

ESTATE PLANNING AND THE DISABLED BENEFICIARY

The Henson Trust Taxation



For thousands of families, estate planning is complicated when a loved one has special needs. Typically, the special needs individual requires financial or money management assistance and is receiving provincial disability benefits. Entitlement to most provincial schemes are contingent on income or capital. Therefore, should the special needs beneficiary receive their share of an inheritance outright it may place them in an awkward position.

One tool available to these families is the Henson Trust. Most provincial regulations allow individuals receiving disability payments to receive discretionary amounts from third parties. A properly drafted Henson trust provides the trustee(s) with an unfettered discretion to make such payments or to refuse to make such payments. The beneficiary has no right to the income or capital. A Henson trust can be set up on a testamentary (established by a deceased person) or inter vivos (established by a living person) basis. The trust is not recognized in all provinces but where it is it and when it is properly drafted it preserves the beneficiary's entitlement to provincial benefits while allowing the inheritance to supplement the beneficiary's lifestyle.

Before a Henson Trust the following should be considered:

(I) AGE OF THE BENEFICIARY

Provincial benefits are typically paid up to age 65, after which time the special needs beneficiary is eligible for seniors' benefits such as OAS and the Guaranteed Income Supplement. If the beneficiary is close to 65, consideration should be made as to whether a Henson trust is the most suitable option and whether it is advisable for the trust to provide that its proceeds are to be paid when the beneficiary reaches age 65.

(II) NATURE AND VALUE OF THE ESTATE ASSETS

If the estate is relatively sizable and there are few beneficiaries, consider whether the disabled beneficiary would want to discontinue receiving provincial benefits and instead be supported by his or her share of the estate. In particular:

- Is the inheritance sufficient to meet the lifelong costs associated with the beneficiary's disability, including potential future increases in costs;
- Would medication benefits or housing subsidies be affected if the inheritance is paid directly. If so, is the inheritance sufficient to cover those ongoing costs;

(III) NATURE OF THE BENEFICIARY'S DISABILITY

Even if a Henson trust is not required because the inheritance is sufficient to meet all the beneficiary's needs the beneficiary may still require the funds to be professionally managed by a trustee.

(IV) WHETHER THE BENEFICIARY WISHES TO CONTINUE TO RECEIVE PROVINCIAL BENEFITS

There are cases where the beneficiary's experience is so poor with provincial regulators they may wish to live off their inheritance and re-apply for benefits once they run out of money. When the beneficiary reapplies their bank statement may be reviewed to determine if they unreasonably spent the inheritance for the purpose of qualifying for benefits. If so the application may be denied.

(V) IS THE MAIN REASON FOR THE TRUST TO MINIMIZE TAXES?

Prior to the recent amendments to the Income Tax Act trusts were taxed at graduated tax rates and trusts created for tax splitting purposes were common. However, today unless a trust is a Qualified Disability Trust, which is only available in certain circumstance, income retained in the trust, is taxed at

the highest marginal rate so if tax savings is the predominant goal, the trust might not be the best avenue to protect the disabled beneficiary.

It is possible to avoid having the income taxed at the highest marginal rate by taking advantage of the preferred beneficiary election which provides that income can be taxed in the hands of the beneficiary even though the funds were retained in the trust. For the preferred beneficiary election to apply the following conditions must be met:

- The beneficiary of the trust is suffering from a mental or physical impairment which is severe and prolonged;
- The beneficiary must be related to the person establishing the trust, either their spouse or common-law partner or a child, stepchild, grandchild or step grandchild, great grandchild or step-great grandchild

Finally, as with any trust an understanding of the administrative and financial cost of a trust must be considered and whether that burden is worth the preservation of benefits.

Henson trusts are not recognized in all provinces and are not right for all families. However, if after considering the planning issues discussed in this article it is right for your situation they provide peace of mind for families with special need beneficiaries.

PROVINCIAL RECOGNITION OF A HENSON TRUST

Henson Trusts are not recognized in all Provinces in Canada. Below is a summary of the status of this planning tool in each Canadian jurisdiction.

Province	Recognized/ not recognized	Statutes
Alberta	Recognized	An Act to Strengthen Financial Security for Persons with Disabilities
British Columbia	Recognized	The Patient Property Act
Manitoba	Restricted. Although Henson Trusts are recognized, regulations are in place which restrict their use	The Vulnerable Personal Living with a Mental Disability Act
New Brunswick	Recognized	The Infirm Persons Act
Newfoundland and Labrador	Restricted. Any trust over \$100,000 makes the beneficiary ineligible for government support	The Advanced Health Care Directives Act The Mentally Disabled Persons' Estate Act
North West Territories and Nunavut	Not Recognized	The Guardianship and Trustee Act
Nova Scotia	Recognized	The Incompetent Persons Act
Ontario	Recognized	The Substitute Decisions Act
Prince Edward Island	Recognized	The Adult Protection Act
Quebec	Recognized	The Individual and Family Assistance Act
Saskatchewan	Recognized	The Adult Guardianship and CoDecision making Act
Yukon	Not tested	Social Assistance Act Yukon Act

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