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What Dental Practitioners Should Know About Trusts

By: Steven Podnos, M.D., CFP®, Senior Wealth Advisor

For dental practitioners who have built substantial personal and professional wealth, a trust may play an important role in transferring assets, guiding an inheritance, and protecting assets for future generations. Understanding what a trust can and cannot accomplish is an important starting point for deciding whether one belongs in your estate plan.

Key Takeaways

- A trust holds assets for designated beneficiaries according to instructions established by the person creating the trust.
- Revocable living trusts may help assets pass outside of probate, but they generally do not provide asset protection for the person who established the trust.
- Trusts can provide greater control over when and how beneficiaries receive an inheritance.
- An inheritance held in trust may offer protection for beneficiaries who face professional liability, marital, or other creditor risks.
- Creating a trust is only one step. Asset ownership and beneficiary designations should also be coordinated with the estate plan.

What Is a Trust?

I'd suspect that almost every dental family has been told that they need a trust as part of estate planning. Indeed, in most cases, a trust is an artificial creation usually designed for assets you leave to heirs.

Think of it like a bucket that holds these assets, with a document, the trust itself, that governs how assets move into and out of the bucket. Then, there is a trustee, or more than one trustee, who executes

the instructions in the trust document and, finally, a beneficiary or several beneficiaries who receive the assets as governed by the trust document and the trustee.

Most trusts we encounter are revocable living trusts. Revocable implies impermanence. You can move assets into and out of the trust while you are alive as you wish. For this reason, these trusts do not offer asset protection because a judge can compel you to invade the trust to pay a plaintiff. These trusts are also sometimes called grantor trusts, as the term “grantor” refers to the person or people forming the trust.

Why Might a Dental Family Need a Trust?

There are really three main reasons to have a trust: to help assets avoid probate, to establish greater control over how assets are distributed, and to provide asset protection for heirs.

Avoiding Probate

The first reason is to avoid probate on the assets owned by the trust itself. Probate is the “clearing” of assets owned by someone who has just died so that the funds can pass to heirs.

If a trust owns the assets during life, the grantor’s death does not change the ownership by the trust, and no probate of those assets is needed. Often, the titling of assets and the use of beneficiary designations can cause most of an estate to pass outside of probate anyway, and the trust may be less important for this reason.

Controlling How an Inheritance is Distributed

A second benefit of a trust is to allow control over the distribution of assets after the death of the grantor or grantors.

If someone has responsible adult children who do not need asset protection for inherited funds, a trust may not be necessary or even desirable. In this case, a simple will dispensing of the assets may be all that is needed.

But in many cases, it is important to decide what level of control you want over the distribution of assets. It may be unwise for younger people to have "too much money," so the level of financial support provided by the trust before an heir is mature and responsible is important.

Many trusts allow a trusted person, the trustee, to have significant discretion over how the money is distributed, with the hope that the trustee will act as the parents would have in similar circumstances.

Any family that would be leaving a significant sum of money to minor children really must have a trust. This trust would provide control over the distribution of the trust's contents while also providing asset protection for this important money. How much control is appropriate and how long it should continue are highly variable and will differ for each family.

Unfortunately, some children never become responsible enough to safely manage an inheritance, and the control over distributions offered by the trust might be valuable for a prolonged period.

Protecting an Inheritance for Your Heirs

One of the best reasons to use a trust is to provide asset protection for your heirs.

At the time of the grantor's death, the trust becomes irrevocable, which means that it is very difficult to change. Once a trust is irrevocable, it may offer significant asset protection, especially if there is at least one trustee who is not a beneficiary.

Depending on the trust's terms and applicable law, a judge may not be able to compel distributions from the trust for the benefit of a plaintiff. Exceptions and limitations may apply, including certain claims involving child support or the IRS.

If control is not desired, friendly trustees can make distributions when no creditors, whether marital, accident-related, or otherwise, are present. We are reluctant to agree to terms that make mandatory distributions based on age, as that may be the exact time a creditor is present.

We counsel some potential inheritors of substantial sums to consider inheriting "in trust" rather than outright. This is particularly true of heirs who work in fields that may expose them to lawsuits, including medicine and dentistry, or who have concerns involving a marriage.

Inheriting in trust may allow them to benefit from the assets without directly exposing those assets to certain marital or malpractice creditors. The effectiveness of these protections will depend on the trust's provisions and applicable law.

Deciding Whether a Trust is Right for Your Family

There is much more to these structures than can be discussed in one article. The process of forming a trust begins with deciding whether it is an appropriate structure for your heirs.

Each family might have different reasons to use trusts. In the past, trusts were often useful in saving on estate taxes. Today, whether a trust provides estate-tax benefits depends on the family's circumstances, the applicable exemption amounts, and the particular trust structure.

At times, a trust may be used to control assets for heirs who are not yet, or may never be, responsible enough to own the assets outright. But in many cases, using a trust represents an act of love and protection.

When an individual or a couple finishes living, they are usually left with assets intended for those they love and care about. In many cases, simply leaving the assets outright to heirs works well, but there are instances in which a trust might provide value.

Because the trust document may convey instructions in somewhat dry legal language, it helps greatly to think about how to communicate the true intent of the trust through the words you choose to use.

Control over how money comes out of the trust might be important to protect an inheriting child from wasting your legacy. Providing asset protection for that money can also be valuable.

Coordinating Your Trust with the Rest of Your Estate Plan

Finally, it is important to remember that many, if not most, of the things you own do not pass through your will.

Retirement accounts and IRAs pass according to their beneficiary designations, as do life insurance policies and most annuities. Assets owned with a right of survivorship with another person will generally pass to the surviving owner.

If you create a trust, you must also make sure that the ownership of your assets and your beneficiary designations are coordinated with the trust and your broader estate plan. In some cases, a trust may be named as a contingent beneficiary while a spouse remains the primary beneficiary.

Before changing a beneficiary designation or naming a trust as a beneficiary, consult with your estate-planning attorney, financial advisor, and tax professional to evaluate the possible legal and tax consequences.

Taking the Next Step

A trust can be an effective estate-planning tool, but its value depends on the family's circumstances, the trust's provisions, and how the family's assets are titled and coordinated.

Dental practitioners should work with their estate-planning attorney, financial advisor, and tax professional to determine whether a trust is appropriate and how it should fit within the broader estate plan.

Are you a dental practitioner interested in learning more about trusts? Connect with Steven Podnos to learn more.

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