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TAX UPDATE: REVIEW OF THE KAESTNER DECISION

In 2019, the Supreme Court of the United States considered North Carolina Department of Revenue v. The Kimberley Rice Kaestner 1992 Family Trust ("Kaestner"), which was on appeal from the Supreme Court of North Carolina. The key issue in Kaestner was whether the North Carolina Department of Revenue could tax the undistributed income of the Kimberley Rice Kaestner 1992 Family Trust from tax years 2005 through 2008 solely because its beneficiaries were North Carolina residents.

In a 9-0 decision, the Court held that it was unconstitutional for North Carolina to tax the undistributed income of the trust solely because beneficiaries of the trust live in North Carolina. However, in reaching this holding, the Court emphasized that its ruling was narrow and limited to the specific facts of the case and tax years in question. In pertinent part, the Court held:

"This case is about the limits of a State's power to tax a trust, North Carolina imposes a tax on any trust income that 'is for the benefit of' a North Carolina resident. The North Carolina courts interpret this law to mean that a trust owes income tax to North Carolina whenever the trust's beneficiaries live in the State, even if—as is the case here—those beneficiaries received no income from the trust in the relevant tax year, had no right to demand income from the trust in that year, and could not count on ever receiving income from the trust. The North Carolina courts held the tax to be unconstitutional when assessed in such a case because the state lacks the minimum connection with the object of its tax that the Constitution requires. We agree and affirm. As applied in these circumstances, the State's tax violates the Due Process Clause of the Fourteenth Amendment."

In this way, the opinion is helpful in reiterating the Due Process Clause's limits on a state's ability to tax income. However, because the opinion is so narrow, the Court has left open for consideration what types of connections with a state are sufficient to satisfy constitutional requirements such that our state can tax the income of a trust.

Next, in terms of updates specific to North Carolina, our General Assembly did not promulgate significant legislation in the area of trusts and estates. However, we continue to monitor proposed statutory changes and pending legislation.

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