The RBC Dominion Securities Family Trust

A guide for clients

Professional Wealth Management Since 1901

RBC Dominion Securities

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Is an RBC Dominion Securities Family Trust right for you?

The RBC Dominion Securities Family Trust allows high-income Canadians to save taxes by earning capital gains in the hands of children or grandchildren that pay little or no taxes. Every child or grandchild in Canada that has no other income can earn approximately $18,000 of capital gains tax-free every year (varies by province) without the income attribution rules applying. The RBC Dominion Securities Family Trust can be established to take advantage of this annual opportunity, while still providing the parent or grandparent with access to the monies funded to the trust. The information contained in this publication reflects current tax laws at the time of printing.

If you have low-income children or grandchildren, there are three major benefits of setting up an RBC Dominion Securities Family Trust:

1. If the child or grandchild has no other income, they can earn approximately $18,000 of capital gains every year tax-free through the trust due to their basic personal tax amount (varies by province). Capital gains earned in excess of $18,000 are still taxed in the name of the child or grandchild but at a much lower tax rate than the high-income parent or grandparent.
2. The parent or grandparent is permitted to loan monies to the RBC Dominion Securities Family Trust (with or without interest), so they should not lose access to the loan capital.
3. Investment income earned in the trust can be used to pay for expenses that directly benefit the child or grandchild (e.g. private school tuition, lessons, camps, gifts, etc).

You may be a candidate for the RBC Dominion Securities Family Trust if you have low-income children or grandchildren and you have surplus non-registered capital you can transfer to the trust.

What is a trust?

A trust, unlike a corporation, is not a legal entity but rather a relationship between the trustees and the beneficiaries. The trustee holds legal title to the property within the trust and the beneficiary holds beneficial title. Beneficial ownership means that the beneficiary has rights to the property, even though they may not be the registered owner of the property. The trustee must exercise her/his powers in accordance with the terms of the trust for the exclusive benefit of the beneficiaries.

The provisions of the trust are set out in a trust agreement or deed. The trust agreement details the name(s) of the trustee(s), the scope of their powers, the beneficiary or beneficiaries of the trust, and how the trust assets are to be managed.

There are many reasons why people establish trusts, including:

- To hold assets for minor, disabled or spendthrift beneficiaries until an appropriate distribution date
- Income splitting
- Privacy
- Creditor protection
- Probate tax avoidance
- Part of an estate freeze transaction for a business owner

The RBC Dominion Securities Family Trust has been structured primarily for the purpose of splitting investment income with low-income family members. The RBC Dominion Securities Family Trust agreement may not be appropriate for some of the other reasons that trusts are established as indicated above. You should consult with your tax and legal advisors if you want to set up a trust for a reason other than primarily income splitting.

Inter-vivos and testamentary trusts – what are the differences?

If you are considering using a trust as part of your financial planning, you should be familiar with the two main types of trusts.

The first is known as an inter-vivos or living trust, which is created while you are still alive. The second is a testamentary trust, which is created by the terms of a person's Will. A testamentary trust is formed when one passes away and is funded by their estate.

The RBC Dominion Securities Family Trust is an inter-vivos trust.

The following table outlines some differences between an inter-vivos trust and a testamentary trust.

	Inter-vivos trust	Testamentary trust
How established	■ Created during the settlor's lifetime ■ Takes effect when the assets are transferred into the trust.	■ Created under the terms of a Will or other testamentary documents. ■ Takes effect after the death of the testator.
Taxation year	■ January 1 – December 31	■ The executor is permitted to select any 12-month period.
How income is taxed within the trust	■ Income and capital gains retained in an inter-vivos trust is taxed at the top personal marginal tax rate with certain exceptions. ■ Income and capital gains that are paid or payable (see below) to the beneficiaries are taxed in the hands of the beneficiaries subject to the attribution rules, instead of taxed in the trust at the top tax rate. ■ The basic personal tax amount cannot be claimed on the trust tax return.	■ Income and capital gains earned in the testamentary trust is taxed within the trust at the same graduated tax rates as an individual, but special rules may enable income to be taxed in the hands of beneficiaries instead of taxed in the trust. ■ Income attribution does not apply, since the testator – as the creator of the trust relationship – is deceased. ■ The basic personal tax amount cannot be claimed on the trust tax return.

