



Snapshots™

PARENTHOOD: GIFTING

HOW TO GIVE MONEY TO GRANDCHILDREN

Giving money and/or gifts to grandchildren is something many grandparents look forward to and enjoy doing. In most instances, the amount of money or the size of gift is relatively modest and can be deposited into a savings or investment account with little or no fuss. But if the gift is more substantial or if it is to change hands long into the future, complexities can arise. The following provides you with a range of considerations to think about when transferring wealth to grandchildren.

When will they be gifting?

The first factor to consider is when will the transfer take place – now, in the future, or both. If you want to gift cash or other property during your lifetime, keep the potential tax consequences in mind. If capital property (e.g., securities, a cottage) is gifted, you will have been deemed to have disposed of the asset at fair market value and must pay tax on any gain.

Also take into account income attribution rules. These rules state that income (but not capital gains) on property transferred or loaned, directly or indirectly, to a related minor child (e.g., grandchildren, nieces and nephews) is attributed back to the transferor or lender. These rules can be punitive and often tilt the balance in favour of deferred giving.

For example, say you transfer \$50,000 in cash and shares with a market value of \$50,000 and an adjusted cost base of \$30,000 to your grandchild on their 15th birthday. You would report a capital gain of \$20,000 on the transfer of shares. The grandchild would report any future gain, but any dividend income from the shares and any income earned on the \$50,000 would be attributed back to you. You must report the dividend and other income as long as the grandchild is under the age of 18 at the end of the year. Income attribution would not apply if the transfer was made to an adult grandchild.

Age of the grandchildren

Another factor that will impact the appropriate giving strategy is the current age and stage of life of the grandchild, including whether the gift should be made outright or via trust. For instance, a grandchild who is an infant when the will is prepared (and should probably receive the gift in a trust) may be an adult when their grandparents pass away and can accept the gift outright. Still, it's advisable to prepare a will that works now, basing it on the current age of the grandchild. You can update it later.

Number of grandchildren

Not only should you consider the current number of grandchildren, you should also think about future grandchildren. And, given the prevalence of blended families, whether any potential step-grandchildren are to benefit as well. If the number of grandchildren is unlikely to grow, you may wish to provide a set cash legacy in your will.

Providing a benefit to grandchildren via a will is the preferred approach for many grandparents as doing so has many benefits. That's because there are fewer uncertainties since the clients may not currently know what they can comfortably afford to give away. Also, the income attribution rules may apply.

But exercise caution if additional grandchildren are likely; otherwise additional bequests could drain your estate. For instance, say your will states that you'll provide \$25,000 to each grandchild. There might only be two grandchildren when you create the will, but by the time of your passing, there could be six. That's an additional \$100,000.

Instead, the safest course might be to provide a lump sum or share of the residue that's divided among all grandchildren. Or you could provide separate pots for each family; \$100,000 to be divided among the children of your son and \$100,000 to be divided among the children of your daughter.

Needless to say, this may produce uneven benefits between the cousins. Whenever beneficiaries are referenced in terms of relationship to the testator (grandchild, niece, nephew, etc.) as opposed to by name, careful drafting is essential to clarify who is to be included.

Trust or no trust?

The ages of the grandchildren and the amounts involved will, in large part, drive this decision. For instance, if they're minors at the time of your death, a trust is required. In the case of modest legacies (less than \$25,000 for instance) a clause empowering the executor to pay the fund to the parents of the grandchild should suffice. But if the inheritance is more substantial, a trust or trusts are preferred for both younger and more mature grandchildren.

Trusts allow a testator to establish how and when the money is used. Trusts can be fixed (all income and/or capital is paid at a fixed time or times) or discretionary (funds are only paid for certain purposes, or under certain circumstances). Testamentary gifting is also tax-efficient and ensures the benefit is received when most needed. It also offers great flexibility. And as long as the grandparents remain mentally capable, they'll be able to alter the plan if circumstances change.

Trusts can also be used to provide incentives. For instance, the trust could be structured so that funds are paid only if and when the grandchild attends or completes a college or university. Whenever conditions, like age and/or achieving a particular goal are attached to a gift, it's crucial that the will state what happens to the funds if the conditions aren't met. Otherwise, that situation could result in partial intestacy or a legal battle.

How can you be fair?

Whether gifts are provided outright or via trust, you need to decide whether you want to provide the same benefit to each grandchild or a customized benefit that takes into account each grandchild's circumstances.

What about your children?

Do you want to skip over your children or do you plan on benefitting both generations? And if you exclude your children do you plan on seeking input or buy-in from their children? Communicating such matters during the planning stage will help avoid or minimize conflict and misunderstanding down the road.

You should be aware that, in certain, situations bypassing a child may not be a viable option. In all provinces, parents have a legal obligation to provide for dependent children. In BC, testators run the risk that even a non-dependent child could challenge the will.

Should the grandchildren be contingent beneficiaries?

Even if grandchildren aren't listed as primary beneficiaries, it's common for grandchildren to be mentioned in wills as contingent beneficiaries.

This means that the children are the primary beneficiaries, but if the children predecease their parents (the testators) then their share will be divided between the grandchildren. Often, contingent clauses are inserted as afterthoughts and do nothing more than substitute the grandchildren for their parents. So, ensure the document is well-drafted. The factors and variables set out in this article (fixed or discretionary; age thresholds) should be reflected in the contingent fit clause as well.

Other options

In addition to the methods of gifting to grandchildren discussed here, there are many other options. You can use insurance (annuities and life insurance), you can invest in a grandchild's registered education savings plan and you can even designate a grandchild as a beneficiary on retirement assets. Just as there are a wide array of options for gifting, there are a wide array of possible tax implications. Take the time to find out which works best for you.

Adapted from an article by Elaine Blades, Director Fiduciary Services, Scotia Private Client Group

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