Transferring Your Wealth to Future Generations

You've worked hard and invested wisely to accumulate enough wealth to last a lifetime and leave a legacy for your loved ones. Wealth transfer is the most mature stage of wealth management and involves sharing or transferring your wealth to your chosen beneficiaries. Wealth transfer considerations can be as simple as making cash gifts to your grandchildren or as complex as setting up sophisticated trusts as part of your estate plan.

You may not consider the full impact of a wealth transfer until you begin the process of estate planning. However, the transfer and distribution of your wealth is something that should be considered throughout your lifetime. Like most people, you'll want to minimize taxation by structuring your estate so that a greater portion of your wealth is left to your beneficiaries. Following are some wealth transfer strategies that you may want to consider for your overall wealth management plan.

Gifts or other transfers to adult children

Parents often want their children to benefit from their wealth in the present instead of waiting for an inheritance. However, your own needs, including a contingency reserve for the unexpected, should come first – for your own protection and for that of your children. Once you gift money you lose control over the funds. It's important to consider the effect your actions will have on your children's lifestyle and motivation as well as potential exposure to your child's creditors or third-party claimants, including those of an estranged spouse (now or future), or your child's heirs should they die before you do. Appropriately structured loans and trusts are suitable alternatives to a gift of money if you want to retain some degree of control over the funds and avoid these and other problems. Tax issues, including the possibility of triggering capital gains on a transfer, or potentially invoking the income tax attribution rules, should also be taken into consideration in any wealth transfer strategy. Depending on the citizenship and residency of you and your beneficiaries, or the type of property to be transferred, U.S. gift tax or U.S. estate tax may also be a consideration.

Help your children purchase a home

Parents may want to help their adult children purchase a home during the early stage of their career (when many young families have increased financial needs); however, parents may be reluctant to help if the home can become subject to a claim by the child's spouse. If a potential family law claim is a concern, a personal mortgage such as a non-interest bearing Demand Promissory Note for some portion or up to the total value of the property at the date of transfer, may be the answer. This may also prevent children from selling or refinancing the home without your consent and preserve capital in the event you need to be repaid in the future.

Funding dependents' care or support

If you're providing for the needs of an adult family member (i.e., an aging parent or a disabled child) consider establishing a trust for that person's benefit. Income from the trust can be used to pay for the care, support and expenses of the individual, and may be taxed at the beneficiary's lower tax rate.

Consider life insurance for intergenerational wealth transfer

You can leave a tax-free legacy to your grandchildren using life insurance, even if you're uninsurable. Purchase life insurance for your child and make your child the contingent owner of the policy in the event of your death; designating your grandchildren as beneficiaries. Your deposits into the life insurance plan will grow on a tax-deferred basis. As the owner, you retain control of the policy which means you can prevent assets from being removed from the policy, and changes to the beneficiary designation will require your consent. Upon your death, your child would assume policy ownership and rights – generally without tax consequences. Furthermore, the insurance policy would not be considered part of your estate, so no probate taxes would be levied on the policy. Upon your child's death, the insurance proceeds would benefit your grandchild on a tax-free basis.

Have a plan for the family cottage

Planning for the future ownership of the family cottage is important because of the emotional attachment many family members feel towards the property – and the likely increase in monetary value. You may want to consider establishing a trust in your Will to hold the property after your death and to manage the family cottage for multiple users. The trustee(s) would be empowered to make decisions about repairs and maintenance on behalf of all users, with the trust providing time for everyone to decide how they want to use and own the property in the future.

You can establish a trust during your lifetime to hold the cottage; however, doing so introduces some possible tax issues, including immediate capital gains tax consequences and potential implications to the beneficiaries' principal residence exemption. Also, the 21-year rule – which can trigger a capital gain of trust property every 21 years – will commence sooner.

Pre-planning to fund the tax liability to your estate may be necessary if you want to keep the vacation property in the family. If self-funding by you or family members is not practical, consider life insurance. The death benefit from a life insurance policy can be used to pay the tax liability and your children can pay the life insurance policy premiums.

Charitable giving

As part of your planning, consider making a final donation to the cause(s) you support and reduce the tax liability payable in the year of death. Canadian tax legislation provides significant incentives for donations of publicly-traded securities instead of cash by eliminating any associated capital gains tax on qualifying donations. There are many options if you have significant charitable intentions, including establishing a charitable foundation, a donor advised fund or an endowment fund. Insurance can also be used to achieve your charitable goals.

Consider the appropriate distribution of your estate

Your estate plan is your final opportunity to set a wealth transfer plan in motion. Remember, not all property you control passes under the terms of your Will. If appropriately documented, joint property with a right of survivorship will pass to the surviving joint owner(s) and insurance and registered plans may pass to those you designate as beneficiaries. You may want to use your estate to equalize beneficiary distributions by taking into account transfers that have already taken place. Or, you may not want to divide your estate equally among your children as some beneficiaries may have special needs or others may not be financially responsible. Consider all of these factors along with the impact your decisions may have on your family once you're gone. To avoid surprises and potential conflicts later on, share your thoughts or concerns with family members and request their input.

Business owners must be particularly concerned about estate distribution and business succession, and may want to consider the tax and other benefits of implementing an "estate freeze." If fair distribution is a concern, there are strategies to ensure that your estate is equalized for the benefit of children who are not involved in the family business.

Remember, you do not have to distribute all of your estate immediately. Trusts may be appropriate to hold an inheritance for the protection of beneficiaries from themselves or others, to provide time for beneficiaries to mature or to encourage certain behaviour.

Your BMO Nesbitt Burns Investment Advisor can help

It's important to have a plan for the eventual transfer of your assets to future generations. Your BMO Nesbitt Burns Investment Advisor is familiar with your financial circumstances and will help you identify the best opportunities for wealth transfer and the need for estate planning services. In addition, your Investment Advisor can introduce you to an estate planning or tax professional to provide advice and help you implement your plan.

All insurance products are offered through BMO Nesbitt Burns Financial Services Inc. by licensed life insurance agents, and, in Quebec, by financial security advisors.

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