Using a trust in your estate plan

By Margaret O'Sullivan | Tuesday, May 01, 2012

Trusts can be used to achieve a variety of estate, tax-planning, or wealth-management objectives. They are particularly useful in their role in family wealth preservation and management. However, there are many misconceptions about trusts and their uses. So in this series of articles, I'd like to introduce you to the concept of a trust, describe some strategies, and help you decide whether a trust might be relevant to your own financial and estate-planning situation.

What is a trust?

A trust is a type of relationship. The key element of a trust is that title to property is transferred to a person (the "trustee") who has a legal obligation to hold the property for the benefit of others (the "beneficiaries").

To establish a valid trust, the person who transfers the property must intend it be held for the benefit of other persons. The trust comes into existence when the property is transferred to the trustee. The three "certainties" or requirements, in order to establish a trust are (i) the intention to create a trust, (ii) property held on trust, and (iii) identifiable beneficiaries.

The trust is viewed as one of the great achievements of English common law because of its concept of "dual" ownership of property – the trustee has "legal" ownership, while the beneficiaries have "beneficial" ownership. Once a trust is created, the person who has contributed the property loses his or her ownership. Ownership is then held between the trustee and the beneficiaries. The trustee, who holds legal title in his or her name to the trust property, is responsible for its management, but is not entitled to benefit from it in his or her capacity as trustee. Only the beneficiaries are entitled to benefit from the trust property.

The trust agreement

A trust agreement provides how the trust property is to be held, to whom and when it is to be distributed, in what amounts, and upon which terms and conditions. The trust agreement also defines the obligations of the trustee. The trust agreement can be tailored to meet various objectives. It can be broad in the discretion it provides the trustee in distributing and managing the trust property, or it can be restrictive and provide little or no discretion but instead require the trustee to distribute the trust property according to specific instructions.

Inter vivos and testamentary trusts

A trust may be established during a settlor’s lifetime (called an “inter vivos” trust), or it may be established under a will and as a result take effect only on death in accordance with the terms provided under the will (called a “testamentary” trust).

Trusts are widely used for wealth protection and management, protecting beneficiaries with special needs, as a substitute for a will, providing for education and other expenses for children and grandchildren, and tax minimization through estate freezes and income-splitting strategies. I’ll continue to look at these in my next article.

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