RDSPs Versus Trusts: Scenario # 1 (Nicholas)

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While its great to say that the general rule is that you should look at using both a trust and an RDSP, whether you have a thousand or a hundred thousand dollars, you do need to make a decision. Based on questions that we receive, we've decided to do a series that will help you in your decision-making.

Scenario # 1: Nicholas

Nicholas, or Nick as his friends call him, just turned 51 in February. Nick lives in British Columbia, receives BC Disability Benefits and has qualified for the Disability Tax Credit. Nick has a mental illness; he has cycles of depression which are fairly well managed now but which have prevented him from working most of his life. As a result he has no assets and requires regular assistance in managing his nutrition, his household and his health. Fortunately, he has a couple of sisters that live nearby and assist him with his affairs.

Nick's father is elderly, has some savings and recently gave each of his sisters a financial gift of $10,000. He would like to do the same with Nick but isn't sure whether he should give him the cash, put it in a trust or use it to set up a Registered Disability Savings Plan. His question is, "What should he do?"

If Nick's father gives him $10,000 in cash, he will immediately exceed the asset limit for BC Disability Benefits, which is $3,000 and will become ineligible for benefits until his assets drop below $3,000 again.

Our first thought would be to put the $10,000 in a trust to allow him to maintain his eligibility for BC Disability Benefits and to make annual payments from the trust to the RDSP to maximize the federal government contributions. Unfortunately, he is 51 and no longer qualifies for the Canada Disability Savings Grant.

A trust is still an option. He could set the $10,000 up in a discretionary trust. Nick's sisters could act as trustees and he could choose a "residual" beneficiary to receive the remainder of the asset should anything happen to Nick. There are, however, some downsides to using a trust. He will have to pay to set up the trust and this will reduce the money that Nick will get. In addition, the amount is too small to get a trust company to manage the trust so his sister's would have to administer the trust and, aside with the inconvenience of managing a trust, generally there are fewer investment options when managing a trust oneself. Finally, there are some limitations on what the funds can be spent on without affecting Nick's BC Disability Benefits.

Because he qualifies for the Disability Tax Credit and is younger than 60, Nick can set up an RDSP. Nick has written a Representation Agreement (like a Power of Attorney, but only available in BC) designating one of his sisters as his Financial Representative. As a result, either Nick or his sister can be the holder of his RDSP. With some financial institutions they could be joint holders of the RDSP. If Nick was prone to poor management of his finances, this would carry some risk as he would have access to his RDSP but he has shown reasonable good judgement and his family are not concerned about this issue.

All of the financial institutions offering RDSPs offer a range of investment options for RDSPs so Nick should get a reasonable return on the investment of the $10,000 and he'll be able to stretch it a bit further this way.

Nick will not be receiving any federal government contributions, because he is already 51 so his personal contributions will exceed federal government contributions. This means he can begin to make withdrawals from his RDSP at any time without any holdback penalties and without the restrictions of the LDAP formula that exist when the federal government contributions exceed personal contributions. The only regulations with respect to withdrawals will be that he must begin to withdraw funds when he turns 60 and he must withdraw the minimum as determined by the LDAP formula at that time.

Furthermore, withdrawals from the RDSP can be spent on anything; unlike the constraints on withdrawals from trusts, BC Disability Benefits places no constraints on withdrawals from RDSPs.

Finally, Nick has a Will, so his RDSP would be distributed through his Will if he were to pass away before it was all spent.

In this situation, it seems like an RDSP makes the most sense for Nick.

PS Feel free to forward your situation. We'll definitely answer your questions and we may blog it (anonymously!)

RDSP resource centre

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