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WealthWisdom

ESTATE PLANNING & WEALTH:
Worried About Beneficiaries?

Ottawa & Kanata Branch

750-45 O'Connor St, Ottawa ON K1P 1

400-450 March Rd, Kanata ON K2K 3K2

www.raymondjames.ca/ottawacorpo

In working with clients, many express concerns about their beneficiaries' ability to manage an inheritance. The old adage, "shirtsleeves to shirtsleeves in three generations," still rings true, suggesting that the wealth accumulated by one generation is often lost by the third. The first generation works hard to build wealth, the second generation benefits and maintains it and the third, having not experienced the hardships of wealth creation, often loses it.

Are you worried about your beneficiaries? As you refine your estate plan, here are three considerations that may help to support the transfer of wealth — each with benefits and disadvantages:

1. Set up a testamentary trust

A testamentary trust takes effect upon death and can be managed by a trustee to distribute inheritance over time according to a predetermined payment schedule. It can specify terms to encourage certain types of behaviour, such as tying income to employment — e.g., "monthly income will increase if the beneficiary maintains a job for x years." Or, it can put constraints on inheritance payments — e.g., "capital won't be distributed until the beneficiary completes their education." There are legal limits to the types of conditions, depending on your particular situation, so consult a qualified trust and estate lawyer. A testamentary trust may be a valuable tool for heirs who lack financial maturity, live with a disability or are financially vulnerable, as it can help preserve wealth or promote responsible behaviours.

Disadvantages

With some exceptions (e.g., a qualified disability trust or graduated rate estate), income earned in the trust is generally subject to the highest marginal income tax rate. However, if income is paid (or payable) to a beneficiary in the year it is earned, it can be deducted from the income of the trust and become taxable in the hands of the beneficiary. There may be associated costs, including initial setup, administration and management. The appointed trustee will have ongoing administrative duties, including record keeping and filing tax returns, which can be burdensome. Hiring a professional trustee is an option but would incur costs; yet, consider that any trustee is entitled to claim compensation.

How Raymond James Ottawa Can Help

If you need support in exploring strategies for teaching financial responsibility, building savings or planning for a financial future, please call the office.

45 O' Connor St Ste 750 Ottawa, ON K1P 1A4
T: 613.369.4600
F: 613.369.4699

2. Direct a portion of inheritance to a life annuity

A life annuity is an insurance product that pays a guaranteed income for life to the individual, the "annuitant," similar to a pension. The annuitant receives regular payments over their lifetime, offering long-term financial security and protection against outliving their resources.

Disadvantages

Allocating funds to an annuity limits income flexibility and eliminates the potential for investment growth. The capital used to purchase the annuity is locked in, and the annuity pays a fixed amount, which may not keep pace with inflation, though an inflation-protected life annuity may be a consideration. As well, once the annuitant passes away, payments typically cease, restricting future legacy planning unless a guarantee period has been included in the annuity. Unlike a testamentary trust, a life annuity doesn't provide the ability to influence the annuitant's financial decisions or behaviour over time.

3. Introduce your beneficiary to us, your trusted advisors

We are here to build a relationship with your beneficiaries, which may be beneficial if there is a need to foster financial literacy or build responsibility. By getting to know us early, your beneficiaries may better learn and understand your own financial values. We can also provide support for family meetings, to discuss the intentions behind your estate plan or help to direct financial planning, estate distribution and the responsibilities that come with inheritance.

Disadvantages

The success of any beneficiary depends heavily on their willingness to engage and learn. There is no guarantee that the beneficiary will adhere to the financial guidance provided. However, establishing this relationship may be highly beneficial as it can supplement the structured control of a trust or annuity.

How We at Raymond James Can Help Guide the Next Generation to Financial Success

- Supporting family meetings to help transition your legacy
- Providing educational resources for the next generation on budgeting, saving, investing or financial planning
- Guiding the next generation to plan for financial milestones such as buying a home or funding a child's future education
- Introducing personalized financial planning for younger clients to help save and invest using RRSPs, TFSAs, FHSAs and other tools
- Planning for a successful wealth transfer to the next generation using tax-efficient strategies and tools like trusts or insurance for estate preservation, equalization and liquidity

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