

# **Tips and Traps when Preparing Estate Accounts; How to Avoid Estate Litigation**

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## **1. Introduction**

Estate litigation often means thousands, even hundreds of thousands of dollars in legal fees and a significant delay in the administration of an estate. In addition to possibly depleting the assets of an estate, estate litigation often destroys families and relationships. At times, the total monies spent in legal fees is not much less than the value of the entire estate.

While estate litigation involving will challenges is fairly common, a significant amount of estate litigation involves estate accounting and the propriety of the conduct of executors and trustees in the management and administration of an estate. Some litigation is unavoidable, particularly where there has been mismanagement or a breach of trust by the executor or trustee. However, a significant amount of litigation can be avoided by maintaining proper estate accounting and understanding the role of an executor or trustee of an estate.<sup>1</sup>

## **2. The Role of an Executor or Trustee and Estate Accounting**

An estate trustee is appointed pursuant to a will. The estate trustee's role comes with numerous duties including managing and administering the estate. All estate trustees, however, are subject to a common law fiduciary duty to act in the best interest of the beneficiaries. This fiduciary duty also requires that estate trustees maintain proper accounts and be ready to fully account to the beneficiaries on the administration and management of the estate assets.<sup>2</sup>

A passing of accounts is a formal procedure developed by the courts for reviewing and approving the accounting and conduct of estate trustees. An estate trustee can be compelled to

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<sup>1</sup> The focus of this paper is the role of an executor and estate trustee appointed in a will. Attorneys for Property may also be required to pass their accounts. Many of the same principles apply as for an executor and estate trustee.

<sup>2</sup> *Sandford v. Porter* (1889), 16 O.A.R. 565 (Ont. C.A.)

pass accounts by anyone having a financial interest in the estate.<sup>3</sup> It is not mandatory for an estate trustee to formally apply to the court to pass accounts, unless, generally speaking, the beneficiaries of the estate are minors or incapable of managing their affairs. Although a formal passing is not a mandatory requirement, it is prudent for an estate trustee to prepare accounts in the same manner and with the same level of detail required by the court in order to fulfill their fiduciary obligations as estate trustees and to protect themselves from personal liability. It is best to assume that a formal passing will be required at some future date and to prepare the accounts and gather documentation from the outset. After all, it is much easier to prepare accounts and gather documentation at an early stage, when the estate is being administered than when suddenly being called upon to do it in a short period of time.

### **3. Tips and Traps and Avoiding Estate Litigation**

#### **a) Plan to Avoid Litigation Altogether**

Often, estate litigation can be avoided with some pre-planning and having a carefully crafted estate plan in place. This includes ensuring that the proper advisors are retained, that an experienced lawyer prepares the will, that the appropriate executor(s) are appointed, that potential conflict or animosity between beneficiaries and/or estate trustee(s) is anticipated and foreclosed, and that the estate plan be regularly reviewed and updated to take into account any changes that may lead to conflict. Having family meetings and communicating with the beneficiaries and estate trustees can in itself also avoid “surprises” that may result in litigation in

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<sup>3</sup> *Ontario Rules of Civil Procedure* R.R.O. 1990, Reg 194, (hereinafter “*Rules of Civil Procedure*”) Rule 74.15(1)(h).

the future or may alert one to some issues or likely sources of conflict which may end up being litigious.

**b) Knowing the Will's Terms and Complying With its Terms**

An estate trustee's authority is derived from the will. The estate trustee must administer and manage an estate in accordance with the will. Knowing the will, complying strictly with its terms, and obtaining the proper advice when unsure about certain matters is key to avoiding allegations of impropriety, mismanagement or even fraud against an estate trustee.

Furthermore, familiarity with the will's provisions is important as the will is what dictates the types of accounts that have to be kept. For example, where a trust is established in the will or instructions are given as to investments, the estate trustee would have to prepare separate trust statements, or ensure investments are only in permitted instruments.

**c) Proper Record Keeping**

Estate trustees are required to keep detailed accounts which contain the following information:

- a) A statement of assets at the date of death;
- b) A statement of all monies received. Capital receipts and income receipts have to be recorded separately;
- c) a statement of all monies disbursed. Capital disbursements and income disbursements have to be recorded separately as well;
- d) A statement of investment accounts, if any;
- e) A statement of all estate assets that have not been realized;

- f) A statement of all estate money and investments;
- g) A statement of all liabilities, including contingent liabilities;
- h) A statement of compensation claimed by estate trustee; and
- i) Such other statements and information as the court requires.<sup>4</sup>

In addition to the information above, estate trustees should also maintain all source documents including bank statements, duplicate deposit slips, cancelled cheques, receipt confirmations and vouchers to support the records or accounts that are maintained by them.<sup>5</sup> Improper record keeping, delay in the provision of accounting information, or providing accounts that do not provide sufficient detail or even failing to provide back-up documentation when requested can raise suspicions and may lead to expensive and acrimonious litigation.<sup>6</sup> Transparency is fundamental to avoiding allegations of impropriety or mismanagement by estate trustees.

