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 investment income 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 up to a certain amount of investment income tax-free every year (varies by province) subject to 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. Assuming your child or grandchild has no other income, they can earn up to a certain amount of investment income tax-free every year due to their basic personal tax amount.
2. Because you loan money to the Family Trust, you 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, such as private school, post-secondary education, lessons and camps.

You may be a candidate for the RBC Dominion Securities Family Trust if you have low-income children or grandchildren and 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 trustee(s) 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 their 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:

- Holding 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 (listed 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 the person 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 the trust is established	■ Created during the settlor's lifetime ■ Takes effect when the assets are transferred to 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 are 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 are 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 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 income that is actually distributed directly from the trust to the beneficiary. If the beneficiary of the RBC Dominion Securities Family Trust is a minor (as they often are), 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 trustee(s) pays 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 income that is not directly paid to a beneficiary or a third party but that the beneficiary is entitled to in the year to enforce payment of the amount. So in this case, the income can be retained in the trust and 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. For ease of recordkeeping, another option is to transfer the income that is payable but not paid to an in-trust account in the name of the beneficiary at any time in the future. The beneficiary has the right to demand payment of the amount of income that was made payable to them and is owed to them (except in the case of the Age 40 Trust as described below).

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 means at a minimum the trustee(s) will designate the realized investment income to be paid or payable to a child or grandchild beneficiary in order for the investment income to be taxed in their hands at their low tax rate.

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

Family income splitting

There are two reasons why income splitting can help you reduce your family's tax burden:

1. Canada's tax system is based on graduated tax rates. A graduated tax rate system means that the higher your taxable income, the higher your tax rate.
2. Everyone in Canada has a tax-free basic personal amount (varies by province). This means a family member (regardless of age) that has no other income can earn the following amounts every year tax-free, subject to the attribution rules:
   - Interest income tax-free up to the basic personal amount
   - Capital gains tax-free up to two times the basic personal exemption amount since only 50% of capital gains are taxable
   - Even higher amounts of Canadian public company dividend income tax-free due to the dividend tax credit

These two reasons mean that if you are a high-income earner and you can shift some of this income to low-income family members, your family can realize substantial tax savings every year (subject to the income attribution rules).

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 saving opportunity.

Attribution rules

In order to prevent abusive income splitting arrangements, the Income Tax Act (ITA) has income "attribution" rules. Basically, in certain instances, these rules will allocate taxable income back to the related family member that actually supplied the capital for investment, thus achieving no tax savings. The table (following page) summarizes the income attribution

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[2]
Gift to trust/adult child or grandchild beneficiary	No attribution	No attribution[2]
Interest-free loan to trust/adult child or grandchild beneficiary	Attribution[1]	No attribution[2]
Prescribed rate loan to trust/spouse, child or grandchild beneficiary of any age	No attribution	No attribution[2]
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.

[2] Assumes the trust is structured to avoid the subsection 75(2) 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.

As indicated in the above table, there is no attribution on any type of investment income distributed from the trust to a child or grandchildren beneficiary of any age if a prescribed rate loan is used to fund the trust.

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 will be attributed back to the person that transferred monies to the trust.

However, there are methods of structuring a trust so that the investment income is 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 investment income distributed from the trust to a child/grandchild beneficiary is not 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 and lender (the person establishing the trust and transferring the cash to the trust) should not be the sole trustee.
- The settlor and lender should not be a beneficiary.
- If a loan is made to the trust, it should be a bona-fide loan.
- The settlor and lender 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.

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

See the section titled "Establishing an RBC Dominion Securities 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 minor child/ grandchild beneficiary	Interest and dividends if beneficiary is a minor; no attribution on capital gains[1]	Interest and dividends if funded by interest-free loan; no attribution on any investment income if funded by prescribed rate loan[1]	Interest and dividends if funded by interest-free loan; no attribution on any investment income if funded by prescribed rate loan[1]
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	$475 ($575 in Quebec)	$475 ($575 in Quebec)

[1] Assumes the trust is structured to avoid the subsection 75(2) attribution.

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 Trusts permit 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 any time 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 than to the RBC Dominion Securities Formal Trust. Greater funding to the RBC Dominion Securities Family Trust may allow the trust to generate more investment income that is subject to little or no tax.