PAID OR PAYABLE

Since the RBC Dominion Securities Family Trust is an inter-vivos trust, if the investment income earned in the trust is not "paid or payable" to a beneficiary during the year, the investment income including capital gains will be taxed in the trust at the top marginal tax rate – defeating the income splitting purpose of the RBC Dominion Securities Family Trust.

PAID INCOME

Income that is "paid" to a beneficiary is when the income is actually distributed directly from the trust to the beneficiary. Since it will be common to have a minor beneficiary in the RBC Dominion Securities Family Trust, it may not be appropriate to pay the income directly to the minor beneficiary. However, according to the Canada Revenue Agency (CRA), income is also considered "paid" to a beneficiary if the trustees pay the income directly to a third party to pay for an expense that directly benefits the beneficiary. See the section titled "Using a trust to pay for children's expenses" for more details on this.

PAYABLE INCOME

Income that is "payable" to a beneficiary is when the income is not directly paid to a beneficiary or a third party but the beneficiary is entitled in the year to enforce payment of the amount. So in this case, the income can be retained in the trust and be reinvested, but the trustee must document that a certain amount of income was made payable to the beneficiary during the year and the trust owes that amount to the beneficiary. As a result, the beneficiary at any time in the future (other than the Age 40 trust exception below) has the right to demand payment of the amount of income that was made payable to them and owing to them.

There are two Family Trust options at RBC Dominion Securities – Discretionary and Age 40 (see section titled "The Trust Options at RBC Dominion Securities" for more information). If an Age 40 Trust option is used then any income earned in the trust before the year the beneficiary turns age 21 is deemed to have become payable but the beneficiary cannot enforce payment of that amount until age 40. With the Discretionary Trust option, the beneficiary (regardless of age) can at any time demand payment of an amount that was made payable to them.

As a result of the above, to achieve family income splitting it is imperative for the Discretionary Trust option (beneficiary of any age) and the Age 40 Trust option (beneficiary age 21 or older) that the trustee make the income paid or payable to a beneficiary before December 31 of each year in order for the income not to be taxed in the trust at the top tax rate. In most cases, this will mean at a minimum the trustees would designate the realized capital gains to be paid or payable to a child or grandchild beneficiary in order for the capital gains to be taxed in their hands at their low tax rate.

Speak to your Investment Advisor for documentation to designate income paid or payable to a beneficiary.

Family income splitting

There are two reasons why income splitting is possible in Canada to reduce the family's tax burden:

1. Canada's tax system is based on graduated tax rates.
2. Everyone in Canada has a tax-free basic personal amount of approximately $9,000.

A graduated tax rate system basically means that there is a higher marginal tax rate on taxable income as income increases. The highest marginal tax rate is not applied until taxable income exceeds approximately $123,000. However, a fairly high marginal tax rate applies even when taxable income exceeds $38,000.

Furthermore, each Canadian resident can earn approximately their first $9,000 of taxable income tax-free every year due to the basic personal tax amount (varies by province). Since only 50% of capital gains are taxable, this means that up to about $18,000 of capital gains can be earned tax-free every year by a person who has no other income, regardless of age.

As a result of these two factors, if income can be shifted from a high-income parent or grandparent to a low-income child or grandchild, then the family can realize substantial tax savings. The RBC Dominion Securities Family Trust can be established to take advantage of this tax savings opportunity.

