

Estate & Trust Insights



Wealth Management
Estate & Trust Services

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RRSP/RRIF estate planning options – and cautions

By Susan Cohen
Tax Manager, RBC Estate & Trust Services

An executor* is responsible for a multitude of duties including preparing and filing tax returns for the estate and the deceased. Among other things, income up to the date of death must be calculated and reported on the deceased's terminal T1 tax return. Income up to the date of death includes income earned up to the date of death, income deemed at death and income resulting from death. This can often generate a great deal of income/gains on the deceased's terminal return.

An executor is responsible for ensuring the taxes are prepared accurately and on a timely basis. The tax preparer looks for ways to reduce the overall tax burden of the deceased and their estate. One such strategy involves shifting the tax burden of an RRSP/RRIF from the deceased to a beneficiary in order to defer tax or take advantage of the beneficiary's lower marginal rate. However, caution must be exercised as this strategy may not be as straightforward as it first appears.

Generally, at death, the balance of an RRSP/RRIF is taxable to the deceased as income, based on its fair market value (FMV), and is reported on their terminal T1 tax return. Designating a specific beneficiary may provide the opportunity to tax the RRSP/RRIF in the hands of the beneficiary or defer the tax.

A beneficiary may be designated in the plan document or in the Will (in Quebec designations can only be made

in a Will). Often we see spouses and children named as beneficiaries of an RRSP/RRIF. Where the spouse is named as the beneficiary of the RRSP/RRIF, it may be possible to defer the tax liability until the date of death of the surviving spouse. Where a child/grandchild is named as the beneficiary of the RRSP/RRIF, as a general rule, the executor must still include the fair market value (FMV) of the plan at the date of death on the deceased's final tax return. There are, however, some exceptions to this income inclusion tax treatment.

If a child/grandchild was financially dependent on the deceased, regardless of their age, the FMV of the RRSP/RRIF on death can be taxed in the hands of either the beneficiary or the deceased. Taxing in the hands of the beneficiary often provides some tax relief when that child/grandchild has minimal income and is taxed at a lower marginal rate.

To qualify as financially dependent, the child must have a net income for the year before the death of the annuitant that's less than the basic personal exemption for that year. If the child/grandchild is a person with a disability, their net income for the year before the death must be less than the basic personal exemption plus the disability amount for that year. If these criteria are not met, the child/grandchild may nonetheless be considered financially dependent if their dependency can be demonstrated to the satisfaction of the CRA.

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Estate & Trust Professionals

Greater Toronto

Chris Burton
Regional Client Service Manager
416-955-5003

Ontario & Atlantic

Steven Newman
Regional Vice President
519-747-2781

Quebec

Carmela Guerriero
Regional Vice President
514-874-2475

Prairies

Tracey Jonasson
Regional Vice President
403-299-5255

British Columbia

Jemison Jackson
Regional Vice President
403-299-5024

If a financially dependent minor child/grandchild is designated as a beneficiary of the RRSP/RRIF, the tax can be deferred by using the funds in the plan to purchase an annuity that ends when the beneficiary reaches the age of 18. The child will receive income from the annuity, which will be spread out on a tax-deferred basis over the term of the annuity, and will pay tax on the annuity income annually. As it is likely that the child will be in a low marginal tax bracket, the overall taxes payable on the funds from the RRSP/RRIF will be minimized. Caution should however be exercised as this means the child will receive their inheritance before they reach the age of majority, and they will incur a tax liability each year. This may be contrary to the parent's/grandparent's intention.

If you name a financially dependent minor child/grandchild as the beneficiary of the estate in a Will, there may still be an opportunity for their legally appointed guardian, trustee or legal representative to defer the tax and use the proceeds to purchase an annuity by way of a joint election. If the financially dependent minor child/grandchild uses the RRSP/RRIF proceeds to purchase an annuity, the child/grandchild can claim an offsetting deduction on their tax return for the amount transferred.

If the financially dependent child/grandchild is disabled, then they may be able to take advantage of other tax

deferral options by transferring the proceeds to their own RRSP/RRIF, then claiming an offsetting deduction on their personal tax return, or transferring the funds to a Registered Disability Savings Plan (RDSP).

In situations where a financially dependent child/grandchild is named as the beneficiary of the RRSP/RRIF in the Will, the ability to utilize this strategy may be challenging if there's another provision stating the child/grandchild is not entitled to any of the money until they turn 25.