#### **d) Seeking Beneficiaries' Consent or Court Approval**

It may be prudent to obtain beneficiaries' written consent or court approval prior to making a major decision or making a contentious payment out of the estate account. One of the highly litigated areas in estate accounting is improper or unsubstantiated disbursements.

In *DeLorenzo v. Beresh*, 2010 ONSC 5655 (CanLII), the estate trustee paid legal fees out of the estate account for litigation between him and the beneficiaries related to the question of

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<sup>4</sup> *Widdifields on Executors and Trustees*, 6<sup>th</sup> ed., Chapter 14 (Toronto: Carswell, 2002) at 14.3.2(a) – 14.4.1

<sup>5</sup> *De Vries v. Resetar et al*, 2010 ONSC 2602 (CanLII);

*Zimmerman v. Fenwick* (The Estate of Signe Kirsten McMichael) [2010] O.J. 2162.

<sup>6</sup> *Ibid.*

whether or not the trustee had properly discharged his duties, including timely steps to pass his accounts. The estate trustee did not obtain the consent of the beneficiaries or the court's approval for the payment of such fees. The court found that since the outcome of the litigation may very well have a bearing as to what costs each of the parties should be required to bear, it was improper for the estate trustee to have paid the legal fees out of the estate without obtaining the beneficiaries' consent. The court ordered the estate trustee to personally repay the estate for amounts paid for legal fees in the litigation.<sup>7</sup>

Further, the court has specific procedures for applying for the court's directions by way of an Application for the Court's Opinion, Advice or Direction which is available in respect of the administration of the estate of a deceased person or the execution of a trust by way of an Application or Motion for Directions which is available to "any person who appears to have a financial interest in an estate".<sup>8</sup> These procedures allow an estate trustee to obtain directions or approval from the court on a specific course of action. Estate trustees are compensated for legal fees incurred by an estate trustee in bringing such court applications provided that the expenses were incurred on behalf of the trust or estate and were not incurred as a result of the estate trustee's misconduct or for defending the estate trustee's personal interests.<sup>9</sup>

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<sup>7</sup> *DeLorenzo v. Beresh*, 2010 ONSC 5655 (CanLII), para. 23 and 24.

<sup>8</sup> *Rules of Civil Procedure*, *supra*, Rule 14.05(3)(a) and 75.06(1).

<sup>9</sup> *Georganes v. Bludd*, 2014 ONSC 4655 (CanLII)

### **e) Impropriety in Payment of Executor Compensation**

One of the highly litigated estate accounting issues is executor compensation. The right to compensation to an estate trustee is derived from Section 61 of the *Trustee Act*.<sup>10</sup> Section 61 states that a trustee is entitled to compensation based on a “fair and reasonable allowance for his care, pains and trouble, and his time expended in or about the estate”. There are no statutory guidelines to determine how compensation is to be calculated. Compensation can also be fixed in the will. Where the compensation is not fixed, the general rule is that compensation is to be calculated by considering the five following factors:

- the size of the trust;
- the care and responsibility involved;
- the time occupied in performing the duties;
- the skill and ability shown; and
- the success resulting from the administration.<sup>11</sup>

The rule of thumb is that an executor is entitled to compensation equal to 5% of the value of the estate (2.5 % on assets or income coming into the executor’s hands and 2.5% on all payments out of the estate). However, that amount can be increased by an application to the court or agreement with the beneficiaries or even decreased depending on the circumstances and the five factors set out above.

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<sup>10</sup> *Trustee Act*, R.S.O. 1990, c. T. 23, sections 23(2) and 61.

<sup>11</sup> *Jeffery Estate, Re* (1990), 39 E.T.R. 173 (Ont. Surr. Ct.)

Executors are permitted a period of one year from the date of the death (sometimes referred to as the “executor’s year”) to gather in and realize estate assets. Where the administration of the estate takes longer than a year, the executor may also seek approval for a care and management fee of 2/5 of 1% of the average annual value of the estate assets. This is however not appropriate where delays in administering the estate are caused by the executor.

Executors’ compensation is intended to compensate the executor for doing their work as executors. It is important to keep time records or dockets of time spent doing executor’s work to support a claim for compensation or increased compensation.

Where an executor hires a person or an agent to do executor’s work, any fees charged in connection with such services are to be deducted from the executor’s compensation. The fees charged by solicitors in doing executors work, such as writing ordinary letters, attending to pay premiums on policies, banking, and performing services which a layperson is able to do are deducted from executor’s compensation.<sup>12</sup> Further, the fees for the preparation of accounts in court format for a Passing of Accounts are usually deducted from the executor’s compensation.<sup>13</sup>

As for the preparation of income tax returns, traditionally, income tax returns are considered executor’s work and fees charged by an accountant in connection with the preparation of income tax returns are deducted from the trustee’s compensation.<sup>14</sup> This is not always the case, however,

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<sup>12</sup> *Sharp v. Lush* (1879), 10 Ch.D. 468, apld.

