Why testamentary trusts are not dead

Ce document est aussi disponible en français.
This document is also available in French.

By using a testamentary trust in your Will, you can stipulate at what age you want a particular beneficiary to receive certain amounts.

Effective 2016, the Department of Finance implemented a number of tax changes with respect to estates and testamentary trusts (trusts created in your Will that come into effect 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 was with respect to tax rates imposed on testamentary trusts. Prior to the changes, testamentary trusts were subject to graduated tax rates, unlike inter vivos trusts which were and are subject to the highest marginal tax rates. The changes effectively eliminated this tax advantage.*

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.

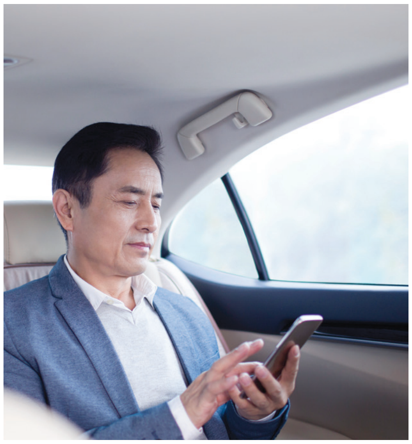
Flexibility in structuring distributions to beneficiaries

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

* 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.



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.

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 involved.* 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 British Columbia, and providing for confidentiality of your assets after your death.

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, speak with an RBC® advisor, call us at **1-855-833-6511** or visit our website at rbc.com/royaltrust.

* In Quebec, the parents of a minor child would handle such funds without any court approval.

VPS107445 124374 (10/2020)