For example, assume the child is 18, financially dependent and not disabled. Using this RRSP/RRIF tax strategy, the 18-year-old would have to report the full amount of the RRSP/RRIF as their income for the year, which would generate a tax obligation (albeit lower than the tax obligation had the funds been included in the deceased's T1 terminal return). Unfortunately, due to the other provision, the 18-year-old may not be in a financial position to pay this tax as the RRSP/RRIF proceeds would not yet be payable to them.

This disconnect can be addressed by including a provision in the Will that allows for some discretion to pay tax incurred by the beneficiary. Caution: even if a provision in the Will exists and a joint election is made, the executor may not be in a position to confirm that the RRSP/RRIF was included on the beneficiary's personal T1 return

and the resulting tax liability was paid. This may result in the CRA questioning the executor in respect of the outstanding tax liability years later. If this were to occur, the beneficiary could amend their T1 return for the year and pay the tax, or the executor could amend the terminal T1 return and include the RRSP/RRIF income, which would result in tax at a higher marginal rate and any applicable interest.

One final caution: in situations where we are dealing with a beneficiary who is a minor, the executor must rely on the child's/grandchild's Guardian for Property, if any, to cooperate in making the joint election, purchasing the annuity and filing the tax returns for the minor child/grandchild. In many situations, a court order to establish this role may not be otherwise warranted, meaning certain post-mortem tax planning opportunities may have to be abandoned.

As executor we have a duty to maximize the value of the estate. This may include assessing and implementing post-mortem tax planning strategies. Caution should nonetheless be exercised before implementing any such strategies to ensure the plan is in the best interests of the beneficiary(ies), it does not conflict with the deceased's intentions and elements required to ensure income tax compliance are in place.

* In Ontario, an executor is called an estate trustee with a Will. In Quebec, an executor is called a liquidator.



When a trustee resigns but no successor trustee is appointed

By Thomas Grozinger, LL.B., C.S., TEP
Principal Trust Specialist, Professional Practice Group

What happens if the terms of a trust instrument permit a trustee to resign and provide a mechanism for appointing a replacement trustee, but following the original trustee's effective resignation, no successor trustee is appointed? Will the original trustee be discharged from the role of trustee, even though they still hold the assets of the trust? Can the original trustee still exercise the powers and discretions provided to the trustee under the terms of the trust?

These issues were examined in *In the Matter of the Representation of RBC Trustees (Guernsey) Limited and in the Matter of the Trusts (Jersey) Law 1984*,¹ a decision of the Jersey court. The case involved an employee benefit trust governed by English law.² The original trustee (referred to as the "representor" in the decision) was a Guernsey company, and the trust was administered out of Jersey.³ The company involved in the establishment of the trust was incorporated in the Isle of Man (the "Company").⁴ Clause 12 of the trust instrument involved a change of trustees and provided for the following:

"12 (a) The power to appoint new and additional trustees of this Trust shall be vested in the Company.

(b) The Company may at any time remove any Trustee and any Trustee may at any time by giving not less than 30 days' notice in writing to the Company retire from the trusts of this Trust (and so that if after such removal or retirement there shall be no continuing Trustee the Company shall subject to obtaining such consent as aforesaid at the same time as such removal is effected or forthwith appoint a new Trustee or Trustees in place of such removed or retired Trustee) PROVIDED that no Trustee shall be personally liable for acting as a Trustee after the date upon which he

*has been removed but prior to actual receipt of notice by him of such removal and he shall continue to be entitled to remuneration and the indemnity contained in this Declaration of Trust conferred on the Trustees until all trust assets have been transferred to the new or continuing Trustees."*⁵

The circumstances were such that the original trustee decided to resign from the trust and obtained a legal opinion confirming that it could unilaterally "...do so but that, at the end of the notice period, if no new trustee had been appointed, the [original trustee] would continue to hold the assets on the same trusts as existed immediately prior to the termination but the [original trustee] could not take any action as an active trustee."⁶

The original trustee then wrote the Company giving notice of its resignation (and included a reminder that the Company was to appoint a replacement trustee).⁷ Following the effective date of its resignation, the original trustee also wrote the approximately 180 employees and former employees of the Company (or any holding company or subsidiary of the Company) and family members of such employees and former employees who were defined as beneficiaries under the trust instrument, and advised them that while it had legal title to the trust assets, it had retired as trustee and could not do anything with the trust assets except transfer them to the replacement trustee.⁸ Unfortunately, the Company dissolved prior to appointing a replacement trustee, so there was no longer any party able to appoint a replacement trustee under the trust instrument.⁹ Unsurprisingly, the original trustee continued to receive requests from the beneficiaries for various actions, including updates and distributions.¹⁰

