

New trust reporting rules

TRUSTS

If you oversee a trust and have not been required to file T3 trust income tax and information returns with the Canada Revenue Agency (CRA) in the past, you should be aware of new federal reporting rules, which became effective in 2023.

Background

The Government of Canada has enacted new legislation requiring trustees of certain trusts to file annual T3 returns with information disclosures. The legislation will impact most Canadian-resident and deemed-resident trusts with **taxation years ending after December 30, 2023**.

Under old rules, certain trusts were exempt from filing T3 returns with the CRA. These included trusts that did not receive any income, did not dispose of assets, and did not distribute capital to beneficiaries.

Examples included:

- Bare trust arrangements;
- Trusts holding personal-use real estate assets (e.g., cottage, vacation home); and
- Trusts holding shares of a private company, where dividends were not received and the shares were not disposed of. These structures typically arose as part of estate freezes.

The new rules come amid a growing focus globally on thwarting tax evasion and are designed to boost the transparency of trusts, among other financial structures.

What is a bare trust?

The CRA defines a bare trust as a “trust arrangement under which the trustee can reasonably be considered to act as agent for all the beneficiaries under the trust with respect to all dealings with all of the trust’s property.” In other words, the trustee of a bare trust only has legal ownership of the trust’s property and has no significant powers or responsibilities other than to deal with the property under the instruction of the beneficiaries. The beneficiaries retain beneficial ownership and control of the trust’s property and continue to be subject to income taxes on such property.

This definition could capture many planning scenarios, such as parents who add their adult children as joint owners of their investment accounts for estate planning purposes, or parents who set up “in-trust-for” accounts for their minor children. Individuals who have similar types of arrangements should seek tax and legal advice to determine whether bare trusts exist in their circumstances.



What needs to be disclosed as part of the new trust reporting rules?

The new rules require annual disclosure to the CRA, through a schedule in the T3 return, of the following details pertaining to **all settlors, trustees, beneficiaries, and other persons that can exert control over a trust:**

- Name
- Address
- Date of birth (if an individual)
- Jurisdiction of residence
- Taxpayer identification number (e.g., Social Insurance Number for Canadian individuals)

Are there any exemptions from these rules?

There are certain trusts that are excluded from the new rules. Notable exclusions include:

- Graduated rate estates and qualified disability trusts
- Trusts governed by registered plans (e.g., RRSP, RESP, TFSA, FHSA)
- Trusts that have been in existence for less than three months
- Trusts that hold less than \$50,000 in assets throughout the year, but only if such assets are money, deposits, government debt obligations, and listed securities

What are the penalties for failure to comply with these rules?

Penalties for failing to file the T3 return start at **\$25 per day**, with a minimum penalty of **\$100** and a maximum penalty of **\$2,500**. Knowingly failing to file or gross negligence can result in additional penalties of **up to 5%** of the highest total fair market value of all property held by the trust in the year.

Note:

Only for the 2023 year, and only for bare trusts, the CRA will waive penalties for T3 returns that are filed late. This relief is intended to provide taxpayers with additional time to identify any bare trusts that they may have in place.

When is the first filing due date under these new rules?

The filing due date of the T3 return for a trust with a December 31, 2023 taxation year end is expected to be **April 02, 2024**.

What are some concerns that may arise as a result of these new rules?

In addition to creating additional costs to trustees to satisfy the reporting obligations and increasing audit risk from the CRA, the major concern over these new rules is privacy. For example, many *inter vivos* and testamentary trusts include a broad class of contingent beneficiaries, who may not know of the existence of the trusts and their inclusion as beneficiaries. These rules mean that such beneficiaries may gain knowledge of their potential interests in trusts, even if they may ultimately not receive anything from them.

The extension of the new rules to bare trusts adds additional complexity and uncertainty to taxpayers. Many may not even know that they have bare trusts in place, since these trusts are not usually documented in a formal manner.

Other questions that should be considered include:

- Should the trustees seek permission from the beneficiaries prior to disclosing their personal information to the CRA?
- How far do trustees need to go down the chain of beneficiaries in terms of disclosure?
- If there are parties to the trust that are residing in a foreign jurisdiction, are there foreign rules that need to be considered?

It is expected that these new rules will impact how future trusts will be structured and how parties to the trusts (i.e., settlor, trustee, beneficiaries) are selected.

How should trustees plan for these new rules?

If you are a trustee of an existing trust, it is recommended that you consider the implications of these new rules. You should consider the following action items:

- Review the deed or will that governs any trust you manage with your tax and legal advisors to determine whether the trust is subject to the new reporting requirements and if so, whether you have the information needed on all the parties to the trust. If not, you should begin gathering the information now.

- If privacy, sensitivity of information, and disclosure to beneficiaries of the trust's existence are concerns, seek tax and legal advice on whether beneficiaries can be changed or whether the trust needs to be completely collapsed and the implications of doing so.
- Consider closing existing trusts that are either dormant or no longer achieve their purposes.

Conclusion

Staying "private" will no longer be an option for the majority of trusts. It will be important for you to consider your involvement in any trusts and the impact of these new reporting rules. For more information on these rules, please refer to the CRA website on trust income tax returns.

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