Testamentary Trusts

A testamentary trust is a trust that is created upon your death by your Will. Income that is earned and taxed within the testamentary trust is taxed like an individual – at graduated tax rates. As such, testamentary trusts are useful if the beneficiaries of your estate are in the highest tax bracket. Trusts can be established for the beneficiaries and the income can be taxed at the lower rate of the trust.

Four your spouse

When the sole beneficiary of the testamentary trust is a spouse, subject to certain tax rules, this is called a spousal trust. This trust is settled for the benefit of the surviving spouse who is entitled to all of the income during his or her lifetime. No one but the spouse can access the trust capital. This will give the testator (deceased) the peace of mind that their spouse is taken care of after they are gone. Again, income earned by the spousal trust is taxed at graduated tax rates, which can help reduce the tax burden.
One significant advantage of a spousal trust is that there will not be a deemed disposition of assets on the death of the testator. As such, tax will be deferred until the asset is sold or when the surviving spouse dies. To ensure you benefit from this tax deferral opportunity, your will must be properly prepared to comply with specific tax laws.

For your children

A testamentary trust should be used if your beneficiaries are minor children. If you were to die and leave assets to a minor child, those assets would be held “in trust” by the courts until that child reaches age 18. At that time, your child would receive their inheritance, which may or may not be what you intended. A testamentary trust with a professionally drafted trust agreement is a highly recommended solution.

In addition, a testamentary trust may be used to protect your assets in the event that they are threatened by a beneficiary’s creditors or as a result of a marital breakdown.

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