The original trustee received legal advice indicating that while it had custodial obligations, it did not have the ability to exercise any powers or discretions under the trust instrument, and to do so, it would need to be reappointed by the court.¹¹ The decision included excerpts from Lewin on Trusts (19th ed. 2014) as well as the decision of Mann J in the case of *Jasmine Trustees Limited v Wells & Hind* [2008] Ch. 194, which were proffered by legal counsel for the original trustee. The latter excerpt involved a trustee de son tort, and explained the difference between a "trustee of the settlement" and a "trustee of the property."¹²

It seems that a trustee of the settlement can be described as the relationship between a trustee and an "abstract concept" defined by, or given structure from, the trust instrument; whereas a trustee of the property can be described as the relationship between the trustee and a physical subject-matter for which the trustee has legal title. The latter does not include all the additional powers and discretions afforded the trustee of the settlement under the trust instrument. It is, arguably, merely a "bare trustee" in relation to that property, although the trustee must account to the beneficiaries and transfer the property upon demand by the replacement trustee (once one has been appointed and accepted the role).

After considering the submissions of the original trustee's legal counsel, the Court stated:

Having considered the terms of clause 12(b), counsel advised that it does indeed provide for a power to retire without the appointment of any replacement trustee. We agree. The clause itself clearly contemplates a situation in which there will be no trustee after the retirement because it

provides "... if after such removal or retirement there shall be no continuing Trustee ...". The clause then goes on to refer to the appointment by the Company of a new trustee "at the same time as such removal is effective or forthwith ...". The reference to "forthwith" can only be a reference to a time after the removal or retirement has taken effect. The clause must therefore be contemplating the possibility of a period between the retirement of the outgoing trustee and the appointment of the new trustee.

The Trust is of course governed by English law and we therefore pay particularly close attention to English counsel. We find his opinion entirely convincing both in relation to the effect of the Resignation Letter and to the position in which the representor now find [sic] itself, i.e. that it has a duty to look after and take proper care of the trust property but it no longer has any of the other powers and discretions conferred on it under the trust deed.¹³

The Court went on to appoint the original trustee as trustee of the trust as well as awarded it the costs for the application.¹⁴

What we learn from this case

This is a very interesting decision as the situation it describes can arise from time to time, where a trustee has the power to resign but, for whatever reason, a replacement trustee is not appointed to assume the role of trustee upon the effective date of the prior trustee's retirement. Assuming the terms of the trust permit such a unilateral retirement, the issue of whether the now retired trustee has the same trustee powers and discretions it had prior to retirement can arise. This case suggests that the answer, absent any terms to the contrary in the trust instrument, is that the retired trustee does not have such powers and discretions.

Prior to retirement, the trustee is a trustee of the settlement as a whole, that abstract concept that is generally described as a relationship between

a settlor, a trustee and a beneficiary. The terms of that relationship are set out in the trust instrument (where the relationship has been reduced to writing). It is those terms which give the trustee of the settlement his, her or its powers and discretions, in addition to any afforded by the law.

However, a retired trustee no longer is a trustee of the settlement as a whole. Such a trustee is only a trustee in relation to the trust property. While the decision did not refer to the concept of "bare trustee," as suggested above, this seems to be an apt description. "Trustee de son tort" may also be appropriate. In any event, such a trustee no longer can access the powers and discretions provided to the trustee of the settlement as a whole, but instead is restricted to fiduciary obligations and duties focused on having custody of the trust property. These include accounting to beneficiaries and transferring the trust property to a validly appointed replacement trustee upon the request of such trustee.

Although the case involved an English law governed trust and a Jersey court, it is submitted that the principles and result would be equally applicable to Canadian common law jurisdictions.

How can we help?

Whether because of age, health, travel interests or other reasons, you may have clients who no longer want to act as trustees of trusts that they have been administering. Absent a change of trustee provisions in the Will or trust instrument, it may be possible to appoint a replacement trustee without having to go to court if the governing law is in a province whose Trustee Act permits the non-judicial replacement of trustees. Of course, a court too can approve the appointment of a successor trustee in place of one wanting to retire from the duties of trustee.

