



Market Activity

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Income Trusts

S&P/TSX Index Watch

Income Trust	164.42	+1.18
Energy Trust	192.14	0.00
REIT	129.37	-0.51

Distribution Report

Enter the income trust symbol e.g. YLO.UN

Related Articles

A place where we summarized the most recent and relevant articles from various channels regarding Canadian income trusts. [Enter here](#)

Trust Ratings

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Trust Selector

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 - ▶ [Resource Trusts](#)
 - ▶ [Utility Trusts](#)
- [All Income Deposit Securities \(IDS\)](#)
- [All Closed-end Investment Trusts](#)

Suggested Readings

- [DBRS: Approach to Rating Income Funds and Stability Ratings](#)
- [DBRS: Personal Liability of Unit Holders of an Income](#)

Income Trust

The variety of businesses upon which income trusts have been created is broad, both in the nature of the underlying industry and assets and in geographic location. The income trust universe is, in general, comprised of the following four categories:

- [Business Trusts](#)
- [REITs](#)
- [Resource Trusts](#)
- [Utility Trusts](#)

Income trusts, also called income funds, are trusts generally structured to own debt and equity of an underlying entity which carries on an active business, a royalty in revenues generated by the assets thereof. The income trust structure was developed to facilitate distributions to investors on a tax-efficient basis. An income trust can generally avoid paying ordinary income tax by paying (or making payable) all of its taxable income (including net realized capital gains) to unitholders, thus avoiding a layer of taxation associated with corporate entities. The income trust structure is typically adopted by businesses that require a limited amount of capital in maintaining their property, plant and equipment and that generate stable cash flows. The projected life of distributions and the sustainability of distribution levels tend to vary with the nature of the business underlying the income trust.

Earnings from the business are distributed to investors each month or quarter with yield ranging anything from 6 to 20 per cent a year. (The higher the yield the riskier the trust.)

The appeal of income trusts

Income trusts have enjoyed surging popularity in recent years because of their potential to deliver higher yields than bonds. The recent low interest rate environment has made higher yields attractive when compared with cash investments as well. Income trusts also boast the potential for higher distributions over time. Another reason income trusts are popular with investors is that they are structured to avoid corporate taxes on distributions. In a traditional tax structure, distributions are taxed both at the corporate level and as dividends in the hands of the investor. Income trusts eliminate or significantly reduce corporate tax; the trust pays little or no tax on its earnings because most of the income is distributed directly to the unitholders.

This flow-through structure means that the distributions to income trust investors are generally higher than dividends from an

Fund

- [Handbook of Canadian Security Analysis](#)
- [2005 Tax Guide for Investment Advisors](#)
- [Common Sense Investing in Real Estate Investment Trusts](#)

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equivalent corporate entity.

Potential risks

Despite the potential for attractive regular payments, income trusts are equity investments, not fixed income securities, and they share many of the risks inherent in stock ownership. In addition, investors need to be aware of the following possible risks:

- **Lack of diversification.** Income trusts tend to be heavily invested in real estate, oil and gas, pipelines, and other infrastructure.
- **Potential sacrifice of growth.** Potential growth may be sacrificed because revenue is passed on to unitholders, rather than reinvested in the business.
- **No guarantees.** Income trusts do not guarantee minimum distributions or even return of capital. If the business starts to lose money, the trust can reduce or even eliminate distributions.
- **Potential for tax changes.** The current structure of trusts — which allows income to flow through to investors and be taxed only at the individual level — could be challenged under existing laws, or the tax laws could change.
- **Liability.** Income trusts do not offer the same limited liability protection that common stocks provide in every province. However, limited liability legislation is now in place in Ontario, Alberta, and Quebec; almost 90% of income trusts have statutory protection.

Recently, in addition to these risk issues, some analysts in the media have expressed concerns because of performance volatility. These are valid concerns, and that's why it's critical to do the research necessary to know what you are getting into.

Source: Excerpt from [TD Waterhouse - "investor insights - July/August 2005"](#)

► Income Deposit Securities (IDS)

An IDS consists of two securities - common shares and subordinated notes of the issuer - which are "clipped" together. Holders of IDSs receive dividends of the common shares and interest at a fixed rate on the subordinated notes to produce a blended yield. The distribution policies of IDS issuers are similar to those of REITs, master limited partnerships and income trusts, which distribute a significant portion of their free cash flow.

IDSs are listed on a stock exchange, but initially the underlying securities are not. However, in time (typically in the range of 45 to 90 days after the closing of the offering), holders may unclip the components of the IDS and trade the common shares and subordinated notes separately.

These securities are proving attractive to both institutional and retail investors, particularly in the current low interest rate environment. Another selling feature is the integrity of the distributable cash model, given recent corporate governance and accounting scandals.

▶ **Closed-end Investment Trust**

Closed-end Investment trusts are investing principally in other income funds securities of a specialized nature, or with Portfolio represents a particular Industry. Closed-end Funds issue only a fixed number of shares and trade on stock exchanges.