ATTRIBUTION RULES

In order to prevent abusive income-splitting arrangements, the Income Tax Act (ITA) has income "attribution" rules. Basically, these rules will attribute taxable income back to the related family member that actually supplied the capital for investment, thus achieving no tax savings. The following table summarizes the income attribution rules depending on how the capital is funded to the trust and depending on what type of investment income is then distributed from the trust to the related beneficiary:

Method of funding trust/ beneficiary that receives distribution from trust	Type of investment income distributed from trust to beneficiary	
	Interest and dividends	**Capital gains**
Gift or interest-free loan to trust/minor child or grandchild beneficiary	Attribution	No attribution
Gift to trust/adult child or grandchild beneficiary	No attribution	No attribution
Interest-free loan to trust/adult child or grandchild beneficiary	Attribution[1]	No attribution
Prescribed rate loan to trust/spouse, child or grandchild beneficiary of any age	No attribution	No attribution
Gift or interest-free loan to trust/spouse beneficiary	Attribution	Attribution

[1] Assumes that one of the main reasons for the loan was to reduce or avoid tax of the parent or grandparent.

As indicated in the above table, in general, there is no attribution on capital gains distributed from the trust to a child or grandchild beneficiary regardless of how the parent or grandparent funded the capital and regardless of the age of the child or grandchild.

Notwithstanding the above, there is a "super attribution" rule in the ITA [subsection 75(2)] where all the investment income earned in the trust could be attributed back to the transferor parent/grandparent, thus achieving no income splitting. That is, if the person that transfers property to a trust has too much control over the trust decisions or can receive back the property transferred to the trust (other than by repayment of a bona-fide loan), then it is possible that all investment income earned in the trust including capital gains will be attributed back to the person that transferred monies to the trust.

However, there are methods to structure a trust so that capital gains are not attributed back to the transferor but can be taxed in the hands of the children/grandchildren achieving income splitting.

RBC Dominion Securities has received a tax opinion from Thorsteinssons LLP on how best to structure the RBC Dominion Securities Family Trust so that capital gains distributed from the trust to a child/grandchild beneficiary would not be subject to attribution and can be taxed in the hands of the child/grandchild beneficiary.

The following are recommendations from Thorsteinssons LLP on how the RBC Dominion Securities Family Trust should be structured to avoid the subsection 75(2) attribution:

- The settlor (the person establishing the trust and transferring the cash to the trust) should not be the sole trustee
- The settlor should not be a beneficiary
- If a loan is made to the trust, it should be a bona-fide loan
- The settlor should not be delegated any investment powers (i.e. should not be the Investment Trustee)

- The settlor can be one of three trustees where all decisions are made by a majority rule decision process at all times

You must consult with your tax advisor for more details on this matter.

See the section titled "Establishing a RBC DS Family Trust" for more details on the structure of the RBC Dominion Securities Family Trust.

The trust options at RBC Dominion Securities

There are three inter-vivos trust options that you can consider at RBC Dominion Securities to achieve family income splitting. All three options have "off-the-shelf" trust deeds that our internal and external legal counsel has prepared. These trust deeds cannot be amended or customized.

Before establishing a trust using one of the three RBC Dominion Securities trust options you must consult with your own tax and legal advisors to review the legal agreements and for advice to discuss the appropriateness of the trust based on your own goals and circumstances.

If one of three RBC Dominion Securities trust options is not suitable for you based on your own goals and circumstances, you can consider having a customized trust deed prepared by your legal advisor.

The three trust options offered at RBC Dominion Securities are:

1. RBC Dominion Securities Formal Trust
2. RBC Dominion Securities Family Trust – Discretionary
3. RBC Dominion Securities Family Trust – Age 40

The key differences between these three trust options are indicated in the following table.

	Formal Trust	Family Trust – Discretionary	Family Trust – Age 40
Type of beneficiaries	Anyone	Spouse, children and grandchildren (can also add parents, siblings, nieces and nephews)	Anyone
Maximum number of beneficiaries per trust	Six	Multiple	One
Minimum initial contribution	None	$50,000	$50,000
Contributions	Irrevocable gifts	Gift or demand loan – interest-free or at CRA prescribed rate	Gift or demand loan – interest-free or at CRA prescribed rate
Contributor's access to capital	None – capital must be used for beneficiary's benefit	If contributor loans money to trust, then full access to loan capital	If contributor loans money to trust, then full access to loan capital
Beneficiary's access to investment earnings payable to them	Immediate	Immediate	If earned prior to age 21, then as late as age 40; if earned after age 21, then immediate
Attribution for child/grandchild beneficiary[1]	Interest and dividends if beneficiary is a minor; no attribution on capital gains	Interest and dividends if funded by interest-free loan regardless of age; no attribution on capital gains	Interest and dividends if funded by interest-free loan regardless of age; no attribution on capital gains
Annual RBC Dominion Securities administration fee	None	$150 (if using Royal Trust for T3 tax return preparation $250 (if not using Royal Trust for T3 tax return preparation)	$150 (if using Royal Trust for T3 tax return preparation $250 (if not using Royal Trust for T3 tax return preparation)
Annual trust tax return fee if using Royal Trust	Accountant to complete	$350 ($450 in Quebec)	$350 ($450 in Quebec)

