Frightening Away Litigation: *In Terrorem* and 'No Contest' Clauses

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Introduction

Testamentary freedom is a widely recognized and fundamental principle of estates and trusts law. A testator of sound mind has the right to dispose of his assets as he wishes, without explanation or reason.[1] Testamentary freedom, however, is not without its limits. There are several principled reasons why a testator may not dispose of his assets without consideration of his obligations, notably:

1. a testator must provide adequate support for his dependants, including a spouse, parent, child or sibling;[2]

2. a testator must honour his prior contractual obligations (e.g. a marriage contract); and

3. a testator may not make bequests which are contrary to public policy.

This paper will focus on the third category of restrictions on testamentary freedom listed above. The common law includes a rich history of testators attempting to reach out from beyond the grave and control the behaviour of their surviving relatives through their Will. When that control takes the form of a restriction on a gift, and when that restriction meets certain criteria, the clause containing the bequest may be considered an *in terrorem* clause. When that control takes the form of a prohibition on litigating issues relating to the Will, the clause is commonly referred to as a

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[1] Brian Schnurr, *Estate Litigation*, 2nd ed. (Toronto: Carswell 2014), Dale Rosenberg , "Issues in Focus: What are the circumstances in which Ontario Courts will strike down a bequest for being against public policy?" at p. 2.
[2] Part V of the *Succession Law Reform Act*, R.S.O. 1990, c. S. 26.

"no contest" clause. While some such clauses will not attract any reproach from the courts, others will be struck down as improper restrictions on testamentary bequests.

There are several comprehensive papers reviewing the *in terrorem* doctrine and the law concerning no contest clauses and the law on these subjects has not changed significantly in recent years.[3] This paper will briefly review the applicable law but will focus on two recent Ontario decisions which deal with these issues: *Spence v. BMO Trust Company*[4] and *Budai v. Milton*.[5]

In Terrorem Clauses

In terrorem is derived from the Latin "*in fear*" or "*by way of threat*". An *in terrorem* clause is a conditional gift in a Will, wherein a beneficiary will lose all entitlement to the gift if they breach or fail to adhere to the condition attached to the gift. It is generally used by a testator to encourage or dissuade particular conduct by a potential beneficiary.

In order to fall within the *in terrorem* doctrine, the following three conditions must be met:[6]

1. The legacy must be of personal property or blended personal and real property;
2. The condition must be either a restraint on marriage or one which forbids the donee to dispute the Will; and
3. the "threat" must be "idle"; that is the condition must be imposed solely to prevent the donee from undertaking that which the condition forbids. Therefore a provision which provides only for a bare forfeiture of the gift on breach of the condition is bad. However,

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[3] See e.g. Peter Lawson, "The Rule Against 'In Terrorem' Conditions: What Is It? Where Did It Come From? Do We Really Need It?", (2006) 25 Estates, Trusts and Pensions Journal, 71-94; and Hoffstein, Elena and Roddey, Robin, "No Contest Clauses in Wills and Trusts", The Six Minute Estates Lawyer 2008, April 8, 2008, Law Society of Upper Canada.
[4] 2015 ONSC 615 (Ont. S.C.J.).
[5] [2014] O.J. No. 4452, 2014 ONSC 5530 (Ont. S.C.J.).
[6] *Kent v. McKay* (1982), 139 D.L.R. (3d) 318, 13 E.T.R. 53 (BCSC); see also *Budai v. Milton*, ibid. at para. 6.

> if the donor indicates that he intended not only to threaten the donee but also to make a different disposition of the property to fix a benefit on another in the event of a breach of the condition, the 'threat' is not 'idle' and the condition is valid.

In Canada, *in terrorem* clauses are considered contrary to public policy and unenforceable.[7] They are unenforceable in large part due to the lack of a gift over provision. Without a gift over, Courts consider these clauses to be idle threats without any intended consequence if the condition is breached, except to deny the beneficiary the contemplated gift. Generally, the purpose of an *in terrorem* clause is simply to coerce a beneficiary to behave in a certain way.

Budai v. Milton[8]

There has been a small number of recent decisions in Ontario considering *in terrorem* clauses. In 2014, the Superior Court of Justice confirmed in *Budai v. Milton*[9] ("*Budai*") that the rule against *in terrorem* clauses continues to apply in Ontario and that any clause which meets the criteria set out in the jurisprudence is unenforceable.

In *Budai*, the validity of three clauses of a Will were at issue. The clauses in question read as follows:

> 6.1 Should my beneficiary, Kathy Budai challenge this Will or my choice of Executrix in any way then she will be removed from the Will and not inherit anything.
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> 6.2 Should Kathy Budai (my paid care giver) break her promise to me and place me back into the hospital for any reason then she will not inherit anything. Should any form

[7] Ibid.
[8] [2014] O.J. No. 4452, 2014 ONSC 5530 (Ont. S.C.J.).
[9] [2014] O.J. No. 4452, 2014 ONSC 5530 (Ont. S.C.J.).

