

Testamentary Trusts Updates

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To date, testamentary trusts have been used as a tool to allow taxpayers to split income after death. These trusts are established through an individual's last Will and Testament for the benefit of another living person, generally a spouse or child. For tax purposes, a testamentary trust has historically had its own set of graduated tax rates, similar to those of individuals.



In the 2013 Federal Budget, the government announced their intention to consult on measures to eliminate the tax benefits that arise from the taxation certain trusts and estates at graduated rates. In the recently released 2014 Federal Budget, the Minister of Finance confirmed the government's intention to eliminate graduated rates for testamentary trusts, certain estates, and grandfathered inter vivos trusts, as proposed in last year's budget, and to instead apply flat top-rate taxation to these trusts and estates and make certain consequential changes.

Graduated rates will continue to apply for the first 36 months of a testamentary trust that arises as a consequence of an individual's death in order to allow executors time to settle the estate, however, any income retained in a testamentary trust beyond the initial three years after death will be taxed at the highest marginal tax rate.

One exception to this proposal is for the establishment of testamentary trusts for the benefit of disabled individuals (also known as Henson Trusts).

These change will likely apply to:

1. testamentary trusts (including certain estates and trusts created by will); and
2. certain inter vivos trusts established before June 18, 1971 (grandfathered inter vivos trusts);

The following are some additional changes that have been proposed in order to enforce this change:

1. the requirement to remit instalments;
2. the requirement to have a calendar year-end (Testamentary trusts that do not already have a calendar year-end will be deemed to have a year that ends on December 31, 2015 (or, for an

- estate, the end of its 36-month period, if later));
- 3. alternative minimum tax requirements;
- 4. classification as a personal trust without regard to the circumstances in which beneficial interest are acquired; and
- 5. liability for Part XII.2 tax.

Notwithstanding the foregoing, there are still other important reasons for establishing testamentary trusts, including spousal trusts, for our clients:

- 1. those established to address blended family situations, to ensure that all parties involved are adequately provided for, having consideration to the effect of the accounting and equalization provision of The Family Property Act (Manitoba);
- 2. those restricting access to funds, whether it be for the benefit of disabled individuals, an immature beneficiaries, or to assist beneficiaries with credit issues;
- 3. those established to hold and maintain funds for minor beneficiaries; and
- 4. those established to access multiple capital gains exemptions.

Testamentary trusts are also a helpful way to allow beneficiaries to protect their inheritance from creditors and possibly from marital property claims. This is beneficial for situations where a beneficiary operates a business or profession with substantial liability risk. This will allow you to ensure that your beneficiaries receive the money that is coming to them.

Testamentary trusts also allow you the flexibility to appoint a trustee who may be given the discretion (and/or instructions) as to paying the income and/or capital out of the Trust or allowing it to remain within the Trust.

Despite the government's proposed change, a testamentary trust continues to be a useful estate planning vehicle as it provides a great way for you to ensure that the beneficiaries of your estate are properly taken care of.

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