[1] Assumes the trust has been structured so that capital gains are not attributed to the contributor.

The primary difference between the RBC Dominion Securities Formal Trust and the two RBC Dominion Securities Family Trusts is that the RBC Dominion Securities Family Trust permits the parent to loan monies to the trust with or without interest, whereas any monies contributed to the RBC Dominion Securities Formal Trust are considered irrevocable gifts.

The demand loan feature of the RBC Dominion Securities Family Trusts allows the parent full access to the loan capital at anytime by calling back all or a portion of the loan. As a result of this "safety feature", the parent is likely more comfortable to fund greater amounts to the RBC Dominion Securities Family Trust compared to the RBC Dominion Securities Formal Trust. Greater funding to the RBC Dominion Securities Family Trust will allow the trust to potentially generate more capital gains that will be subject to little or no tax. For example, to create $18,000 of annual tax-free capital gains in the name of the child, assuming annual realized capital gains of 6%, the parent would have to fund $300,000 to a trust [$300,000 x 6% = $18,000]. Most parents are not comfortable making an irrevocable gift of $300,000 to the RBC Dominion Securities Formal Trust, which their child would have full rights to at age of majority. However, loaning $300,000 to the RBC Dominion Securities Family Trust, which the parent can call back any time, is a strategy that many parents would consider in order to create tax-free capital gains.

Having said this, by loaning larger amounts to the RBC Dominion Securities Family Trust, there will likely now be more investment income that must be paid to the beneficiaries or used directly for their benefit. You should take this into consideration when determining how much to loan to the RBC Dominion Securities Family Trust. Speak to your Investment Advisor for additional guidance.

INTEREST-FREE LOAN VERSUS CRA-PRESCRIBED RATE LOAN

The lender will have the option of loaning monies to the RBC Dominion Securities Family Trust at either the CRA-prescribed rate or on an interest-free basis. There will be no attribution on any investment income (interest, dividends and capital gains) if the loan is made at the CRA-prescribed rate at the time the loan is established. In this case, the trust must pay interest to the lender at the CRA-prescribed rate. The annual interest must be paid on or before January 30 of the following year. The lender would declare the interest received and pay tax at their marginal tax rates. Alternatively, if an interest-free loan is made to the trust, then interest and dividends distributed to a child or grandchild (regardless of age) will be attributed back to the lender but not capital gains if the trust is structured properly.

If the CRA-prescribed rate is high, then there may not be any meaningful tax savings by loaning cash to the RBC Dominion Securities Family Trust at the CRA-prescribed interest rate since the lender parent would have to declare higher interest income on the loan and pay tax at their high marginal tax rates. In this case, it may be preferable to loan monies to the trust on an interest-free basis with the trustees focusing on generating primarily capital gains for a child or grandchild beneficiary so the attribution rules do not apply. Of course, the investment risk of earning primarily capital gains is generally higher compared to earning interest and dividends, so the trustee needs to take this into consideration.

You should speak to your tax advisor to determine the pros and cons of loaning monies to the trust either at the CRA-prescribed interest rate or on an interest-free basis.

