Using Trusts in Estate Planning

What is a Trust?

A trust is a legal structure often used to provide someone with the benefit of an inheritance without giving them control over the inherited assets. Where assets are held in a trust, it is the trustee or trustees that manage and control the trust assets for the benefit of the beneficiary or beneficiaries.

The terms of the trust are generally drafted in an individual's Will or in a separate trust document. These terms will include the beneficiary or beneficiaries, the name(s) of the trustee(s), and instructions on how the trust is to be managed. The trust's terms can give the trustee full decision-making power over how much to pay out from the trust, for what purposes and when (a "discretionary trust") or can proscribe very rigidly the amounts that are to be paid out (a "non-discretionary trust"). A trust can also be a combination of these two, including some required payment schedule with the ability for the trustee to pay out more if reasonable. For example, a trust may require the trustee to pay $1,000 per month to the beneficiary, or to pay for all educational expenses, but may allow the trustee to pay additional sums at their discretion.

A trust which does not become operative until the settlor – the individual who creates the trust – dies is called a "testamentary trust." Most often, but not always, the terms of these trusts are found in the settlor's Will. A trust that is funded and operated during the settlor's lifetime is called an "inter vivos trust."

The following are common types of trusts used in estate planning:

- **Trusts for Minor Beneficiaries:** Individuals under the age of majority are not legally capable of owning and controlling assets. If an inheritance is received directly by a minor, the moneys need to be paid into court and will be largely inaccessible until the beneficiary attains the age of majority. As a solution, trusts should always be used when gifting large sums of moneys or assets to minor beneficiaries.

- **Trusts for Beneficiaries with Disabilities:** For beneficiaries who may be in receipt of government disability benefits, receiving a large inheritance could disqualify them from receiving such benefits in the future. Gifting through a discretionary trust is one way to preserve entitlement to such benefits. Even if the receipt of government disability benefits is not a governing factor, beneficiaries with disabilities can be particularly fiscally vulnerable and may benefit from the protection that a trust structure can provide for their inheritance.

- **Trusts for Vulnerable or Spendthrift Beneficiaries:** A trust can protect the inheritance received by a beneficiary who may be fiscally vulnerable. Such a trust could provide for an income stream to the beneficiary and could allow the trustee to pay for additional expenses, such as a car or reasonable travel.

- **Spousal Trusts:** Spousal trusts are an excellent tool to ensure that an individual is provided for when their spouse passes, while still protecting the funds. These types of trusts are frequently used in blended family situations. By placing funds in a spousal trust, an individual can still determine to whom the funds should ultimately pass once the surviving spouse has also passed away.

- **Trusts for Tax Savings:** In certain circumstances, trusts may offer tax advantages through income-splitting opportunities. However, the tax benefits of trusts have been significantly reduced in recent years due to changes in the Income Tax Act.

- **Trusts for Creditor and Marital Breakdown Protection:** Holding assets in a trust can provide for significant protection from creditors or on a marital breakdown. The extent of this protection may depend on the choice of trustee and the trust terms themselves.

- **Alter Ego and Joint Partner Trusts:** Alter Ego Trusts (AET) and Joint Partner Trusts (JPT) are special inter vivos trusts that individuals over the age of 65 may set up, primarily for incapacity and probate planning purposes. Assets can be moved into the AET or JPT on a tax-rollover basis, and the individual(s) who established the trust will receive the benefit of the trust's income, as well as of the trust assets unless they decide otherwise when setting up the trust. An Alter Ego Trust will be for the benefit of one individual, while Joint Partner Trusts are for the benefit of spouses or common-law partners.

Appointing a Trustee

Choosing the right trustee(s) is an important part of creating an effective trust structure. The trustee is responsible for ensuring the smooth, effective administration of the trust and must follow their fiduciary and legal obligations. The trustee must also be able to effectively communicate with the beneficiaries and any other related parties. For these reasons, among others, individuals may wish to engage the services of a professional trustee, such as a trust company, to act as a sole or co-trustee.

Speak to your financial advisor to learn more about the use of trusts in estate planning, and whether this solution is right for you.

[1] In Quebec, for example, the law requires that an independent trustee, being one who does not stand to inherit from the trust, be appointed as a trustee of all Quebec trusts.