<sup>13</sup> *Re Goldlust Estate*, (1991), 44 E.T.R. 97 (O.C.G.D.)

<sup>14</sup> *Re Briand Estate*, (1995), 10 E.T.R. (2d) 99 (O.C.G.D.)

and the court in *Re Holt Estate*, held that the question of who should pay for the preparation of tax returns should be decided on a case by case basis due to the diversity among estates.<sup>15</sup>

It is important to note that unless the will specifically states otherwise, an estate trustee can only receive compensation when the amount of compensation has been consented to by all of the beneficiaries or the court fixes the amount of compensation. To take compensation prior to obtaining consent or court approval is referred to as “pre-taking” and is considered improper and can lead to expensive litigation.<sup>16</sup>

The payment of executor compensation without obtaining the consent of the beneficiaries can lead to litigation against the estate trustee.<sup>17</sup> In *Zucker Estate*, the deceased left an estate valued at approximately \$43,000,000. Two executors were appointed as executors and estate trustees of the will, Kevey Leibow and an accountant by the name of Michael Moore who was a partner at the firm Taylor Leibow LLP.

Over the course of the administration of the estate, Mr. Leibow was paid \$500,000 in executor compensation and Mr. Moore received \$2,397,424.34 in executor’s compensation. Approximately \$1,182,439.54 that was received by Mr. Moore was transferred to the firm due to Mr. Moore’s partnership agreement with the firm. The firm at all times knew that Mr. Moore was performing executor services for the estate and approved him doing that work. A specific accounting code entitled “executor compensation” was set up in the accounting firms’ records to allow Mr. Moore to docket his time working on the estate. Mr. Moore used the firm’s resources

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<sup>15</sup> *Re Hold Estate*, (1994), 2 E.T.R. (2d) 163 (O.C.G.D.)

<sup>16</sup> *Re Pilo Estate* [1998] O.J. No. 4521 (O.C.G.D.)

<sup>17</sup> *Zucker Estate*, 2012 ONSC 2262 (CanLII)

to administer the estate, including the computer system, copy machines, fax machines, emails, courier services and support staff and sent letters dealing with estate matters on the firm's letterhead. The money received by the accounting firm as executor and trustee compensation for Mr. Moore's executor services were added to the firm's general revenues and allocated out to the partners as with any other firm revenue.

The beneficiaries commenced proceedings to, among other things, compel Mr. Moore and Mr. Leibow to pass accounts and repay executors compensation. In addition, there was a subsequent motion whereby the accounting firm itself, was also added as a party to the proceedings because the court found that the accounting firm needed to be added to adjudicate the matter effectively and to determine the firm's liability to the beneficiaries for Mr. Moore's actions.

On that motion, there were 7 counsel who appeared in court to argue the motion to add the accounting firm as a party, and thus, the legal fees were substantial, to say the least.

This case is an expensive lesson on "pre-taking" and the importance of obtaining the consent of all beneficiaries before taking compensation. It is a reminder that such conduct may leave the executor in the middle of a lawsuit, with a reported decision detailing their conduct forming part of the public record, thousands of dollars in legal fees and having to repay the beneficiaries the monies taken in excess of what would have been an appropriate executor compensation.

## 5. Costs Ramifications

An award of costs is the amount of money that a party in a litigation is required to pay to the opposing party towards legal fees incurred in the litigation. Traditionally, in estate litigation, costs were usually awarded to all parties, and to be paid out of the estate. More recently, the courts have been more willing to award costs against the unsuccessful party, as is the case in ordinary litigation. In *Susin v. Susin*,<sup>18</sup> a beneficiary applied to the court to have his brother removed as estate trustee. The court reviewed the trustees conduct and determined that he had acted properly and reasonably in administering the estate and ordered costs against the beneficiary. There have been instances, however, where the estate trustees have been ordered to pay costs personally and where they have been ordered to pay the legal costs of the other litigants.<sup>19</sup>

## 6. Conclusion

While some estate litigation is unavoidable, keeping proper estate accounts and understanding the role of an executor or estate trustee can certainly reduce the risk of conflicts arising or escalating to litigation. Estate litigation can be very expensive and can destroy families, relationships and reputations. Ultimately, the estate trustee's duty is to act in the best interests of the beneficiaries and often, the measuring stick for determining how well that duty has been complied is the quality and level of detail of the estate accounting records kept by the

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<sup>18</sup> (2007), 34 E.T.R. (3d) 770.

<sup>19</sup> For example, *Zandersons Estate Re*, 2011 ONSC 6755 (CanLII), and *Teffer v. Schaefers*, 2008 CanLII 46929.

estate trustee and the approval by the beneficiaries of the trustee's conduct and claim for compensation.