Trusts and other alternatives for making financial gifts

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When making financial gifts, using a trust may help you to have a say in when and how the recipient may use the funds. This report discusses how a trust may be used to make gifts, along with some alternatives.

What is a trust?

A trust is not a legal entity but rather a relationship that separates the legal ownership of property from the beneficial use and enjoyment of that property. With a trust, rather than transferring funds directly to the recipient of a gift, you (the settlor) transfer the funds (property) to someone to hold the funds in their name (the trustee). Although you no longer own the funds after they are transferred, you set the terms of the trust. The trustee agrees to manage the money under the trust terms for the benefit of the individual (the beneficiary) who would otherwise have directly received the gift.

The critical elements for a valid trust are that the settlor intended to create a trust, and that the trust property and beneficiaries can be identified. More information on trusts is available in CIBC's reports, In trusts we trust: Tax and estate planning using inter vivos trusts and The strategic use of trusts.

Informal and formal trusts

A trust can be created even without formal legal documentation. An “informal trust” is still a trust for legal and tax purposes[1], however the trust arrangements are not documented, so it can be difficult to determine how and when the funds inside the trust are to be used or distributed. Without documentation, it may also be difficult for others to figure out if the settlor actually intended to create a trust in the first place, rather than intending to simply gift money to a third person or save money to use for a certain person, such as a child, in the future. Even if it’s understood that the settlor intended to create a trust, the beneficiaries, trust property and trust terms may not be certain.

With a formal trust, the intention to settle a trust is clear and there is a written trust agreement (the trust deed)[2] that lists the parties to the trust (settlor, trustee(s) and beneficiaries). It also details the trust’s terms, so it's clear how the trustee(s) must manage and distribute the trust’s property, as well as any other requirements.

An example of informal and formal trusts

Stella intends to give $10,000 to her son, Bruce, for his education, and asks her brother, Trevor, to manage the funds.

If Stella simply transfers the funds to Trevor, the terms may not be clear. At best, Trevor would understand Stella’s intentions and act as a trustee of an informal trust, using the funds to make payments for Bruce’s education. If Trevor did not clearly understand Stella’s intentions, he might still act as trustee and use the funds for Bruce's benefit, although perhaps not for Bruce's education. Alternatively, Trevor may even believe that Stella simply gave the funds to Trevor himself, for his own personal use, and the funds may never ultimately be used to benefit Bruce.

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1 In Québec, the concept of informal trust does not exist and trusts can only be created by contract, will or in certain cases by law.

2 A trust may also be created under a will upon the death of an individual.

Instead, Stella (the settlor) and Trevor could create a formal trust by signing a trust agreement that includes terms for how Trevor (as trustee) could manage and distribute trust funds for the benefit of Bruce (the beneficiary).[3] For example, the trust terms may allow Trevor to use the trust funds and any resultant income or gains only to pay for Bruce's postsecondary tuition, books and equipment.

When the settlor and trustee are the same person

It is possible for one individual to have multiple roles (settlor, trustee, beneficiary) in the trust relationship.[4] For example, parents often act as settlors and put funds into a trust for their children (as beneficiaries) and the parents manage the funds as trustees.

In our example, Stella might have acted as trustee (rather than Trevor) for the $10,000 to be used for Bruce's education. Stella would make a gift to Bruce at the time the funds were transferred into a trust. Stella would no longer own the funds but would be acting as trustee to manage and distribute the funds for Bruce's education. If this was an informal trust, with no documentation, it may not be clear that Stella is the trustee and that the funds are to be used by Stella solely for Bruce's education.[5]

Financial accounts that may be useful when making gifts

There are many accounts that may be used when making financial gifts. A CIBC Financial Planner or Wealth Strategist may be able to help you identify different options based on your individual investment needs.

Informal trusts

To reduce risk of unintended consequences and complications for account holders and potential beneficiaries, some financial institutions, including CIBC, no longer offer financial accounts for informal trusts.

Formal trusts

Trustees may open and use CIBC accounts for the financial activities of new or existing formal trusts. Speak to a tax advisor or lawyer regarding the formal trust solutions that are most suitable for your personal circumstances.

Registered plans for individuals

Registered plans may help build wealth and pay for expenses, while offering tax deferral or reduction and other government benefits. More information is available online about Building wealth with registered plans and a brief overview is provided below.

Registered Education Savings Plans (RESPs)

RESPs allow you to save for a child's education while deferring tax. For each student, up to $50,000 per student can be contributed and government grants and bonds may add over $7,200 to the savings. RESP funds can be used to pay for post-secondary education, and the student may pay little or no tax on withdrawals of income and government assistance. See more information online to Invest in your child's future.

First Home Savings Accounts (FHSAs)

You may wish to give funds to family members (over the age of 18) so they can save using the new FHSA. The contribution limit is $8,000 annually and up to a lifetime total limit of $40,000. Contributions within the limits are tax deductible. The full balance can be withdrawn from an FHSA tax-free within 15 years (or by age 71) to make a qualifying home purchase. You can find more information online about the First Home Savings Account.

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3 There are a number of attribution rules that can result in trust income being taxed in the settlor's hands, so a tax advisor should be consulted.

4 In Québec, the settlor or the beneficiary may be a trustee but shall act jointly with a trustee who is neither the settlor nor a beneficiary.

5 In Quebec, parents are the legal tutors to their children and, in that role, administer their children's properties. The father and mother, the parents or the tutor may accept gifts made to a minor.

Tax Fee Savings Accounts (TFSAs)

You can gift funds to family members (who are over 18) who can then use the funds to make contributions to a TFSA. The TFSA dollar limit for 2023 is $6,500 but those who've never contributed to a TFSA may contribute up to $88,000 to a TFSA in 2023, depending on their age and length of Canadian residence. The funds, and any associated income or growth, can then be withdrawn tax-free by that family member. For more information, see our TFSA report entitled Start saving today, tax-free.

Registered Disability Savings Plan (RDSPs)

Canadians eligible for the Disability Tax Credit, their parents and other eligible contributors can contribute to a an RDSP. Depending on family income, it may be possible for the plan to receive up to $90,000 in government assistance. The beneficiary will be taxed on the income, growth, and government assistance when withdrawn from the RDSP. Additional information is available online about the Registered Disability Savings Plan (RDSP).

Non-registered accounts

If you are looking to save for a family member but are not making an immediate gift of the assets, you may want to consider opening a non-registered personal account as an option. You can uniquely identify the purpose of any personal accounts that you set up using the Wood Gundy Online (WGOL) and/or Online Banking – "Account nickname" functionality.

In addition, your CIBC Advisor can include an indicator on a new or existing account, such as a child's name, which will appear on statements and can help you track different non-registered accounts established for different purposes.

CIBC offers savings solutions for youth and students with CIBC Smart™ Start accounts.

Learn more online about CIBC's offerings for bank accounts and investments, as well as solutions from CIBC Private Wealth.

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