> of machine or treatment be used to prolong my life against my wishes then she will inherit nothing. Should she be investigated or charged with any inappropriate care during my last days or death the she will receive nothing. It is my decision that this hospital visit is to be my last. I have chosen to pass away in my home without any further attempt to keep me alive. Kathy Budai has agreed to this action. Absolutely no action is to be taken to prolong my life and suffering.
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> 6.3 Should the estate have holdings due to my beneficiary not honouring my final wishes to pass away without any further efforts to prolong my life then the Executrix shall be in the control of distribution of the Estate. She may give away the funds in any way she sees fit. She may invest the balance of the Estate and use it for donations or any other purpose as long as the funds last. There are no restrictions to what she may do with the balance of the Estate.

Clause 6.1 is a good example of an *in terrorem* clause:

(1) since the applicant was the sole beneficiary of the estate, the legacy is of personal property or blended personal and real property;

(2) the condition forbids any challenge to the Will or choice of executrix; and

(3) There is no provision of a gift over in the event the condition is breached; therefore, the threat is idle.

Clause 6.1 was held to be *in terrorem* and declared void as contrary to public policy. Arguably, had the testator included a gift-over provision, clause 6.1 would not have come within the *in terrorem* doctrine and might have formed a valid “no contest” clause.

Clause 6.2 was challenged on the basis of uncertainty. The first two conditions, that the care giver not place the testator in a hospital for any reason and that no form of machine or treatment be used to prolong the testator's life for any reasons, were not found to be uncertain. The third condition, however, that the care giver not be investigated or charged with any inappropriate care during the testator's last days, was held to be void as contrary to public policy. The Court held that the wording of the clause allowed frivolous or false allegations to trigger the condition in the clause. It was held to be contrary to public policy to uphold and enforce a conditional clause which may encourage a person to make false allegations in order to disinherit a potential beneficiary.

Clause 6.3 was challenged on the basis that the executrix of the Estate drafted the Will, which raised suspicious circumstances. The Court acknowledged that suspicion was aroused by the executrix both drafting the Will and being a potential beneficiary, but held that this was not in and of itself sufficient to invalidate the clause.

Although *Budai* stands for the principle that the rule against *in terrorem* clauses continues to apply in Ontario, it also contains another lesson: the importance of seeking professional advice when drafting a Will. At the outset of his reasons, Justice Salmers noted that the case involved a terribly drafted Will and "an example of why untrained people should not attempt to undertake complicated matters on behalf of other people". Had a little more thought and effort be put into drafting the Will, the testator's intention to prevent litigation could have been upheld.

No Contest Clauses

Testators wishing to ensure that their Estate is not dissipated through costly litigation are not without recourse. Canadian courts have recognized the validity of "no contest" clauses in many circumstances.

In order to avoid being struck out as an invalid *in terrorem* clause, a no contest clause must provide for a gift over in the event that the condition is breached. By providing a gift over, the threat of forfeiture of the bequest if the condition is breached is a real threat, and not an idle one. As explained in *Feeney's Canadian Law of Wills*:

> (…) unless there is a gift over, the court will consider the condition as being *in terrorem* and void, although normally the condition will not be void if there is a gift over. The reason for the rule is that the court considers an express gift to someone else sufficient *prima facie* evidence that the gift was not *in terrorem*; the presence of the gift over tending to show that the condition was inserted not simply to coerce the original done but also to fix a possible benefit to another. [10]

In addition to a gift over provision, a valid no contest clause cannot be contrary to a public policy objective. This arises most frequently in cases where a testator attempts to deprive the Court of its jurisdiction or a dependant of a claim for support.

It is well established that a no contest clause cannot completely deprive a beneficiary of access to the judicial system. In *Harrison v. Harrison*,[11] it was held that a no contest clause must be limited to actions which seek to challenge a Will and they cannot extend to actions for the enforcement, interpretation or construction of a Will.[12] In other words, no contest clauses cannot be a blanket prohibition on all forms of litigation, which would entirely remove a Court's jurisdiction.

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[10] MacKenzie, James, *Feeney's Canadian Law of Wills*, 4th ed. (MarkhamL Butterworth's, 2000) at paras. 16.63.
[11] [1904] 7 O.L.R. 297.
[12] Hoffstein, Elena and Roddey, Robin, "No Contest Clauses in Wills and Trusts", The Six Minute Estates Lawyer 2008, April 8, 2008, Law Society of Upper Canada at p. 5; *Harrison v. Harrison*, (1904), 7 O.L.R. 297.

A no contest clause is also contrary to public policy, and therefore invalid, if it attempts to prevent a dependant from commencing a claim for support. A dependant's entitlement to seek support is protected by statute.[13] The purpose of such legislation is to protect dependants precisely in cases where a testator has not adequately provided for them. It would defeat the purpose of the legislation entirely, and would be contrary to public policy, if a testator could simply contract out of their statutory obligations through a Will.[14]

In some circumstances, a beneficiary may decide to proceed with litigation despite the no contest clause. If that beneficiary is successful in challenging the validity of the Will, the no contest clause will have no effect. In such a case, the entire Will, including the no contest clause, will be found to be invalid.

