Leaving life insurance proceeds to a minor beneficiary or trust

You have options when leaving life insurance proceeds to a minor beneficiary or trust. Your chosen method to create the trust depends on the considerations relevant to your situation. This article provides a brief review of the methods available to you and the considerations to keep in mind. As trusts are complex, consult a lawyer and accountant before acting on any information contained in this article. **This article is not applicable to Quebec residents.**[1]

Methods of creating the trust

Life insurance proceeds can form a large part of your estate. In some cases, you may not want the beneficiary to receive the proceeds outright. For example, if the beneficiary is a minor. Or you may wish to delay the distribution to a beneficiary of any age. There are three methods available to create a trust when leaving money to a minor or trust.[2]

Name a trustee on insurance application or beneficiary designation form

Name the estate as beneficiary with trust terms in your will

Life insurance trust

Which option you choose depends on the following considerations.

Considerations when creating a trust for minors

Not everyone has the same concerns when leaving money for a minor or trust. Although not an exhaustive list, some of the main considerations include:

Flexibility/control
When you create a trust, the trustee needs instructions on how to manage the money. This can include instructions about:

- access to income, capital, or both;
- the age at which a beneficiary receives the money (age of majority[3] or later);
- investing the money;
- purposes or use of the money (e.g. education, maintenance, etc.);
- contingent or alternate beneficiaries and income splitting opportunities.

Without proper instructions, trustees must rely on provincial trustee laws and common law established over time. These can be difficult and costly to manage and require legal advice.[4]

Ease of set up/cost effectiveness
Ease of set up and being cost effective is a major concern for many. However, being easy to set up does not replace prudent and sound estate planning. This consideration requires balance against other considerations.

For smaller amounts, formal trust terms may not be cost-effective. For larger amounts, a formal trust is more appropriate.

Privacy/confidentiality

You may want to ensure the details of the trust are private and confidential (e.g. amount of money, distribution times, etc.). This may include keeping it confidential from the public probate process or from other family members.

Probate is a public process used to prove your will under provincial laws. Other family members entitled to estate assets may also see a copy of the will. In these cases, you lose privacy. However, not all wills need probate and not all assets pass through the estate for probate purposes.[5]

Creditor protection (policy owner)

During lifetime. Provincial laws across Canada exempt certain policies from seizure by a policy owner's creditors during their lifetime. This creditor protection is available where the beneficiary is an irrevocable beneficiary. It is also available where the named beneficiary is from the "protected class" prescribed by provincial law. The protected class generally includes spouses, children, grandchildren and parents.[6]

At death. Creditor protection for the policy owner also includes keeping the money outside of your estate for probate purposes. Naming a beneficiary other than your estate helps achieve this goal. It may protect the life insurance proceeds from claims by estate creditors.

It is important to note provincial creditor protection may not apply in all situations.

Creditor protection (policy beneficiary)

Money held in trust for a beneficiary may be exempt from seizure by the beneficiary's creditors. This can include general creditors and marital claims depending on your provincial laws. The protection applies while the money remains in the trust. Once a beneficiary receives the money, it may be subject to claims.

The extent of creditor protection for the beneficiary depends on the terms of the trust and provincial laws.

Reduction of probate fees

When life insurance proceeds flow through the estate for probate purposes, probate fees will apply.[7] You can reduce probate fees by having less assets flow through the estate thereby leaving more to your beneficiaries.

Choosing your preferred method

Choosing your preferred method depends on your goals and objectives. Consider each of the three methods against your concerns to determine which method is right for you. Then, consult your lawyer to finalize and implement your choice.

Trustee on insurance application or beneficiary designation form

This option is generally only available for minor beneficiaries. In this case, life insurance proceeds will flow to the trust and not your estate. The trustee manages the money in line with the terms set out on the form or provincial trustee laws. This creates a bare trust with limited ability to make payments to the minor. The trustee must pay the proceeds to the beneficiary at the age of majority.

Consideration	Result
Flexibility/control	You are limited to standard wording instructions used on insurance forms. Further, the beneficiary is entitled to receive the money at the age of majority. Most standard forms contain limited instructions or may have no instructions at all. Without instructions, the trustee must rely on provincial trustee laws to guide them which requires legal advice.[4]
Ease of set up/cost effectiveness	You simply name a trustee on the standard form.
Privacy/confidentiality	You name a beneficiary directly on the form. Therefore, life insurance proceeds do not form part of your estate or the public probate process.
Creditor protection (policy owner)	<u>During lifetime</u>. If you name a protected class beneficiary, the policy is exempt from seizure by creditors under provincial insurance laws. <u>At death</u>. Life insurance proceeds do not form part of your estate. Therefore, proceeds are generally not available to creditors of the estate.
Creditor protection (policy beneficiary)	Creditor protection is potentially available while money is in the trust. Once the minor reaches the age of majority, money will form part of their assets subject to creditor claims.
Reduction of probate fees	Life insurance proceeds pass outside of the estate to the beneficiary. Therefore, the proceeds are not subject to probate.

This option is the easiest to set up but may result in the least flexibility and control.

Name the estate as beneficiary with trust terms in your will

This option is available for beneficiaries of any age. In this case, life insurance proceeds flow to your estate. Your executor manages the money in line with the terms set out in your will.[8]

Consideration	Result
Flexibility/control	You can provide any form of instruction for the trustee to manage the money. This includes distribution over time, maintaining funds past the age of majority, limiting distributions to specific purposes, and more.
Ease of set up/cost effectiveness	You need to have a will drafted with trust terms included. This may increase your cost, although potentially only a nominal amount.
Privacy/confidentiality	Your will and its contents may be subject to the public probate process. Other beneficiaries of the estate may also be privy to the trust, its beneficiaries, and amounts.
Creditor protection (policy owner)	<u>During lifetime</u>. The beneficiary is the estate. Therefore, there is no protected class beneficiary named. The policy may be subject to seizure and creditor claims during your lifetime. <u>At death</u>. Money flows to the estate. Therefore, money may be subject to claims by the creditors of the estate.
Creditor protection (policy beneficiary)	You can draft the trust to continue past the age of majority for the beneficiary. This extends potential protection from their creditors.
Reduction of probate fees	Life insurance proceeds flow to the estate and may be subject to probate fees, where applicable.

