Advice from

THE BATTLEFRONT

Insight from life in the trenches

Why Trust?

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Trust me, trusts are a remarkably flexible legal structure that can provide numerous benefits when properly used. Trusts can protect assets from creditors and bankruptcy, permit an individual to structure personal affairs beyond his or her lifetime, multiply individual lifetime capital gain tax exemptions in Canada, and provide the tax efficient transfer of assets, along with other possible benefits.

However, trusts come with risks. There are specific legal formalities needed for the establishment and maintenance of a trust. Failing to strictly comply with these legal requirements can result in the trust failing which can lead to an expensive mess and failure to achieve the intended benefits. Further, as a failure to comply is usually not detected until a problem has arisen, it is frequently too late to implement corrective action and assets can be attacked by creditors or tax benefits lost.

Trustees must be aware of their responsibilities and fiduciary duties to the beneficiaries. Trustees are liable for carrying out the terms of the trust and can be at risk for not maintaining appropriate prudence in exercising their authority and judgement over the trust property.

Trusts are wonderful structures but must be implemented carefully with proper advice.

What is a Trust?

Contrary to widespread belief, a trust is not a separate legal entity. A trust is a relationship between the settlor (the gifter of the initial property), the trustees (one or more individuals that hold legal ownership of the trust property), and the beneficiaries (one or more persons that eventually receive the assets and/or income of the trust). A trust needs to strictly satisfy the **three certainties** required by law which are: (1) **Certainty of Intention** – a clear intention to create the trust relationship (i.e. trustees who agree to hold the initial trust property for the benefit of the beneficiaries); (2) **Certainty of Subject Matter** - clearly defined property to establish a trust (ex: a gold coin or a specific $20 bill); and (3) **Certainty of Objects** - clearly defined beneficiaries (ex: spouse and dependents). Trusts can be challenged on various grounds of uncertainty, so a carefully crafted trust agreement is strongly recommended to provide the certainties required for a properly established trust.

Trusts can be created during the lifetime of the settlor (*inter vivos trust*) or can be created pursuant to the last Will of a deceased (*testamentary trust*). Trusts come in a range of permutations to fulfill a range of situations – Discretionary Trusts; Directed Trusts; Fixed Trusts; Generation-Skipping Trusts; Henson Trusts; Hybrid Trusts; Irrevocable Trusts; Land Trusts; and Spendthrift Trusts among others.

Why use a Trust?

Trusts have long been used in personal matters to provide for the inter-generational transfer of wealth and assets. However, trusts can also be used effectively in business to insulate key assets from the liabilities of the risks of business while also growing value for other family members. Trusts can control tangible or intangible assets. The settlor may retain control over the assets as trustee, while also accumulating wealth for eventual transfer to the next generation. Additionally, trusts can be used to hold land and buildings to capture rising land values for other family members without surrendering control. These trust structures may also be implemented to multiply the lifetime capital gains tax exemption for Canadian residents. In certain situations, trusts can be used to provide for the long-term care of a special needs individual.

Who uses a Trust?

The flexibility of trusts make this legal structure adaptable to meet the needs of a wide range of individuals. Typically, business owners are good candidates for the effective use of trusts either at the initial stages of a business with large growth potential (i.e. capture growth for family planning purposes), or owners of mature operating businesses who are looking to protect value and plan for succession without giving up effective control during their lifetime. However, individuals may also use trusts to achieve financial objectives as well. There is no minimum or maximum value of assets that may be handled by a trust, as such a trust could be used by anyone seeking to structure their assets to achieve short-, medium- and long-term objectives.

Where to use a Trust?

Establishing a trust for family wealth planning (i.e. a family trust) is effective for planning the inter-generational transfer of wealth and assets, i.e. estate planning. However, trusts can also be used as a strategic part of insulating key business assets from business risks, including any liabilities to which the business owner may personally be exposed, i.e. personal guarantees in support of the business. Land trusts can be established to hold land separate from other risky activities or to transfer ownership after the lifetime of the settlor. Trusts can be designed to fit the particular circumstances as needed.

When to use a Trust?

Sooner than later! The key benefit of creditor protection can commence immediately once a trust is properly established. The additional benefit of accumulating value for other family members grows over time, so the earlier the assets are transferred into a trust, the more growth value will be captured within the trust structure. However, for income tax purposes in Canada, a trust is deemed to have sold and re-acquired all its assets every 21 years which may trigger tax consequences to the trust and beneficiaries. Proper planning is necessary to transfer value to the beneficiaries before negative tax consequences arise!

Thoughts to Take Away

Trusts are flexible, adaptive and useful structures in proper planning for both personal and business goals. Trusts can be crafted to fit the needs and the circumstances of individuals and businesses. Trusts can provide creditor-proofing for individuals and businesses, accumulate growth in a tax efficient manner, and plan for the inter-generational transfer of wealth. So, *trust me*, trusts are worth your trust!

About Loopstra Nixon LLP

Loopstra Nixon is a full-service Canadian business and public law firm dedicated to serving clients involved in business and finance, litigation and dispute resolution, municipal, land use planning and development, and commercial real estate. Major financial institutions, insurance companies, municipal governments, and real estate developers along with corporate organizations and individuals are among the wide range of clients we are proud to serve.

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