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 should 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 low, it may be beneficial to loan monies at the prescribed interest rate so there is no attribution on any type of investment income, and a more balanced, lower-risk portfolio can be structured. However, if the CRA-prescribed rate is high, then there may not be any meaningful tax savings 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 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 consider a separate Age 40 Trust per beneficiary.

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 minor child rather than let it all accumulate 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 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 minor 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 for having 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
- Nanny expenses

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 benefited the child beneficiary. Furthermore, there were some concerns that the trust income was not used to benefit the child beneficiary directly but rather used to benefit the parent or the entire household. If this is the case, the trust income could 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 trustee(s) plan on using the trust's income to pay for expenses of the beneficiary, the expenses must unequivocally benefit the beneficiary, and the trustee(s) must keep proper records. Furthermore, in some cases where an expense is tax-deductible to the parent (e.g. daycare, some nanny expenses, etc.) it may be more tax-effective for the parent to pay this expense directly rather than have 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's 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 on what expenses the funds can be spent. The RBC Dominion Securities Family Trust tends to be more flexible in terms of funding limits and when and for what expenses the funds in the trust can be used. 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 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 an RBC Dominion Securities Family Trust. Following are some of the considerations (potentially not an exhaustive list).

	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; no attribution on any investment income if monies loaned by prescribed rate loan
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 + applicable taxes	Annual RBC Dominion Securities administration fee ($150 or $250 + applicable taxes) and annual tax return fees

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.

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 knowing 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 acknowledged or renewed on a periodic basis. Typically the loan agreement should be acknowledged or 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 recommend the loan agreement be acknowledged or renewed on an annual basis, regardless of your province of residence.

LENDER LOSES RIGHT TO GROWTH

Given the settlor/lender 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 for 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 will still benefit 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 to 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 from 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%-50% 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 from 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 (generally interest and dividends) that is attributed back to the lender, which would result 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.

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 is required. Furthermore, trusts resident in Quebec 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 established an RBC Dominion Securities Family Trust for their two minor children. We will assume that Mr. X had $1,000,000 of cash in a non-registered account in his sole name and is in the highest tax bracket. We will also assume that each of the children are enrolled in private school with fees of $12,500 each or $25,000 in total that are not tax-deductible to the parents.

1. Mr. X (the "settlor") sets 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") then loans $1,000,000 cash to the RBC Dominion Securities Family Trust at the current CRA-prescribed interest rate of 1% (subject to change) 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 a bona-fide loan. Therefore, if Mr. X has securities that he wants to fund the trust with, it is recommended he first sell the securities in his account (potentially triggering capital gains to Mr. X) and then loan the cash sale proceeds to the trust.

3. Mrs. X works with her RBC Dominion Securities Investment Advisor to invest the $1,000,000 in the trust at an investment management fee of 1.5%.

4. Assume $50,000 of investment income (blend of interest, dividends and capital gains) is earned in the trust in the first year. Mrs. X could use $25,000 of the income earned to pay for the children's private school fees. She should properly document this payment from the trust and keep proof of the expense. Alternatively, Mr. X could pay for the private school fees himself, and get reimbursement from the trust for his expense. In this case, proper records must be kept.

5. Since the investment income is used for expenses that directly benefit the child, for tax purposes, before December 31, Mrs. X must designate that the $25,000 of income is payable to the children ($12,500 to each child) and taxable to each child on their personal tax return. Assuming the children have no other income, there will be very little or no tax payable due to each child's basic personal amount.

6. After paying the $25,000 private school fees, the remaining $25,000 of income earned in the trust can be used to pay the $15,000 investment management fees and $10,000 interest on the loan. It is imperative that the interest be paid on or before January 30 of the following year. If this deadline is missed, then attribution will apply in the current and future years, defeating the purpose of the family trust strategy.

The tax savings for Mr. X of shifting his investment income to his two children using the family trust strategy would be about $200,000 over 20 years (varies by province). Your tax savings will vary based on your investment return, amount of loan and time horizon.

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 in 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 the investment income earned in the trust 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 they are 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

Royal Trust has agreed to prepare the T3 trust tax return for your RBC Dominion Securities Family Trust for a fee of $475 + applicable taxes per trust tax return ($575 + applicable taxes 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 FEE

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

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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