ALERT
JULY 2019

United States Supreme Court Rules State Cannot Tax Trust's Income

***Kaestner* ruled that a state's taxation of a trust's income, where the only connection to the state was an in-state beneficiary, violates the Due Process Clause.**

On June 21, 2019, the United States Supreme Court unanimously ruled unconstitutional a state's taxation of a trust's income where the only connection to the state was an in-state beneficiary. In *North Carolina Department of Revenue v. Kimberley Rice Kaestner 1992 Family Trust,* North Carolina sought to tax the income of a trust that was settled in New York, managed by a trustee in New York under New York law, and had no assets or direct investments in North Carolina.

The Due Process Clause requires, for tax jurisdiction, both (i) a minimum connection between the state and the person, property, or transaction it seeks to tax and (ii) a rational relationship between the tax and activities occurring within the state. In previous decisions the Court ruled states may tax trust distributions to an in-state beneficiary, and a trust's income if the trustee administers the trust in that state.

In *Kaestner*, North Carolina argued that the presence of trust beneficiaries in the state created sufficient nexus for North Carolina to tax the trust's income. The Supreme Court, however, held that the beneficiaries' mere presence—with no control over the trust's assets or distributions—does not create the minimum connection required by the Due Process Clause. The Court left open the possibility that a tax on out-of-state trusts could pass muster if an in-state beneficiary exercised control over the trust's assets or income.

Cases regarding state courts' ability to exercise jurisdiction over out-of-state litigants have historically informed the Court's state tax Due Process Clause jurisprudence. In 1992, relying on such cases, the Court announced in *Quill Corp. v. North Dakota* a relatively lax standard for state tax Due Process. Since then, many adjudicative jurisdiction cases have implied that a more robust connection between the taxpayer, its activity, and the taxing state is required. But to reach its narrow holding in *Kaestner*, the Court did not need to engage with these cases. Future cases may test the outer boundaries of state tax jurisdiction under the Due Process Clause.


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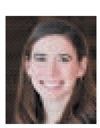
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