RBC DOMINION SECURITIES FAMILY TRUST - DISCRETIONARY TRUST VERSUS AGE 40 TRUST

The Discretionary Trust option and the Age 40 Trust option are identical in all respects except the following two differences:

1. Number of beneficiaries per trust
2. Beneficiary's right to the income that was made payable to them

That is, the Age 40 Trust only allows one beneficiary per trust. The Discretionary Trust automatically names a "class" of multiple beneficiaries, which includes the settlor's spouse, children and grandchildren. If you wish, you can also have a Discretionary Trust agreement where in addition to the spouse, children and grandchildren as beneficiaries, the settlor's parents, siblings, and nieces and nephews are also beneficiaries. As previously discussed, the settlor would not be a beneficiary of the trust.

The other key difference between the Age 40 Trust and the Discretionary Trust is that with the Discretionary Trust, a beneficiary has the right to immediately demand the payment of any income that was not paid to them directly but rather designated as payable to them for income splitting. With an Age 40 Trust, the beneficiary cannot demand payment of any income that was payable to them before age 21, until age 40 (the trustee can pay earlier if they wish).

If you expect to have multiple beneficiaries, the Discretionary Trust may be suitable. If you only have one beneficiary, the Age 40 Trust is most suitable. However, even if you have multiple beneficiaries, if you want greater control of the income earned in the trust that was not paid directly to a beneficiary, then a separate Age 40 Trust per beneficiary could be considered.

Using a trust to pay for children's expenses

The RBC Dominion Securities Family Trust is a tax-effective strategy to create long-term wealth for your children or grandchildren. However, if structured correctly and documented properly, it may also be possible for the trustee to use some of the trust's investment income (interest, dividends and capital gains) to pay for expenses that directly benefit the child rather than let it all accumulate it in the trust.

As previously mentioned, in order to avoid having the investment income taxed in the trust at the top marginal tax rate, the income must be paid or made payable to the beneficiary. However, the CRA has taken the administrative position that it is possible to have income earned in the trust to be deemed paid to a beneficiary and thus considered taxable income of the beneficiary (subject to the attribution rules) even though that income was not paid directly to the beneficiary but rather used by the trustee to pay for expenses that directly benefit the beneficiary.

In *Income Tax Technical News #11*, CRA has indicated that expenditures made for the child's benefit by the trustee can include amounts paid for the support, maintenance, care, education, enjoyment and advancement of the child, including the child's necessaries of life. If the trust income is used to pay for expenses that benefit the child, it is important that the expenses are documented properly and receipts retained. Parents and trustees should review *Income Tax Technical News #11* to determine the process to have trust income paid directly for expenses that benefit the child.

Some types of expenses that may qualify as directly benefiting the child include:

- Private school tuition
- Post-secondary school fees
- Lessons
- Camps
- Sports equipment
- Gifts
- Clothing

Note that there have been well-known court cases where a family trust was set up, but there was not sufficient documented evidence that the trust income was used for expenses that directly benefit the child beneficiary. Furthermore, there were some concerns that the trust income was not used to benefit the child beneficiary directly but rather benefit the parent or the entire household. If this was the case, the trust income would be taxed in the trust at the top marginal tax rate and potentially also taxed in the hands of the individual that actually benefited from the trust expenditure resulting in double taxation.

If the trustees plan on using the trust's income to pay for expenses of the beneficiary, the expenses must unequivocally benefit the beneficiary and the trustees must keep proper records. Furthermore, in some cases where an expense is tax-deductible to the parent (e.g. daycare) it may be more tax-effective for the parent to pay this expense directly rather than having it paid by the trust.

Parents and trustees should speak to their legal or tax advisor for further advice and guidance on this matter before using the trust income to pay for the children's expenses.

RBC Dominion Securities Family Trust versus a Registered Education Savings Plan

Many parents and grandparents have contributed to a Registered Education Savings Plan (RESP) in order to save for post-secondary education. The following table outlines the differences between an RESP and the RBC Dominion Securities Family Trust.