This option can provide flexibility and control but results in a potential loss of privacy and creditor protection.

Life insurance trust

This option is also available for beneficiaries of any age. In this case, the life insurance proceeds flow to the trust. Your trustee manages the money in line with the terms of the trust.

Consideration	Result
Flexibility/control	You can provide any form of instruction for the trustee to manage the money. This includes distribution over time, maintaining funds past the age of majority, limiting distributions to specific purposes, and more.
Ease of set up/cost effectiveness	You need to have a life insurance trust drafted (either in your will or in a separate trust deed). This may increase your cost. Costs vary depending on legal fees and the terms you choose.
Privacy/confidentiality	If contained in the will, your will and its contents may be subject to the public probate process. Other beneficiaries of the estate may also be privy to the trust, its beneficiaries, and amounts. If contained in a separate trust deed, the trust document is generally not subject to the public probate process. Only the trustee and beneficiaries are privy to the information.
Creditor protection (policy owner)	During lifetime. It is currently unknown whether provincial creditor protection extends to life insurance trusts. If the beneficiaries of the trust are from the protected class, there **may** be creditor protection during your lifetime. Legal advice is necessary to find out if the designation meets creditor protection laws in your province.[9] At death. If drafted properly, the life insurance proceeds flow outside of your estate for probate purposes. In these cases, money would not be available to creditors of the estate.
Creditor protection (policy beneficiary)	You can draft the trust to continue past the age of majority for the beneficiary. This extends potential protection from their creditors.
Reduction of probate fees	If drafted properly, life insurance proceeds do not flow through the estate for probate purposes. This is true even where the will includes the trust terms.

This option provides flexibility and control along with potential privacy but may require additional cost to set up.

If you wish to include a life insurance trust in your estate plan, meet with your legal advisor to draft the trust deed or appropriate clauses in your will. Your advisor can work with you and your legal advisors to place the necessary documents on file to help meet your wishes.

A note about beneficiary designations

A note of caution when creating trusts using life insurance. Provincial laws across Canada provide several methods for drafting a beneficiary designation. In general, you can make a designation (sometimes called a declaration):

- on a standard insurance form (insurance application or beneficiary designation form);
- in a will; or
- by separate declaration in writing in compliance with provincial laws.

It is also important to note that a new designation revokes a previous designation and takes precedence. For example, a designation in your will is effective upon execution. If you subsequently make a designation in a standard form, it overrides the designation in the will. This thwarts the planning you intended.

Therefore, creating a trust requires careful attention and coordination among you, your lawyer and your advisor. You don't want to undo proper planning with a new beneficiary designation. In some cases, your lawyer may instruct you not to sign any standard forms. Instead, they may prefer you place a copy of the designation or trust on file with your insurance company.

Summary

The method used to create a trust for your beneficiary depends on your situation. There is no one-size fits all as it depends on you and your goals and objectives. Regardless of your choice, we recommend coordination among you, your lawyer and your financial advisor in order to help meet your wishes.

Published and revised by: Estate & Financial Planning Services
Last revised: January 2023

---

[1] This article is intended to be used solely by residents of the common law provinces and territories of Canada. Quebec is governed by a civil law framework, which carries different outcomes on this subject matter. This includes the options available, creditor protection and probate, to name a few. A review of the available options in Quebec can be found in our article titled "Life insurance proceeds for the benefit of minors (Quebec version)".

[2] This article assumes you are the policy owner and the life insured and you wish to name a trustee to hold insurance proceeds on behalf of the intended beneficiary rather than a direct gift to them, whether a minor or not. A direct gift to a minor is generally not recommended.

[3] Age of majority is 18 in Alberta, Manitoba, Ontario, PEI, Quebec and Saskatchewan. It is 19 in all other provinces and territories.

[4] Provincial trustee laws vary across Canada. They range from allowing (1) no access to income or capital without Court approval; (2) access to income only and capital only with Court approval; (3) access to income and up to 50% of capital without Court approval. Common law established over time provides further guidance and restrictions, but requires legal advice.

[5] Probate is usually required where a third party requires verification of the will. This includes situations where financial institutions hold the deceased's money or where real property registries are involved. Assets that pass outside of the estate directly to the recipient include jointly held assets with right of survivorship or assets that allow beneficiary designations.

[6] All common law provinces and territories (i.e. not Quebec) include the spouse, child, grandchild and parent of the life insured as a "protected class". British Columbia, Alberta, Saskatchewan, Manitoba, Ontario, Northwest Territories and Nova Scotia extend this to common law partners.

[7] Probate fees vary across Canada and range from a flat amount of $35 up to 1.695% of the value of assets flowing through the estate. As of July 1, 2020 there are no probate fees in Manitoba.

[8] This method requires you to have a properly drafted will prior to your death with the requisite trust provisions. If you do not have a will, there are no trust terms provided and your Court appointed personal representative will administer the money in accordance with provincial intestate and trustee laws.

[9] There is no reported case law to confirm whether provincial creditor protection extends to life insurance trusts with beneficiaries from the protected class. Careful wording is needed for the beneficiary designation itself to meet provincial laws and will need to be reviewed with your legal advisors to determine if provincial creditor protection is available for your situation.