Understanding common types of trusts

These accounts give you more options over how you control and distribute your assets.

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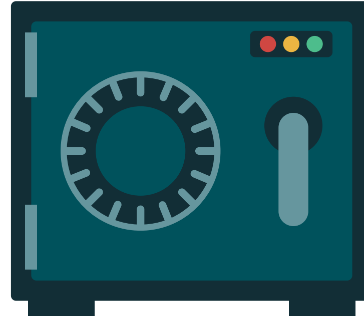

Many people think of trusts as something for ultra-wealthy people—a financial term you might hear about in an episode of Succession—but trusts can actually be useful financial planning tools for most Canadians.

In essence, a trust is a three-way relationship between a person with money or property to give, known as the settlor, the person they hand it over to for safekeeping, known as the trustee, and the ultimate beneficiary or beneficiaries of their largesse. Usually, these wealth transfers come with strings attached. Upholding those covenants is the trustee's responsibility, and they may be compensated for their services under the terms of the trust.

Trusts fall into either of two categories:

- **Testamentary** or estate trusts are bestowed by the settlor, upon their passing, as specified in the person's will. More specific kinds of testamentary trusts include qualified disability trusts and testamentary spousal trusts.
- **Inter vivos** or living trusts cover all other situations, with the common thread being that the settlor is still alive. There are many iterations of an inter vivos trust; the Canada Revenue Agency identifies 33. Here are some of the most common:

Family trust

Often set up by a business owner to transfer their company (or shares thereof) to their spouse, children, and grandchildren before they die. This process often involves an estate freeze, where the owner of the company (or real estate) locks in the value of the asset. The settlor only pays capital gains taxes on the appreciation until the day of the freeze; the beneficiaries would pay for any gains made after that date. Using an estate freeze, the settlor and trustee can determine who takes over the business without having to rack up a higher tax bill.

Alter ego trust

This is for someone 65 or older who wants the exclusive right to the income generated by assets in the trust. They will receive every dollar from the trust for as long as they live—no one else can claim anything that's in the trust as their own—after which these get directed to the beneficiaries

Revocable trust

Most trusts are irrevocable, meaning the settlor can't change their mind and reclaim the assets. With this type of trust, they can.

Henson trust

For protecting the assets of a person living with a disability. It also protects their eligibility to receive government benefits. Unlike other trusts, the trustee has full discretion over when and how much income and capital is distributed.

People create trusts for all kinds of reasons. One is to set conditions on the wealth transfer—for example, that it be doled out as monthly income to a spendthrift child rather than all at once, or be dedicated to the recipient's education expenses. Another is to hold real estate or securities for minors who may not be legally allowed to own certain assets.

Still another reason to establish a trust is to minimize taxation for the settlor, the beneficiaries or both. The trust itself is subject to tax at the top marginal rate, so trusts usually distribute their income to the beneficiaries, who may benefit from lower tax rates. Trusts are also not subject to probate fees and reduce estate taxes at the time of death.

Finally, in contrast to wills, details around how much and what assets are in a trust can be kept private if you'd prefer others not to know the details of who you've left your money to.

While the concept of a trust is fairly straightforward, with so many options, how to use one in practice can be confusing. If you're considering setting one up, consult a lawyer or tax planning expert first.

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