Due to the government grant (CESG) available with an RESP and the tax-deferred growth within an RESP, saving for a child or grandchild's post-secondary education costs using an RESP is a sound financial strategy for most parents and grandparents. The RBC Dominion Securities Family Trust is not necessarily meant to replace an RESP. However, an RESP has limits on contributions and when and what expenses the funds can be spent on. The RBC Dominion Securities Family Trust tends to be more flexible in terms of funding limits and when and what expenses the funds in the trust can be used for. Therefore, depending on your goals, the RBC Dominion Securities Family Trust can act as a supplement to an RESP, a tax-efficient vehicle to pay for a broader category of expenses for

	RESP	RBC Dominion Securities Family Trust
Contribution limits	Lifetime limit of $50,000 per beneficiary	No contribution limits but minimum initial contribution of $50,000
Canada Education Savings Grant (CESG)	Up to $7,200 per beneficiary	None
Use of funds	RESP contributions can be returned to contributor; Income and CESG grant must be used for reasonable post-secondary education costs	Loan capital can be returned to lender; broader category on use of funds even while minor — investment income must be payable to child or spent directly on an expense that directly benefits the child
Taxation	Earnings grow tax-free; withdrawals of income and CESG are taxable to beneficiary	If monies loaned on an interest-free basis then interest and dividends attributed to lender; capital gains taxable to child which in many cases will be tax-free
Tax returns	No annual tax returns required, other than a potential T1 tax return for the beneficiary when a withdrawal is made	Annual trust tax return required, plus potential personal tax returns for beneficiaries
Annual fees	RBC Dominion Securities administration fee of $50 + GST	Annual RBC Dominion Securities administration fee ($150 or $250 + GST) and annual tax return fees

the beneficiary, regardless of age, or as a long-term savings vehicle for the beneficiary.

RBC Dominion Securities Family Trust Considerations

There are a number of important issues that the lender and trustees need to consider before establishing a RBC Dominion Securities Family Trust. Following are some of the considerations (potentially not an exhaustive list).

ADDITIONAL ADMINISTRATION

The RBC Dominion Securities Family Trust is a formal legal trust. As a result, there are a number of administrative duties that the trustee(s) will have to perform as part of their responsibilities as a trustee. See the section titled "Trustee responsibilities" for a list of some of these responsibilities.

INVESTMENT RISK OF EARNING CAPITAL GAINS

If the trust is funded with an interest-free loan (beneficiary of any age) or a gift (minor beneficiary), then to achieve income splitting with a child or grandchild beneficiary, capital gains must be earned in the trust. Earning capital gains generally involves investing in the equity markets, which will involve additional investment risk compared to earning interest and dividend income.

However, there are specific investments and investment strategies to minimize the risk and volatility of earning capital gains. Speak to your Investment Advisor for further information regarding which investments are suitable for the RBC Dominion Securities Family Trust to generate capital gains within an appropriate risk tolerance.

RENEWAL OF DEMAND PROMISSORY NOTE

In most cases you will be loaning monies to the RBC Dominion Securities Family Trust. This way you have comfort that you can receive the loan capital back in the future. The loan to the RBC Dominion Securities Family Trust is structured as a demand promissory note, meaning you should be able to call back the loan capital any time.

Depending on your province of residence, there are provincial laws that state that the lender's ability to enforce the repayment of a demand loan will expire after a period of time unless certain steps are taken. Therefore, in order to ensure that the ability to repay the loan remains enforceable for the lender at all times, the loan agreement should be renewed on a periodic basis. Typically the loan agreement should be renewed every two years but in some provinces it can be renewed every six years.

To be safe and to ensure that the ability to have the loan capital repaid to the lender always remains enforceable, we are recommending the loan agreement be renewed on an annual basis regardless of your province of residence.

LENDER LOSES RIGHT TO GROWTH

Given the settlor will not be a beneficiary of the trust, by loaning cash to the RBC Dominion Securities Family Trust the lender loses the rights to the growth and income on the loan capital. This is the case even on any income that is attributed back to the lender for tax purposes.

However, given the lender's family are the beneficiaries of the Discretionary Trust, the family beneficiary is still benefiting from the investment income earned on the loan capital. Nonetheless, family dynamics and relationships can change over time, so the lender should be aware of this before loaning a large amount of cash into the trust.

