

Alter Ego and Joint Partner Trusts

Tools to achieve estate planning goals during your lifetime



Alter ego and joint partner trusts can be useful tools for Canadians to achieve their financial and estate planning goals. Some of the typical objectives in using these trusts include: deferring taxes, contingency planning during one's lifetime, probate fee planning, maintaining estate confidentiality and protecting individuals who are vulnerable due to age, disability or spendthrift ways.

The Basics

To set up an alter ego or joint partner trust you must be a Canadian resident and at least 65. Your partner (spouse or common-law partner) does not need to meet this age requirement to be a beneficiary of your joint partner trust. However, they cannot contribute assets to the trust until they are 65 years old. Both of these trusts are known as *inter vivos* trusts — set up when the person establishing the trust, (the “settlor”), is still alive.

For an alter ego trust, the terms must ensure that during the lifetime of the settlor, the settlor is entitled to receive all the income, and no one other than the settlor can use or benefit from the trust capital. With a joint partner trust, the terms must ensure until both the settlor and partner pass away, they are entitled to receive all the income, and no one other than them can use or benefit from the trust capital.



Tax Treatment

The transfer of capital property into these trusts can typically be done on a tax-deferred basis. Tax liability is generally deferred until the death of the settlor, or with a joint partner trust the last to die of the settlor or partner. Meanwhile, all income and gains from the trust would typically continue to be taxed in the settlor's hands in the case of an alter ego trust, or settlor or partner's hands in the case of a joint partner trust.

The 21-year deemed disposition rule, which applies to other *inter vivos* trusts does not generally apply to alter ego trusts during the lifetime of the settlor, or to joint partner trusts, during the lifetime of the settlor and their partner. However, an alter ego trust may make an election in its first taxation year to have the 21-year rule apply, in which case the settlor will also not be entitled to transfer property to the trust on a tax-deferred basis.

A deemed disposition of the assets held in an alter ego trust will arise upon the settlor's death and on the death of the surviving partner with a joint partner trust. With both types of trusts, should they remain in existence, 21 years after the aforementioned deaths — and every 21 years after that — a deemed disposition is triggered, which could give rise to taxes from taxable capital gains.

One of the reasons for using this strategy, involving the election, is that these trusts cannot claim the lifetime capital gains exemption (LCGE) on death. As a result, additional planning may be required to ensure the settlor can make full use of the LCGE when transferring certain property (i.e., shares of a Qualified Small Business Corporation (QSBC)) into these trusts. One way to utilize the LCGE typically involves opting out of the previously mentioned tax-deferred rollover of this property when it is transferred into the trust.

Upon the death of the settlor of an alter ego trust, or the surviving partner in a joint partner trust, the trust will be deemed to have disposed of its assets at fair market value, and any gains will be subject to tax at the highest marginal tax rate.

Finally, while these trusts are generally tax neutral during the settlor's lifetime, foreign tax credits may be trapped inside the trust and unavailable to offset Canadian income tax payable by the settlor. Similarly, when the deemed disposition occurs on death, as mentioned above, any gains or losses in the trust cannot be used to offset gain or losses in the deceased's estate.

Benefits of Alter Ego and Joint Partner Trusts

Power of Attorney for Property Alternative: These trusts may be used as an alternative to establishing a Power of Attorney (POA) for Property. If the settlor and/or their partner become incapacitated, the trustee would continue to manage the trust assets for ongoing benefit of the named beneficiaries. This may be helpful in instances when assets such as real estate are owned in several jurisdictions.

Privacy: Unlike a Will, which becomes a public document when probated, alter ego and joint partner trusts remain private on your death. This ensures that the assets held in the trust are not subject to public scrutiny, thereby preserving the privacy of the settlor's affairs after death. Disclosure to financial institutions handling the account, provincial property registries and the Canada Revenue Agency may continue to apply.

Protection against Court Challenges: In several provinces, the partner and children of the deceased may apply to Court to vary the terms of the deceased's Will, if they feel it did not make "adequate provision" for their support and maintenance. Since the assets in these trusts do not form part of the settlor's estate, it may be difficult for them to make a claim after the settlor's death.

Reducing Probate Fees (where applicable): Upon death, alter ego and joint partner trust assets do not require an application be made for probate before they can be distributed to beneficiaries. As a result, these assets will not be subject to the estate administration process, which can be time consuming and involve costly legal fees. When an estate contains assets of significant value, the potential probate savings could be substantial and may leave more of the estate to be shared between the beneficiaries.

Potential Drawbacks of Alter Ego and Joint Partner Trusts

There are costs associated with establishing and maintaining these trusts, which will need to be factored into the decision set one up. Other considerations include:

Flexibility and Control: Once assets are transferred into the trust, the trustee(s) will assume full control of these assets. With an *inter vivos* trust, changes can only be made according to the terms of the trust document. This contrasts with a Will, which can be amended by a testator, at any point in their life, as long as he or she has the mental capacity to do so.

Charitable Donations: As a result of the deemed disposition on death, the trust may not be able to take full advantage of charitable donations.

Concluding Thoughts

When deciding whether an alter ego or joint partner trust is suitable for your estate planning needs, consider both the advantages and disadvantages relevant to your unique circumstances in addition to your personal and family priorities. Speak with your TD advisor and tax specialist to determine if an alter ego or joint partner trust is a viable tool for your estate plan.



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