There may be sound reasons for a testator wanting to ensure that his Estate is not tied up in years of litigation. Disputes between second spouses and children of a first marriage, or disputes among siblings, are increasingly common. A well drafted no contest clause is one way of circumventing such disputes. Such a clause must include a gift over provision and should not contravene any public policy objectives. Otherwise, it may be found to be unenforceable and the testator's intention defeated.

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[13] Part V of the *Succession Law Reform Act*, R.S.O. 1990, c. S. 26;
[14] *Bellinger v. Fayes*, 2003 BCSC 563 at para. 16; Peter Lawson, "The Rule Against 'In Terrorem' Conditions: What Is It? Where Did It Come From? Do We Really Need It?", (2006) 25 Estates, Trusts and Pensions Journal, 71-94 at p. 93.

Testamentary Freedom and Public Policy: *Spence v. BMO Trust Company*[15]

The fine line between testamentary freedom and public policy objectives is once again at the forefront of estate practitioners' minds with the recent release of Justice Gilmore's decision in *Spence v. BMO Trust Company.*

Historically, Courts have been reluctant to interfere with a testator's freedom to dispose of his assets on the basis of public policy. It is only in the clearest of cases that Courts have intervened, notably in cases where a condition incites the commission of a crime, discriminates based on race or religion, promotes illegal activity, or interferes with family relations or marriages.[16]

In *Spence*, the testator had two daughters, Donna and Verolin. His relationship with Donna was limited at best. She moved to the United Kingdom in 1979 and had little to no contact with her father. The testator's relationship with his second daughter, Verolin, came to an end in 2002 when she announced she was pregnant and the father was a Caucasian man. The testator made it clear that he would not allow a "white man's child" into his house. In his Will, the testator left his entire Estate to Donna and added the following paragraph:

> I specifically bequeath nothing to my daughter Verolin Spence as she has had no communication with me for several years and has shown no interest in me as a father.

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[15] 2015 ONSC 615 (Ont. S.C.J.).

[16] MacKenzie, James, *Feeney's Canadian Law of Wills*, 4th ed. (MarkhamL Butterworth's, 2000) at paras. 16.57. See for example *Re Hurshamn* (1956), 6 D.L.R. (2d) 615 (B.C.S.C.) (discrimination based on religion); *Canada Trust Co. v. Ontario (Human Rights Commission)*, 2000 BCSC 445 (B.C.C.A.) (discrimination based on race); *Re Peach Estate*, [2009] N.S.J. No. 643 (S.C.) (restriction on alienation of property).

Justice Gilmore recognized that the Will on its face does not offend public policy, but she went on to consider the evidence of the applicant and another witness to conclude that the Will was invalid on the basis that Verolin was disinherited on the basis of racism, which is contrary to public policy. Justice Gilmore's reliance on extrinsic evidence to support a finding that the Will was invalid as contrary to public policy has been the subject of much debate and criticism in the legal community. The Will itself contains no offensive words and the admissibility of extrinsic evidence of the testator's intentions is questionable. The law normally does not allow direct extrinsic evidence of a testator's intentions where that evidence contradicts the wishes expressed in the testator's Will.[17]

The decision in *Spence v. BMO Trust Company* is also exceptional because it finds that the Will is contrary to public policy on the basis of the testator's intentions (evidence of which, the reader will recall, was adduced through normally inadmissible direct extrinsic evidence). Previous decisions finding condition gifts void for public policy reasons focus on the express wording of the Will.

This decision may significantly broaden the scope of challenges to the validity of no contest clauses, and conditional gifts, generally. It remains to be seen whether this decision is followed in other cases.

A Note About Incentive Trusts

It is still possible for a person to influence the behaviour of their prospective beneficiaries through the use of trusts, both *inter vivos* and testamentary. These so-called "incentive trusts" purport to motivate and reward certain behaviour (and discourage or punish opposite behaviour) through the

[17] See e.g. *Rondel v. Robinson*, 2011 ONCA 493.

terms which govern the distribution of income and capital from the trust property. There are many pitfalls which must be avoided in order to realize the settlor's intentions and proper advice is essential. This is a complex and highly technical aspect of succession planning and it is beyond the scope of this paper to review this subject. Several excellent papers are available.[18]

Conclusion

The *in terrorem* doctrine is alive and well in Ontario. However, the recent decision in *Spence* suggests that the Courts may begin taking a broader approach to public policy issues in Wills. If Courts apply the principles from *Spence* more generally, judges risk imposing their own values on a testator's wishes, significantly limiting testamentary freedom. While it is not without its own drawbacks, incentive trusts may offer a better approach to achieving a similar result, suggesting that the law finds it less objectionable to motivate behaviour with the "carrot", rather than the "stick".

[18] See e.g. Hoffstein, M.E., Roddey, R., and Stuckler A., "Incentive Trusts", Special Lectures 2003, Estates and Trusts Forum, LSUC, November 19-20, 2003.