

ESTATE LAW

Is a Trust Considered a Business or Individual?

A trust is neither a person nor a typical business. This guide clarifies its distinct legal standing and how it functions as a unique financial tool.



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A trust is a legal arrangement where one party, the trustee, holds and manages assets for the benefit of another, the beneficiary. This structure is created by a person known as the grantor. Whether a trust operates as an individual or a business is complex, as it can be treated differently for legal, tax, and financial purposes depending on the context.

The Legal Identity of a Trust

A trust is not a separate legal entity like a corporation; it is a fiduciary relationship recognized by law. In this arrangement, the legal ownership of assets is held by the trustee, who has a duty to manage them according to the trust document, while beneficiaries hold an equitable interest. A trust generally cannot act in its own name and instead acts through its trustee. For instance, lawsuits involving the trust are brought by or against the trustee in their official capacity, tying the trust's legal standing to its trustee.

How Trusts Are Treated for Tax Purposes

For tax purposes, the treatment of a trust depends on whether it is revocable or irrevocable. A revocable trust, often called a grantor trust, is a "disregarded entity" by the Internal Revenue Service (IRS). This means the trust itself does not pay taxes, and all income and deductions are reported on the grantor's personal income tax return, Form 1040, using the grantor's Social Security Number.

An irrevocable trust is typically considered a separate taxable entity that cannot be easily changed by the grantor. These trusts must obtain their own Employer Identification Number (EIN) from the IRS. The trustee files Form 1041, the U.S. Income Tax Return for Estates and Trusts, to report income. The trust itself pays taxes on any income it retains, subject to compressed tax brackets that reach high rates at lower income levels than for individuals.

If a trust distributes income to beneficiaries, it can deduct that amount, and the beneficiaries report the income on their tax returns via a Schedule K-1. This pass-through nature is similar to how some business entities are taxed. Filing Form 1041 is required if the trust has any taxable income or gross income of \$600 or more during the year.

ACCOUNTS

When opening a bank or investment account, financial institutions treat a trust as a distinct client, separate from the trustee as an individual. This process is more similar to opening a business account than a personal one. The bank's primary goal is to verify the trust's legal existence and the trustee's authority to act on its behalf.

To open an account, a trustee will need to provide a copy of the executed trust agreement or a Certification of Trust, which outlines the trust's terms. The bank will also require the trust's Taxpayer Identification Number (TIN) and the trustee's personal identification, such as a driver's license or passport.

How Trusts Are Treated for Owning Property and Assets

A trust holds legal title to assets, which legally separates them from the personal ownership of the grantor, trustee, and beneficiaries. When an asset like real estate is transferred into a trust, the property deed is updated to reflect the new ownership. The title is held in the name of the trustee on behalf of the trust.

For example, a property deed would be retitled to "Jane Doe, Trustee of the Doe Family Trust dated January 1, 2024." This titling makes it clear that Jane Doe owns the property in her fiduciary role as trustee. This legal distinction is a public record once the new deed is recorded with the local county office.

This separation of ownership has implications for asset protection. In an irrevocable trust, assets titled in the trustee's name are generally shielded from the personal creditors of the grantor and the beneficiaries. If a beneficiary faces a lawsuit or bankruptcy, creditors typically cannot seize assets held within the irrevocable trust.

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