

# WHY TESTAMENTARY TRUSTS ARE NOT DEAD

In 2014, the Department of Finance implemented a number of tax changes with respect to estates and testamentary trusts (trusts that are usually created in your Will and are only created after your death). The changes effectively eliminate the tax advantages of such trusts over inter vivos trusts (trusts set up during your lifetime), while potentially preserving some limited tax advantages in respect of estates and qualified disability trusts.

The most significant change is with respect to tax rates imposed on testamentary trusts. Currently, testamentary trusts are subject to graduated tax rates, unlike inter vivos trusts which are subject to the highest marginal tax rates. New legislation that takes effect in 2016 has eliminated this tax advantage.<sup>1</sup>

Although the tax advantages of such trusts have been eliminated, there are still many non-tax reasons why you may want to use a testamentary trust. Some of the advantages of using testamentary trusts are highlighted below.

## NON-TAX ADVANTAGES

### CONTROL OVER THE TIMING AND AMOUNT OF THE INHERITANCE

If your Will does not set up any testamentary trusts, your beneficiaries will receive their entire inheritance once the administration of your estate is complete. This may be undesirable, for example, in instances where a beneficiary is

still young (but has reached the age of majority in your province) and may not be able to handle a large sum of money. By using a testamentary trust in your Will, you can stipulate at what age you want a particular beneficiary to receive certain amounts. For instance, you could specify that a beneficiary receive 1/3 of the inheritance at age 25, 1/3 of what remains in trust at age 30 and the remainder at age 40.

### FLEXIBILITY IN STRUCTURING DISTRIBUTIONS TO BENEFICIARIES

If you give your trustee(s) discretion over the timing and amount of distributions from the trust, you can better protect the financial interests of your beneficiaries who may not have the responsibility or capacity to manage their own finances. By establishing a trust, you can ensure that your beneficiaries' ongoing needs are addressed. You can also provide incentives for certain behaviour through the use of a testamentary trust. For example, you could set up an education trust which specifies that distributions of income will only be made for post-secondary education.

### MANAGEMENT OF INHERITANCES FOR MINOR BENEFICIARIES

An increasing number of grandparents are designating their grandchildren as beneficiaries on their registered plans and life insurance policies. If your grandchildren are under the age of majority in their province at the time of your death, there may be complications concerning access to the funds. Such funds may have to be paid into court, and a government agency and/or a court-appointed guardian may become

<sup>1</sup> An exception to this general rule is available for a "qualified disability trust". All testamentary trusts will still be able to allocate income to multiple beneficiaries to utilize those beneficiaries' individual graduated tax rates as a "top up" to their other taxable income.



RBC Wealth Management

involved.<sup>2</sup> A better way to handle these and other testamentary gifts to minor beneficiaries is through the use of a testamentary trust, where the trust funds will be invested and properly managed until the beneficiaries meet the age of majority or some other age milestone (which you have specified) is reached.

### PRESERVATION OF A FAMILY INHERITANCE

Particularly with blended families on the rise, parents want to ensure that on their death, their surviving spouse is cared for but their children are not left out. A testamentary trust is a flexible tool that allows funds to be invested such that the income is distributed to the surviving spouse during his or her lifetime and the capital is distributed to the children after the death of the spouse. If your spouse remarries after your death and has more children, a trust can help ensure that on the death of your spouse, it is only your children who will benefit from the assets of your estate.

### PROFESSIONAL INVESTMENT MANAGEMENT

If you know that some of your beneficiaries are novice investors, by setting up a testamentary trust that allows for professional investment management, you can have peace of mind that your estate assets will be prudently invested for the benefit of your beneficiaries.

### A FINAL WORD

All of the non-tax advantages noted above also apply to inter vivos trusts. Accordingly, in certain circumstances it could be advantageous to set up an inter vivos trust during your lifetime to accomplish the same estate planning goals. Added advantages of using inter vivos trusts over testamentary trusts include potential probate fee savings, possible avoidance of will challenge legislation in BC, and providing for confidentiality of your assets after your death.

<sup>2</sup> In Quebec, the parents of a minor child would handle such funds without any court approval.

For those who do not want their assets tied up in trusts during their lifetime, testamentary trusts remain a useful vehicle for preserving and facilitating wealth transfer in accordance with your wishes.

### FOR MORE INFORMATION

**For more information, speak with an RBC advisor, call us at 1-855-833-6511 or visit our website at [www.rbc.com/estateandtrustservices](http://www.rbc.com/estateandtrustservices).**

RBC Estate & Trust Services refers to Royal Trust Corporation of Canada and The Royal Trust Company. This document has been prepared for use by Royal Bank of Canada, Royal Mutual Funds Inc., RBC Phillips, Hager & North Investment Counsel Inc., RBC Global Asset Management Inc., RBC Dominion Securities Inc.\*, Royal Trust Corporation of Canada and The Royal Trust Company. Royal Mutual Funds Inc., RBC Phillips, Hager & North Investment Counsel Inc., RBC Global Asset Management Inc., RBC Dominion Securities Inc., Royal Trust Corporation of Canada, The Royal Trust Company and Royal Bank of Canada are separate corporate entities that are affiliated. RBC Phillips, Hager & North Investment Counsel Inc., RBC Global Asset Management Inc., RBC Dominion Securities Inc., Royal Trust Corporation of Canada and The Royal Trust Company are member companies of RBC Wealth Management, a business segment of Royal Bank of Canada. \*Member—Canadian Investor Protection Fund.

The strategies, advice and technical content in this publication are provided for the general information only and benefit of our clients. This publication is not intended to provide specific financial, investment, tax, legal, accounting or other advice for you, and should not be relied upon in that regard. Readers should consult their own professional advisor when planning to implement a strategy to ensure that individual circumstances have been considered properly and it is based on the latest available information.

©/TM Trademark(s) of Royal Bank of Canada. Used under licence. © Royal Bank of Canada 2015. All rights reserved. Printed in Canada.