

New Tax Reporting Requirements for Trusts

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Trusts are powerful instruments in tax and estate planning. Broadly speaking, a trust is a relationship between a settlor and a trustee¹ in which the trustee holds property transferred by the settlor for the benefit of beneficiaries specified by the settlor. Using this basic framework, a variety of arrangements are possible and significant planning objectives can be met. This article focuses on the tax reporting requirements for trusts, including forthcoming changes to these tax reporting requirements for trust taxation years ending on, or after December 31, 2021.

For tax purposes, a trust is considered an (individual) taxpayer which entails a number of tax filing requirements with which the trustee(s) must comply. In the 2018 Federal Budget², the government proposed to expand these tax reporting requirements. This was followed by draft legislation announced on July 27, 2018, to be effective for trust taxation years ending on, or after December 31, 2021. As most trusts have a calendar year-end for tax purposes, the new requirements will be relevant for most trustees in preparing 2021 trust income tax returns.

What are the current rules?

For taxation years ending on, or before December 30, 2021, an (inactive) trust that does not earn income or make distributions in a year is generally not required to file an annual (“T3”) return of income. Conversely, if the trust has tax payable or if it distributes all or part of its income or capital to its beneficiaries, a T3 return must be filed. Currently, trustees are not required to disclose the identities of settlors, trustees or beneficiaries on an annual basis. In cases where the trust merely holds property and has not received and/or distributed any income in the year, the trustee does not usually prepare and file a trust tax return for that particular year.

What are the new rules?

To improve the collection of beneficial ownership information, the 2018 Federal Budget and the subsequent draft legislation proposed a series of new trust reporting requirements.

These new requirements included the following:

- “Express trusts” (see below) must file a tax return for each taxation year, regardless of income or distributions to beneficiaries, subject to certain exceptions; and
- These trusts must disclose detailed information about the settlors, trustees, beneficiaries and individuals who could exert control over trustee decisions regarding the appointment of income or capital of the trust (e.g., protectors), including:
 - Name;
 - Address;
 - Date of birth;
 - Jurisdiction of residence; and
 - Taxpayer identification number (such as SIN, trust account number, business number or taxpayer identification number used in a foreign jurisdiction, as applicable).

Who is impacted by the new rules?

The new rules apply to express trusts (or for civil law purposes, any trust, other than a trust that is established by law or by judgement), subject to some exceptions³. The Canada Revenue Agency (“CRA”) considers an express trust to be “a trust created with the settlor’s express intent, usually made in writing (as opposed to a resulting or constructive trust, or certain trusts deemed to arise under the provision of a statute).”

What are the penalties for failure to comply?

The penalties for non-compliance can be significant.

Failure to file the return or file the required disclosures on a timely basis could result in a penalty of \$25 per day (minimum \$100), up to a maximum of \$2,500 per year. However, more punitive penalties may apply in some circumstances, equal to the greater of:

- \$2,500; and
- Five per cent of the highest value at any time in the year of all property held by the trust at that time.

These more serious penalties apply to any person or partnership who:

- Fails to comply with a demand to file a trust tax return; or
- Knowingly or under circumstances amounting to gross negligence:
 - Makes or acquiesces in the making of a false statement or omission in the trust tax return; or
 - Fails to file a trust tax return.

Seek advice

The new trust reporting requirements greatly expand the number of trusts subject to annual tax filing requirements as well as the amount of information trustees are required to collect and disclose each year. Furthermore, trustees are exposed to potentially severe penalties if they fail to comply with the new reporting requirements. As such, it is recommended that the trustees of any trust contact their tax and/or legal advisors to confirm if the new rules will apply to them and, if so, begin collecting the necessary identification information immediately to ensure compliance for 2021 and subsequent taxation years. It is further recommended that persons considering the establishment of a trust give careful thought to the person(s) being appointed as trustee(s). Appointing a corporate trustee, such as BMO Trust Company, can provide considerable peace of mind given the ever evolving responsibilities.

For more information, speak with your BMO financial professional.



¹ Or a patrimony by appropriation, autonomous and distinct under the Civil Code of Quebec.

² The Quebec government has announced that its tax legislation and regulations will be amended to incorporate the changes made to the Federal legislation and regulations relating to trusts, in accordance with their general principles, subject to certain exceptions (such as the applicable penalties).

³ Exceptions to the new reporting requirements include the following types of trusts:

- Mutual fund trusts, segregated funds and master trusts;
- Trusts governed by registered plans (i.e., deferred profit-sharing plans, pooled registered pension plans, Registered Disability Savings Plans, Registered Education Savings Plans, registered pension plans, Registered Retirement Income Funds, Registered Retirement Savings Plans, registered supplementary unemployment benefit plans and Tax-Free Savings Accounts);
- Lawyers' general trust accounts;
- Graduated rate estates and qualified disability trusts;
- Trusts that qualify as non-profit organizations or registered charities;
- Trusts that have been in existence for less than three months (at the end of the year);
- Trusts that hold less than \$50,000 in assets throughout the taxation year (provided that their holdings are confined to deposits, government debt obligations and listed securities); and
- Certain other specified trusts.

The trust reporting and disclosure obligations contained in this publication may or may not apply to your situation. As such, we recommend that you consult with your independent tax and legal professionals to determine the annual reporting obligations applicable to your situation and to ensure proper documentation.

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