to their children after death can introduce a clause in their will stipulating that they want the inheritance and any growth on it to be exempt from family law, says Tina Tehranchian, senior wealth adviser at Assante Capital Management Ltd. in Toronto.

Ms. Ferguson says there’s less need to introduce this clause in B.C. given the recent amendment, however it can be helpful if a client’s beneficiaries live in other provinces.

Parents can also employ trusts if they're leaving substantial amounts of money, Ms. Tehranchian says. Inter-vivo trusts, which operate while the parent is still alive, and testamentary trusts that come to life after their death, are "separate legal entities" from the child and protect the funds from the equalization process, as well as from creditors or any lawsuits against the child.

Ms. Ferguson says her firm strongly recommends family trusts to parents who own shares in private companies that they want to pass on to their children, and encourages them to ask their children to sign domestic agreements with their partners to stipulate the shares aren't family property. "Most parents don't want their child's ex-spouse as a shareholder," she says.

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