ESTATE & TAX PLANNING · RECREATIONAL PROPERTY

Keeping the Cottage in the Family

A practical guide to passing down recreational property without forcing a sale.

Generations return. For many Canadian families, the cottage is the most emotionally valuable asset they own — and, quietly, one of the most tax-exposed. When the second parent dies, the CRA treats decades of appreciation as realized all at once.

Illustrative & Educational. General education only — not tax, legal, insurance or investment advice. The family is a composite created for illustration; names, details and all figures are hypothetical. See the Important Information on page 4.

01 The family at the lake

Paul and Diane are recently retired and live in Alberta. Their lake property, bought in the mid-1980s and improved over the years, is now worth far more than they paid. Their daughter **Claire** and her family use it most weekends; their son **Andrew** lives in another province and visits rarely — but neither child wants to see it sold. Their savings will fund retirement; what keeps surfacing is the cottage, and three goals they worry may be in conflict.

WHAT THEY WANT — ALL AT ONCE

- **Keep it in the family** rather than sell to settle the estate.
- **Treat both children fairly** — though only one uses the property.
- **Plan for the tax bill** that comes due at the next generation.

THE CORE TENSION

An asset everyone is attached to, used mainly by one heir, carrying a large tax bill that lands at the worst possible moment.

Solving it well takes tax, estate and insurance planning working together — the subject of this briefing.

02 Why a long-held cottage is a tax problem

Canada has no inheritance or estate tax. Instead, the tax arrives through a rule called a **deemed disposition**. On death, a person is treated as having sold their capital property at fair market value immediately beforehand — even though no sale takes place. The accrued gain on the cottage becomes taxable on the final return.

The spousal rollover buys time — it does not erase the tax

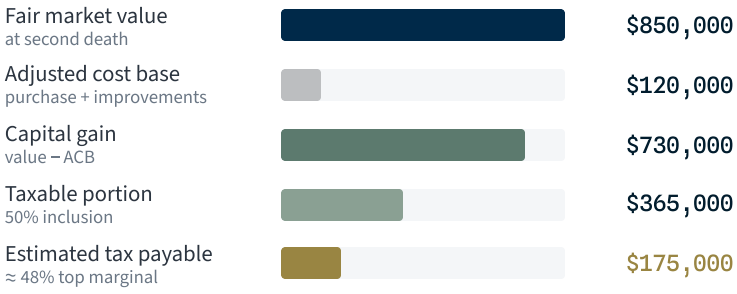
When the first spouse dies and the property passes to the survivor, a spousal rollover generally applies: the cottage transfers at its existing cost base and no gain is triggered. The tax is **deferred, not forgiven**. It surfaces in full on the second spouse's death — exactly when the family is least prepared for it.

One-half is taxable — the rate did not rise

As of 2026, one-half of a capital gain is included in income; a proposed increase to two-thirds was cancelled in 2025. The taxable half is then taxed at the deceased's marginal rate. For a long-held cottage, that single event can push the estate into the top bracket.

How the tax stacks up at the second death

ILLUSTRATIVE



Hypothetical figures for a property like Paul and Diane's. Even a "modest" cottage can carry a six-figure tax bill at the second death. Actual results vary by province, marginal rate and circumstances.

DEFINITIONS

Deemed disposition
A tax rule generally treating capital property as sold at fair market value upon the death of the owner (or the surviving spouse), triggering the accrued gain.

Adjusted cost base (ACB)
What the family paid plus capital improvements (a new roof, boathouse, major addition). A higher ACB means a smaller taxable gain.

Spousal rollover
Transfer to a surviving spouse at existing cost base, deferring — not forgiving — the gain until the second death.

Marginal rate
The tax rate on the next dollar of income. A large one-time gain can push an estate into the top bracket.

ADVISOR TIP

Keep every receipt. Capital improvements over the decades raise the ACB and directly shrink the taxable gain — one of the simplest, most valuable habits a cottage-owning family can build. Routine repairs do not count.

03 The principal residence exemption: a choice, not a freebie

A cottage *can* qualify as a principal residence — but a family unit may designate only **one** property for any given year. Using exemption years on the cottage means giving them up on the city home, and vice versa. The right choice depends on which property has grown more in value *per year of ownership*. For most families with a valuable city home, the exemption is best saved for that home — leaving the cottage gain to be managed through the structures on the next page.

04 Four ways to pass down the cottage

There is no single "right" structure — each trades simplicity against control, tax timing and family fairness. The table compares the options families most often weigh.