If an Age 40 Trust is used, then given there is only one beneficiary (likely a child or grandchild), then the loss of the future growth and income on the loan capital should be carefully considered.

Of course, should family relationships change in the future, the lender always has the ability to call back the loan capital for their own use and investment.

LENDER'S WILL

It is recommended the lender review their Will with their lawyer to determine if there is any clause in the Will that discusses outstanding loans at death. That is, if the lender's Will states that all loans are forgiven at death, then the beneficiaries of the RBC Dominion Securities Family Trust will ultimately benefit from the assets in the trust if the loan to the trust was not repaid prior to death. It may be your intention that the capital loaned to the RBC Dominion Securities Family Trust is to be distributed to different beneficiaries upon your death than the beneficiaries named on the RBC Dominion Securities Family Trust. If this is the case, then you will need to inform your lawyer to revise your Will accordingly.

TAX DEDUCTIBILITY OF INVESTMENT MANAGEMENT FEES

If you are paying investment management fees related to your non-registered investment account, a portion of the investment management fees may be tax deductible against your income at your marginal tax rate. If you are in the highest marginal tax bracket then the tax benefit of deducting a portion of the investment management fee can range anywhere from 39%-48% depending on your province of residence.

If investment management fees are being charged in the RBC Dominion Securities Family Trust, then a portion of the investment management fees may be similarly tax-deductible. In this case, the investment management fees would be tax-deductible against the taxable income earned in the trust. This tax deduction in the trust can help minimize the amount of taxable income that is taxed in the hands of the beneficiary and/or the amount of any taxable income (i.e. generally interest and dividends) that is attributed back to the lender, which results in less tax payable for the family. However, if there is not adequate income and realized capital gains earned in the trust in a particular year, then it is possible there may be a reduced tax benefit of deducting a portion of the investment management fees. As a result, you may want to earn some interest or dividend income in the trust which will then be offset by the investment management fees paid by the trust resulting in little or no attribution of this income back to the parent or grandparent.

ADDITIONAL FEES AND TAX RETURN PREPARATION

The RBC Dominion Securities Family Trust has been structured as a very cost-effective tax-minimization solution and the income-splitting tax savings will generally outweigh the costs. Please see the section titled "Fees" for a breakdown of the fees for the RBC Dominion Securities Family Trust.

Given the RBC Dominion Securities Family Trust is a formal legal trust, an annual T3 trust tax return will be required. Furthermore, trusts resident in Quebec will require an additional Quebec trust tax return. In addition, if income is distributed to the beneficiaries, then a personal income tax return will likely need to be completed for the beneficiaries.

Establishing an RBC Dominion Securities Family Trust

Let's go through an example of how parents Mr. X and Mrs. X can establish a RBC Dominion Securities Family Trust for their two minor children. We will assume that Mr. X has $500,000 of cash in a non-registered account in his sole name. Mr. X is in the highest tax bracket. We will also assume that each of the children are enrolled in private school with fees of $15,000 each that are not tax-deductible to the parents.

1. Mr. X (the "settlor") will set up an RBC Dominion Securities Family Trust (Discretionary) by gifting a $20 bill to Mrs. X (the "trustee") in order to "settle" or establish the trust for their two children (the "beneficiaries"). Mrs. X is also a beneficiary of the trust but not Mr. X. The $20 bill should be kept by Mrs. X with the trust agreements and should not be spent, invested or commingled with the other trust funds.

2. Mr. X (the "lender") will loan $500,000 of cash to the RBC Dominion Securities Family Trust on an interest-free basis from his sole non-registered account. If the cash was in a joint account between Mr. X and Mrs. X, but the monies in this account were originally earned by Mr. X., then the cash should first be transferred to a sole account in Mr. X's name before funding the trust. Loaning cash from a joint account to the trust could jeopardize the income-splitting benefit of the trust.

   Furthermore, it is recommended that only cash be loaned to the trust to make the loan appear as a bona-fide loan. Therefore, if Mr. X had securities that he wanted to fund the trust with, it is recommended that the securities first be sold in his account (potentially triggering capital gains to Mr. X) and then the cash sale proceeds are loaned to the trust.

