

## Alter Ego and Joint Spousal Trusts

### “65 and Over”

Recent changes to the *Income Tax Act* over the past year now permit individuals at least 65 years of age to develop Alter Ego Trusts and Joint Spousal Trusts. For some, this may be an attractive estate planning vehicle and can serve as an alternative to a Will.

Similar to an Alter Ego or Joint Spousal Trust, an Inter Vivos Trust, or living trust, has always been available to Canadians, however, its use as an alternative to a Will, (similar to a revocable Living Will in the US), was always unattractive in Canada because of the tax consequences involved in their use. The concern being that if you transfer to a trust an asset that has increased in value, this is a disposition and triggers immediate capital gains tax.

Under the Alter Ego or Joint Spousal Trust amendments, anyone over 65 can now transfer assets to this particular type of trust on a tax-deferred basis. In other words, the trust takes over the asset at its cost; the tax on the gain is deferred until the disposition of the asset by the trust, or until the trust is terminated and the asset distributed to the beneficiaries. In short, the transfer is tax neutral. There are no income tax advantages, nor any disadvantages.

For the tax rules to apply, the income and capital must be solely for the benefit of the settlor or his/her spouse (that is, the original owner of the assets) during his or her lifetime. The settlor is also the trustee, so retains complete control over the assets until his or her death. He or she can name as beneficiaries of the trust on death whomever would have been beneficiaries under his or her Will, including charities. The trust can hold all or only some portions of the client's estate.

If the trust holds everything, it replaces a Will, but with this important difference: as long as a testator has capacity, he or she can change a Will at any time, right up to the time of death; with a trust, it is not so easy to change. This can be a good thing (it avoids the risk of undue influence) and a not such a good thing (if urgent changes in beneficiary are legitimately desired).

There are two essential benefits of an Alter Ego or Joint Spousal Trust. Initially, everything transferred to the trust during one's life is not in the estate on death, and is therefore free of probate fees and the costs of probate. Secondly, since the trust already owns the transferred assets at the time of death, they are not part of the estate so the *Wills Variation Act* does not come in to play. This advantage is of particular importance with second marriages, where the potential frequently exists for a conflict between the testator's children and the surviving second spouse. Once everything is in the trust, with both the wife and the children as beneficiaries in proportions the settlor has decided upon, then not only will fights after death be avoided, but the settlor can make clear to all parties during his or her remaining years that all is settled, fair and final.

The special tax treatment afforded to the Alter Ego Trust is available also to the Joint Spousal Trust, where distribution occurs only on the death of the surviving spouse. One or both can

contribute to the trust (if the contributor is 65), and the income can only be used for the benefit of the settlor and the spouse during their joint lifetimes.

In appropriate circumstances, the Joint Spousal Trust could replace the very common Wills where each leaves everything to the other spouse, and on the survivor's death, the remainder goes to the children or grandchildren. But often in these cases, the spouse who believes he or she will die first worries that the surviving spouse will remarry some gold-digger who will take everything from the kids! The Joint Spousal Trust would help this situation.

Despite the obvious advantages of these trusts--the saving of probate fees, the minimization of *Wills Variation Act* problems, and the protection against gold-diggers--one must be careful to remember the limitations to their use. Some examples: in the case of real estate, the transfer to the trust may trigger Property Purchaser Tax, which would counteract any savings in probate fees for properties over \$300,000 in value. However, it should be noted that a Principle Residence along with its associated Principle Residence exemption is transferable to the Alter Ego Trust.

RRSPs and RRIFs cannot be transferred to the trust at this time. As well, where the estate consists of appreciating assets, it is important to check with an accountant to see if the savings on probate fees would be offset by the need to pay greater capital gains tax on death, for the reason that a trust, unlike an individual, does not have personal exemptions available to claim in the year of death.

But subject to these limitations, I believe there are many situations where an Alter Ego Trust or a Joint Spousal Trust could be of great advantage in an estate plan, whether used as a replacement to Wills or used alongside the Wills for particular assets only. As always, your particular situation should be assessed by an experienced professional before determining whether this vehicle will work for you.

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***I caution my readers that the information expressed in this article should in no way be construed as legal advice. If you would like further information on this or any other topic please contact me at the address below.***

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