APPROACH	HOW IT WORKS	STRENGTHS	WATCH-OUTS
Outright gift or sale now	Transfer the cottage to a child during life.	Simplicity; removes future growth from the estate.	Triggers tax now at fair market value; loss of control; exposure to the child's creditors or divorce.
Joint tenancy with a child	Add a child as joint owner so the property passes by survivorship.	Avoids probate on that asset; feels simple.	Can trigger an immediate partial disposition; creditor / marital exposure; often sparks disputes between siblings.
Bequest in the will	The cottage passes through the estate under the will.	Full control retained for life; flexible.	Full deemed-disposition tax at the second death; no built-in fairness mechanism between heirs.
Testamentary cottage trust	A trust created in the will holds the cottage for the next generation under set rules.	Governance, fairness and protection; defers and structures the transfer; a neutral trustee keeps the peace.	More complex and costly to set up; subject to the 21-year deemed-disposition rule; needs funding for upkeep and tax.

The 21-year rule. A testamentary trust is taxed on its accumulated gains roughly every 21 years — a date that must be planned for, not discovered.

05 Funding the tax — instead of selling the cottage

Structure decides *who* gets the cottage and on what terms. It does not, by itself, *pay the tax*. That is the gap life insurance is designed to fill. A **joint last-to-die policy** pays out precisely when the deemed-disposition tax comes due — at the second spouse's death — and the death benefit is generally received tax-free, giving the estate liquidity so heirs are not forced to sell.

FUNDS THE TAX

Tax-free proceeds arrive when the CRA bill does — no fire-sale of the property.

APPROX. **$175,000**

EQUALIZES THE ESTATE

The cottage goes to the child who uses it; the other receives comparable value in cash.

KEY RISK

Without a funding plan, the deemed-disposition tax must be paid from the estate's other assets — or by selling the cottage itself. Joint tenancy and outright gifts can also expose the property to a child's **creditors or divorce**.

ADVISOR TIP

Insurance converts an unpredictable, ill-timed tax bill into a **funded, planned-for event** — and can solve fairness in the same stroke.

**Insurance products and services are offered through Raymond James Financial Planning Ltd.*

06 Back to Paul and Diane

With the pieces understood, the plan comes together. Paul and Diane keep the **principal residence exemption** on their city home, where it shelters the larger per-year gain. They establish a **testamentary cottage trust** in their wills — a neutral trustee, clear rules for how Claire may eventually acquire the property, and a plan for upkeep. They put a **joint last-to-die policy** in place so that, at the second death, tax-free proceeds cover the capital-gains tax and provide Andrew with an equalizing share in cash.

THE OUTCOME

The cottage stays in the family. Both children are treated fairly. The tax is funded in advance rather than scrambled for — and the plan is written down, so the next generation inherits clarity instead of conflict.

07 Five takeaways for cottage-owning families

1 **Know the number.**
Have fair market value and adjusted cost base estimated now — and keep receipts for every capital improvement.

2 **Plan for the second death.**
The spousal rollover only defers the tax; the full bill lands when the surviving spouse passes.

3 **Choose the exemption deliberately.**
The principal residence exemption applies to only one property per year—model which property it best protects.

4 **Match structure to the family.**
Gifts, joint tenancy, a simple bequest and a cottage trust each carry very different trade-offs.

5 **Fund the tax in advance.**
Life insurance can deliver tax-free liquidity exactly when the tax is due, and equalize between heirs.

How we can help

Cottage succession sits at the intersection of tax, estate law and insurance — areas usually handled separately and rarely coordinated. Our team works alongside your accountant and lawyer to model the tax, weigh the ownership structures and put the right funding in place, so the plan holds together as one.

IMPORTANT INFORMATION

This material is for general informational and educational purposes only and does not constitute investment, tax, legal, insurance or accounting advice, nor an offer or solicitation to buy or sell any product or service. The client story is a composite illustration; names and details are fictional and do not represent any actual client. All figures, scenarios and graphics are hypothetical and for illustration only; they are not predictions or guarantees, and individual results will vary based on personal circumstances, applicable law and other factors.

Tax and estate rules are complex, change over time, and differ by province; the discussion reflects rules the authors believe to be current as of 2026 and is necessarily general. Advisors are not tax or legal advisors. Clients should obtain independent advice from qualified tax, legal and accounting professionals before acting on any strategy described here. Securities-related products and services, insurance products, and trust services are offered through separate regulated and non-regulated affiliates; not all are members of an investor protection fund. Cochrane Wealth Management is a personal trade name.