

# TODAY'S ISSUES



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## TRUSTS VERSUS PERSONAL BEQUESTS

When I talk with clients about financial planning, a phrase I hear most is “We have been to our lawyer and our wills are up to date”. Yeah right! Almost every will I see for high net worth people is profoundly lacking in the tax planning area. I don’t know how many articles I’ve written about the use of trusts in wills but seldom do I see them as a planning tool.

To cut to the chase, I simply want to provide readers with an example of the tax benefits of leaving assets to a trust instead of an outright bequest. There are many variations.

Jimmy Jones has a substantial estate and can leave \$1,000,000 to his wife Jenny without any significant tax – even if capital gains are realized on the bequest. Jenny in her own right is well off and is in the top tax bracket. As Jimmy’s will is now written, Jenny will get the \$1,000,000 directly. Jenny plans to invest 70% of her inheritance in stocks producing annual capital gains of 10% and dividends of 3% of her portfolio. She will invest \$300,000 of her inheritance in bonds with a 5% return.

Jenny’s annual income tax on her inheritance (after considering her existing income) would be as follows:

<b>Income</b>	
Dividends	21,000
Capital gains	70,000
Interest	<u>15,000</u>
Total Income	106,000
<b>Personal Income Tax</b>	28,600

Had Jimmy revised his will to direct the \$1,000,000 to a trust for Jenny (a non-qualifying spousal trust in this case), the tax result would have been dramatically different. The trust income tax would be as follows:

<b>Trust Income Tax</b>	14,400
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If Jenny needs cash, she simply withdraws capital from the trust without personal income tax. She could even receive income if this suits her total tax situation.

If Jenny invested her \$14,000 annual tax savings at a 6% after tax rate of return, she would have \$185,000 in 10 years. By passing the property to a trust for Jenny instead of to her directly, her annual tax is cut in half. That would probably pay a grandchild's education.

There are other advantages from the use of trusts in a will such as reducing the OAS claw back of the survivor, the tax-free transfer of capital to remaining beneficiaries and the elimination of one level of probate fees. There are others as well.

If you are a high net worth person, does your will contain an appropriate trust – better still several trusts? Maybe you should have a look.

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