Preparing for the new trust beneficiary reporting rules

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Trusts are an integral estate planning tool in Ontario – they can be used to avoid probate taxes and provide a variety of other benefits. Since 2018, the federal government has indicated that new reporting rules would be put into place for trusts, providing greater transparency around beneficial ownership. It appears that the new reporting rules will finally come into force later this year, potentially adding a new layer of complexity to the use of trusts in estate planning. Draft legislative proposals containing the new rules were released by the federal government in February of 2022, and can be read online.

Reporting will be required annually

To be clear, the new rules are not intended to alter the tax treatment of affected trusts; however, a T3 Trust Income Tax and Information Return will soon need to be filed annually for all trusts subject to the rules, regardless of whether the trust has tax payable or whether any portion of the trust's income has been distributed.

Additional information will also have to be provided related to the beneficial ownership and control of a trust, as noted in subsection 17(1) of the draft legislation. Each trustee, beneficiary, and settlor of the trust whose identity is known or can be ascertained with "reasonable effort" must be identified – even contingent beneficiaries – along with any other person who can exert control over trustee decisions related to the allocation of trust income or capital. If a beneficiary is not known or cannot be ascertained, such as an unborn beneficiary, the person making the return is still required to provide sufficiently detailed information to make it clear that such beneficiaries may benefit from the trust.

In addition to providing the name of each trustee, beneficiary, settlor, and other persons who can exert control over trustee decisions, further personal information about each person must also be provided, specifically each person's address, date of birth, jurisdiction of residence, and tax identification number, unless this information is subject to solicitor-client privilege.

Affected trusts

The new disclosure requirements apply to a variety of trusts used in estate planning, including express testamentary trusts, *inter vivos* trusts, trusts established as part of an estate freeze, and bare trusts. The inclusion of bare trusts is a new development – when the mandatory beneficiary reporting rules were first proposed in 2018, bare trusts were not referenced. However, subsection 15(2) of the draft legislation now expressly defines bare trusts as "an arrangement under which the trust can reasonably be considered to act as agent for all beneficiaries under the trust with respect to all dealings with all of the trust's property."

Exempted trusts

Not all trusts utilized for estate planning will be subject to the new beneficiary reporting requirements. For example, disclosure will not be required for a graduated rate estate or a qualified disability trust. Also, the reporting requirements will not apply to trusts that have been in existence for less than three months at the end of the year, trusts that qualify as registered charities, and trusts that hold certain types of assets, as long as the fair market value of those assets does not exceed $50,000 throughout the year. A full list of trusts exempted from the new reporting requirements is set out at subsection 15(2) of the draft legislation.

Adapting to the new reporting rules

Due to the new mandatory disclosure rules and the cost of hiring an accountant to prepare annual returns to comply with those rules, trusts may be less attractive for certain estate planning clients, particularly if an asset held in trust will not generate income.

For clients who still wish to use trusts as part of an estate plan, it is advisable to have the client provide the requisite personal information about each trustee, beneficiary, and settlor when the trust is created, along with contact information for each of those individuals. Once obtained, this information ought to be provided to the client's accountant to ensure that T3s related to any trust are not filed late – penalties for filing late include a fine of $2,500 or 5% of the highest fair market value of the trust property during the year, whichever is greater (see subsection 16(1) of the draft legislation).

Clients also ought to be aware that penalties may be imposed for either making, participating in, assenting to, or acquiescing in respect of a false statement included in (or omission from) a T3, even if the false statement or omission is unintentional or results from negligence. It is crucial that clients ensure the information provided to satisfy the trust beneficiary reporting rules is correct and complete.

The new reporting rules are expected to come into force before the current tax year ends, and to apply starting in 2023. During the final six months of the year, clients may want to consider winding up trusts that no longer serve their respective purposes. Depending on the complexity of a trust, it may take months to secure the necessary information that must be included on a T3. Accordingly, it would also be prudent to begin reaching out to clients who have no intention of winding up their trusts to encourage them to start the process of collecting the personal information of trustees, beneficiaries and settlors soon to be required.