Taking on the fiduciary obligations of a trustee can be onerous, both in terms of time and potential liabilities.

In some cases, a trust company may be an appropriate choice for a successor trustee, rather than burdening a family member or friend. RBC Wealth Management®, Estate & Trust Services has a long history of accepting successor trustee appointments for qualified trusts where there is a benefit to having a corporate trustee appointed. To facilitate the transition between a current trustee and Royal Trust Corporation of Canada/The Royal Trust Company, RBC Estate & Trust Services has developed clauses that can be provided to the trustee's lawyer to facilitate the completion of the documentation for the successor trustee appointment.

For more information on whether a trust qualifies for an RBC Estate & Trust Services successor trustee appointment, please speak with an RBC® advisor by calling us at 1-855-833-6511, or visit our website at rbc.com/estateandtrustservices

¹ [2017] JRC 135.

² *Ibid.*, at paras.3 and 18.

³ *Ibid.*, at para.4.

⁴ *Ibid.*, at para.3.

⁵ *Ibid.*, at para.5.

⁶ *Ibid.*, at para.8.

⁷ *Ibid.*, at para.9.

⁸ *Ibid.*, at paras.3, 10 and 19.

⁹ *Ibid.*, at para.11.

¹⁰ *Ibid.*, at para.12.

¹¹ *Ibid.*, at para.13.

¹² *Ibid.*, at para.15.

¹³ *Ibid.*, at paras. 17-18 (per Sir Michael Birt).

¹⁴ *Ibid.*, at para.23.

One-minute market update – Spring 2018

By RBC Global Asset Management

Economy

- The economic backdrop is quite good by post-crisis standards, with many of the macroeconomic indicators we monitor at or near cycle highs.
- Inflation is firming, but our view is that inflation is simply transitioning to more normal levels after many years of being too low, rather than shifting higher to problematic levels.
- Key risks to our outlook are the aging business cycle, rising interest rates and protectionism, but we should not ignore the potential tailwinds from structural reforms in Japan and fiscal stimulus in the U.S.
- On balance, we expect the positives to outweigh the negatives, and for the global economy to grow at its fastest pace in eight years. Our forecasts for growth and inflation are slightly above consensus.

Fixed Income

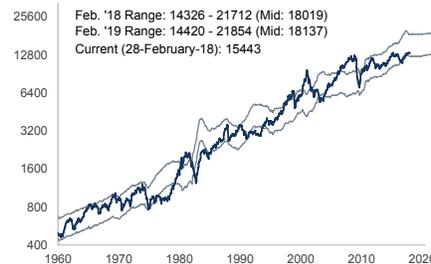
- Central banks are likely to continue dialing back monetary accommodation in an environment of improving economic growth and rising inflation.
- Our models suggest the long-term direction for bond yields is higher, but that the meaningful increase in yields over the past quarter has alleviated valuation risk in the near term.
- Although rising yields could act as a drag on fixed-income returns for many years, bonds play a critical role in a balanced portfolio serving as ballast against market volatility. We took advantage of the recent increase in yields to reduce our underweight position in fixed income by one percentage point, sourced from cash.

Equity Markets

- Stocks corrected last month after a year of strong performance and unusually low volatility, as investors were unsettled by the prospect of higher inflation and interest rates.
- Our models suggest that rising interest rates and inflation are a mild drag on equity-market valuations. That said, price-to-earnings ratios may be even more susceptible to investor confidence, which is currently high and bolstered by the outlook for double-digit growth in corporate profits.
- We remain overweight stocks because we continue to expect them to outperform bonds, but our asset mix is closer to neutral than it has been in many years given the maturation of the business and market cycles as well as demanding valuations.

CANADIAN EQUITIES – Fair value range

S&P/TSX Composite Index

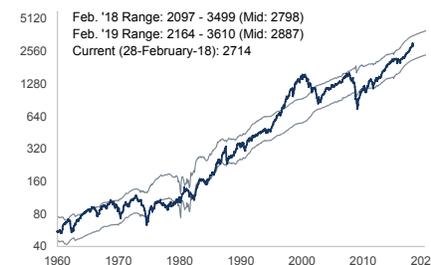


Over the three-month period ended February 28, the index decreased by -3.23%. Valuations remain at the lower fair value band.

