Trusts, Tax Returns, and Tax IDs: A Primer

Presented by Warren Wealth Associates

If you've thought about (or finalized) an estate plan, chances are you've considered or established a trust as a part of that plan. In brief, a trust is a separate legal entity that can hold title to assets. The Trustee of the trust owns legal title to the trust's assets but must administer those assets on behalf of the trust's beneficiaries as provided in the trust.

Since a trust is a separate entity, one question that often arises is whether a trust needs to file its own tax return. The answer, as usual, is "it depends." As discussed below, revocable or "living" trusts will generally not require a separate return while the grantor (the person who created and funded the trust) is living. Trusts that do require a return will need to obtain a tax identification number – also known as a "tax ID number" or an "employer identification number" ("EIN") – to file those returns.

This piece is meant to give a brief overview of what a tax ID number is, when a trust might need to obtain one, and how to go about obtaining a tax ID number when necessary. Please note that these issues are necessarily complex and require tax and legal decisions that can have a significant impact on a trust (and a beneficiary's!) taxation. It is therefore strongly recommended that either the attorney or accountant for the trust obtain or assist with obtaining any tax ID number.

What is a tax ID number?

A tax ID number is essentially a social security number for organizations, including certain types of trusts. It's a number assigned by the IRS for tax reporting purposes that allows the IRS to track organizations in the same way as individuals. For trusts that require a tax ID number, tax reporting documents, such as 1099s, are issued to the trust under that tax ID number, and the trust would file its tax return under that number.

When does a trust need a tax ID number?

Generally, a trust will need a tax ID number unless it is specified exempted under IRS rules as a "grantor trust" – that is, taxable to the person who created and funded the trust.

While the precise details of when a tax ID number is necessary beyond the scope of this article, in practice, we can think about three types of trusts:

- **Single grantor revocable trusts.** When you establish a trust that remains amendable and revocable by you, all income would generally be taxed to your social security number, and the trust would not require a tax ID number while you are living. Upon your death, however, your revocable trust becomes irrevocable (even if the word "revocable" appears in the title of the trust, which it often does). The IRS has issued a specific regulation governing this scenario, under which, upon the death of the grantor of a revocable trust, that trust becomes a separate tax reporting entity and generally must obtain a tax ID number. All income earned by the trust after the death of the grantor would need to be reported under that tax ID number. If the trust splits into multiple subtrusts as a result of the grantor's death, multiple tax ID numbers may be required – one for each subtrust.

- **Joint grantor revocable trusts.** Married couples often execute joint revocable trusts as a part of their estate planning. Generally, while both spouses are living, a joint trust will be fully amendable and revocable by those spouses. Accounts for the trust would be administered under the social security numbers of one of the spouses. Whether a tax ID number is required at the death of the first spouse will depend on the terms of the trust. It's possible that a portion (or all) of the trust would continue to be administered under the surviving spouse's social security number, and another portion (or all) would require a tax ID number. At the death of the second spouse the trust would require a tax ID number, if not obtained already.

- **Irrevocable Trusts.** While beyond the scope of this article, many irrevocable trusts will require a tax ID number even while the grantor is living, unless the trust is specifically drafted to be taxable to the grantor. When establishing an irrevocable trust, you should consult carefully with your estate planning and tax professionals regarding the income tax consequences of that trust.

An example:
Let's take a simple example to help illustrate these points. Jane and John Smith are a married couple who each established a revocable trust in their estate plans. We'll focus on Jane's trust here. During Jane's life, all income earned by assets in the trust would simply be taxed on her own tax return. Unfortunately, Jane recently passed away. Jane's trust provides that at Jane's death, the trust is to split into two shares – one share for John, known as the "Marital Trust," and one share for John and their children, known as the "Family Trust," both of which will receive assets as a result of Jane's death. Let's assume that John Smith is named as the Trustee of both of those trust shares.

Because Jane's trust is now irrevocable as of her date of death, and because it splits into two separate, funded shares, each share will require its own tax ID number.

How do I obtain an EIN?
While a tax ID number can be obtained by mailing or faxing a paper application (IRS form SS-4), in practice most tax ID number applications are now filed online through the IRS' online EIN portal, located at this link. Applying online allows for assignment and receipt of the tax ID number within minutes of beginning the application, as opposed to days or weeks with a paper application.

Generally, when obtaining an EIN number for a formerly revocable trust where the grantor is now deceased, the following information will be required:

- Name of the trust. This may, and often does, differ from the name of the original trust document. In our example, the name of the Marital Trust share under Jane's trust would be something like the "Marital Trust fbo John Smith" ("for the benefit of" is often designated as "fbo").

- Type of trust. There are numerous types of trusts to choose from in the online application, including Charitable Remainder Trusts and categories not often thought of as trusts, such as conservatorships. In our example, the type of trust would be "irrevocable trust."

- Name and social security number of the “responsible party.” For trusts, the responsible party is the grantor, owner, or trustor. When filling out the online form, and subject in each case to confirmation from legal counsel or a tax preparer, you would generally list the grantor of the trust – *even though they are deceased in our example* – as the responsible party (in our example, this would be Jane Smith). (Putting in the Trustee’s information could lead to errors on the form.) Note that the grantor’s social security number would be needed here.

- Name of the trustee.

- Address of the trust. This should generally be the Trustee’s address.

- Decision on a so-called 645 election – making this election would allow the trust to be combined with the grantor’s estate – another separate taxpaying entity – for tax reporting purposes. Care would need to be taken on the decision to make this election – which is not amendable once made – and the attorney or accountant should be consulted, as the election will impact tax planning for the trust. If no 645 election is made, the closing month for the tax year of the trust must be December.

- Date the trust was funded (phrased as the “Date the business was started” on the paper form SS-4). For our example, this would generally be the date of Jane’s death, *even if* the trust had been funded during Jane’s life.

- Whether the trust anticipates having any employees – generally, this would be “no.”

If submitting the paper form, there are several other questions relating to business that would be inapplicable to trusts. Those questions are avoided by utilizing the IRS’ online application.

Once submitted, it is difficult to correct errors in a tax ID application, so care must be taken to get it right the first time.

Again, the above is just meant as a general overview on these issues and is not meant to be determinative or substitute for the advice of legal counsel or a tax preparer. Your advisor can help guide you through these issues and prepare you for meeting with that counsel or tax preparer to help efficiently obtain a tax ID number when needed.

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