3. Mrs. X will work with her RBC Dominion Securities Investment Advisor to invest the $500,000 in the trust.

4. Assume $30,000 of capital gains are realized in the trust in the first year. Mrs. X uses the $30,000 of capital gains to pay for the children's private school fees and will properly document this payment from the trust and keep proof of the expense.

5. Since the capital gains were used for expenses that directly benefit the child, for tax purposes, before December 31, Mrs. X will designate that the $30,000 capital gains are payable to the children ($15,000 to each child) of which 50% or $7,500 is

taxable to each child on their personal tax return. Assuming the children have no other income, there will be no tax on the capital gains since the $7,500 taxable capital gain is less than the child's basic personal amount for the year of about $9,000 each.

The tax savings in the first year by shifting $30,000 of capital gains from Mr. X to his two children is about $7,000 (varies by province). Over 15 years, the compounded tax savings can amount to over $200,000, depending on how much of the annual trust income is used to pay the children's expenses and how much is reinvested. Your tax savings will vary based on your investment return, amount of loan, time horizon and how much of the trust income is used to pay the child's expenses and how much is reinvested.

Trustee responsibilities

If you are a trustee for an RBC Dominion Securities Family Trust, you must take this role seriously. There are numerous legal and fiduciary responsibilities you have as a trustee, such as (not an exhaustive list):

- Make decisions in the best interests of the beneficiaries
- Operate and manage the trust in accordance with the trust deed or documents
- Ensure that trust tax returns are accurate and filed on a timely manner
- Consult with qualified tax and legal advisors if you need professional advice on matters related to the trust
- Maintain written records of all trust decisions (i.e. trustee minutes), which include distributions from the trust, evidence of using the trust income to directly pay for expenses that benefit the beneficiary, etc.
- Document to have investment income earned in the trust to be payable to the beneficiaries before December 31 of each year so that the investment income is not taxed in the trust at the top marginal tax rate but rather in the hands of the beneficiary (subject to the attribution rules)

We strongly recommend that the trustee consult with their tax and legal advisors to discuss the responsibilities of a trustee before agreeing to be a trustee for an RBC Dominion Securities Family Trust.

Fees

There are no set-up fees that RBC Dominion Securities charges for establishing an RBC Dominion Securities Family Trust. However, given we strongly recommend that you consult with your accountant and lawyer for tax and legal advice and have them review our legal agreements to ensure that it is appropriate for your situation, there will likely be professional fees incurred at the time of set up. Furthermore, there will be annual fees associated with the RBC Dominion Securities Family Trust as follows:

- Investment fees
- Tax return fees
- RBC Dominion Securities administration fee

INVESTMENT FEES

Similar to other types of accounts, investment fees charged to the trust will either be commissions on the purchase and sale of investments and/or investment management fees if a managed account program is used. It may be possible that some or all of the investment fees can be deducted against the income taxable in the trust. Commissions will reduce any taxable capital gain realized in the trust.

TAX RETURN FEES

RBC Royal Trust has agreed to prepare the T3 trust tax return for your RBC Dominion Securities Family Trust for a fee of $350 + GST per trust tax return ($450 + GST in Quebec for both the federal and Quebec trust tax returns). These fees are subject to change. Alternatively, your accountant can prepare the trust tax return.

The beneficiaries of the trust may also be required to file a personal tax return depending on the type and amount of income allocated to them from the trust, in addition to any other sources of income. Your accountant will be responsible for preparing the beneficiary's personal tax return and determining the amount of income on the T3 slip from the RBC Dominion Securities Family Trust that is attributed to the parent or grandparent, if any.

RBC DOMINION SECURITIES ADMINISTRATION FEES

The annual RBC Dominion Securities administration fee for the RBC Dominion Securities Family Trust is $250 + GST. If RBC Royal Trust is used to prepare the trust tax return, then this annual administration fee will be reduced to $150 + GST.

If you have any questions about your RBC Dominion Securities Family Trust, please contact your Investment Advisor.

For more information, please contact
your Investment Advisor.

RBC Dominion Securities

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