Source: RBC GAM

U.S. EQUITIES – Fair value range

S&P 500 Index

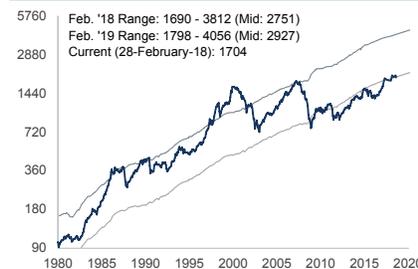


The U.S. stock market made progress over the three-month period ended February 28, rising 3.0% in local currency terms as the economic expansion continued. While valuations have increased, they still hover slightly below the midpoint of the fair value band.

Source: RBC GAM

EUROPEAN EQUITIES – Fair value range

Eurozone Datastream Index



The MSCI Europe Total Return Index (USD) was up 1.1% for the three months as of February 28, 2018 and valuations sit just below the lower limit of the fair value band.

Source: Datastream, Consensus Economics, RBC GAM

EMERGING MARKETS – Fair value range

Emerging Markets Datastream Index



Emerging-market equities extended their recovery, rising 7.1% (USD) in the three months ended February 28, 2018. With significant gains over the past year, valuations continue to move above the lower limit of the fair value band, but are still well below the midpoint.

Source: Datastream, RBC GAM

Fair value estimates are for illustrative purposes only. It is not possible to invest directly in an unmanaged index.

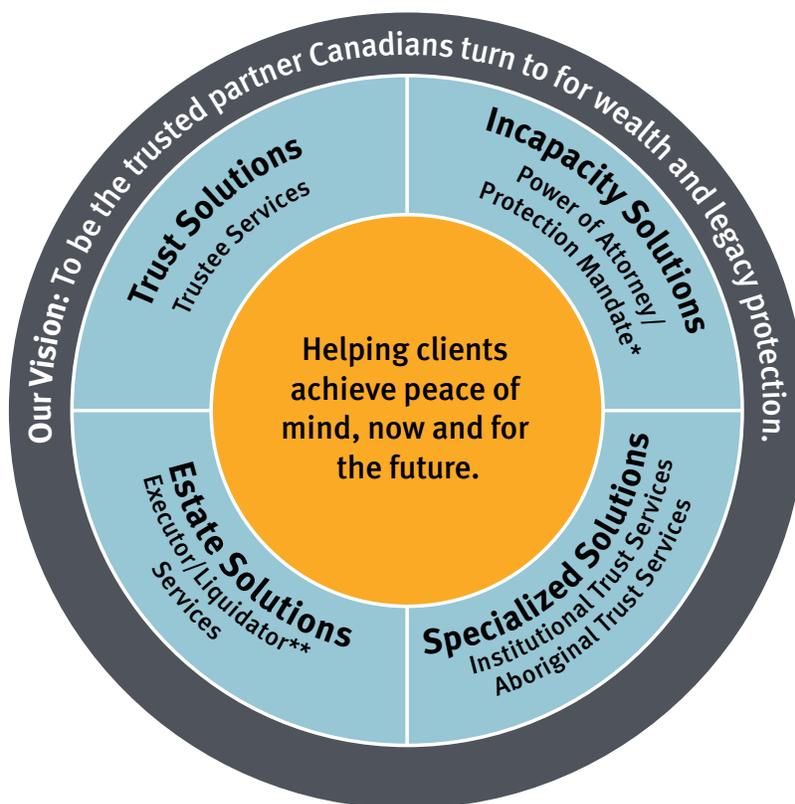
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Our Estate & Trust Services team comprises specialized and experienced professionals including legal counsel, accountants and other specialists with years of estate and trust experience. We are an exceptionally strong professional trust services firm, supported by the strength, stability and resources of RBC, one of Canada's largest banks.

What we offer our clients

- Guidance through life events and times of transition with expertise, empathy and efficiency
- Compassion and understanding of the family's experience
- Peace of mind knowing that there is stability and continuity in the long-term relationship with beneficiaries
- Assistance in the preservation, management and transfer of wealth between generations by providing solutions to implement clients' estate and trust plans
- Financial security to Canadians who require assistance in the management of their affairs as they grow older



* In Quebec, a power of attorney is referred to as a protection mandate.

** In Ontario, an executor is called an estate trustee with a Will. In Quebec, an executor is called a liquidator.



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