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Justices Won't Weigh Denial Of Minn. Attempt To Tax Trusts

By [Daniel Tay](#) · June 28, 2019, 8:56 PM EDT

A Minnesota Supreme Court holding that Minnesota violated due process when it tried to tax four trusts as residents based on the grantor's residency will stand, as the [U.S. Supreme Court](#) declined the state's review request Friday.

The Supreme Court declined to review the Minnesota Supreme Court's decision that the trusts, established by a lifelong Minnesota resident, lacked sufficient connection to the state for the department to tax the trusts' worldwide income. The state high court had awarded refunds totaling over \$1 million. The Supreme Court announced its decision without comment, in keeping with its typical practice.

The department, in requesting review, [had said](#) the Supreme Court needed to clarify whether a state could tax a trust administered outside its borders as a resident and remain consistent with the U.S. Constitution's due process clause, as state appellate courts were "deeply divided" and had issued conflicting rulings. According to the department, the "flawed and outdated" interpretation of the due process clause used by various courts deprives states of revenue and allows individuals to avoid taxes by placing their assets in trusts and retaining trustees residing in no-income-tax states.

Reid MacDonald, a lifelong Minnesota resident, established the trusts in 2009 and relinquished control over them in 2011, after which the trusts became irrevocable. In 2014, the trusts sold shares of a Minnesota S corporation, and the department asserted they were deemed Minnesota residents because of their grantor's Minnesota residency at the time the trusts became irrevocable. According to the department, this made the trusts subject to tax on the full amount of gain from the sale as well as on the full amount of income from other investments.

The Minnesota Supreme Court [ruled, however](#), that MacDonald's residency did not qualify as a minimum connection for the trusts to be subject to taxation as residents. The state high court said his residency was irrelevant to the relationship between the trust income being taxed and the protection and benefits the state provided to the trust's income-generating activities. Instead, the court considered the Texas residency of the trustee, William Fielding, and said other connections with Minnesota, such as the trusts' incorporation of Minnesota law, were insufficient for due process purposes.

Stuart Kohn, head of the Trusts and Estates Group at [Levenfeld Pearlstein LLC](#), told Law360 Friday it was not surprising the Supreme Court declined to take up the case, given that it had [already taken up](#) another state trust taxation case in [North Carolina Department of Revenue v. Kimberley Rice Kaestner 1992 Family Trust](#).

Kohn said it was interesting the court had taken up Kaestner instead of Fielding given that more states use the grantors' residence, and not the beneficiaries' residence, to determine how

to tax trusts, but added that the issue could still come before the high court, if another state rules differently from Minnesota's high court.

Kohn also said it was interesting that Minnesota had ruled the grantor's residency did not qualify as a minimum connection.

“Here, the grantor availed himself of the benefits of that state. It seems to me the state does have more of a connection that justified the tax,” Kohn said. “It'll be interesting to see whether that decision, and now that cert was denied, that we might see similar cases in the other 21 states.” He was referring to the other states that consider grantor residence in determining trust taxation.

Jeff Carson, senior vice president at Diversified Trust's national office, agreed that Kaestner and Fielding were not so different that the court would take both cases up, although he told Law360 on Friday he felt the argument for taxation in Fielding was weaker than in Kaestner.

“For the grantor, particularly in Fielding, he had no control,” Carson said. “Other than his residency and the fact that he created the trust several years before, there was nothing to allege by the state that he had any possession, any control ... it's really the possession and control factor.”

Carson told Law360 that states like Minnesota may try to change their laws to adjust what they consider minimum connection.

Representatives for Fielding and the trusts did not respond to requests for comment.

Representatives of the department declined to comment.

Fielding and the trusts are represented by Walter A. Pickhardt, Laura S. Carlson, Caitlin E. Abram and Nicholas J. Nelson of [Faegre Baker Daniels](#).

The department is represented by John M. O'Mahoney of the [Minnesota Attorney General's Office](#).

The case is Cynthia Bauerly, Commissioner, [Minnesota Department of Revenue](#) v. William Fielding, Trustee of the Reid and Ann MacDonald Irrevocable GST Trust for Maria V. MacDonald et al., case number 18-664, in the U.S. Supreme Court.

--Editing by John Oudens.

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