



FIELDING vs. COMMISSIONER OF REVENUE: AFTER MORE THAN 20 YEARS, IS MINNESOTA’S FIDUCIARY “PERMA-TAX” ON IRREVOCABLE TRUSTS NO LONGER PERMANENT?

Since January 1, 1996, the State of Minnesota has taxed the income, both ordinary and capital gains, of what Minn. Stat. § 290.01, subd. 7b(a) defines as a “resident trust.” Such a trust is one that is not a grantor trust for tax purposes and that either (1) was created under the will of a decedent who at death was domiciled in Minnesota or (2) is an irrevocable trust, the settlor of which was domiciled in Minnesota at the time the trust became irrevocable (and regardless of whether the settlor subsequently became domiciled in another state or foreign country).

Affirming a 2017 decision of the Minnesota Tax Court, the Minnesota Supreme Court, in *Fielding vs. Commissioner of Revenue* (A17-1777, July 28, 2018), ruled that, *as applied to the four trusts at issue in the case*, Minn. Stat. § 290.01, subd. 7b(a) is unconstitutional in violation of the due process clauses of both the U.S. and Minnesota Constitutions. The *Fielding* opinion is available at:

<https://mn.gov/law-library-stat/archive/supct/2018/OPA171177-071818.pdf>

Although *Fielding* did not declare the “resident trust” statute unconstitutional on its face, it appears that, after more than 20 years, there once again is the opportunity to formulate a course of action by which at least an *inter vivos* irrevocable trust can affirmatively change its tax residence from Minnesota to a state, such as South Dakota, that does not levy fiduciary income tax. Involvement of expert tax counsel is critical in this regard, however, since Minn. Stat. § 290.01, subd. 7b(a) remains on the books, and the specific facts that underlie the *Fielding* opinion must be considered in designing and executing an effective strategy for changing Minnesota tax residence.

In addition to not standing as a broad declaration of the unconstitutionality of Minnesota’s post-1995 “resident trust” statute, there are two other matters of legal significance outside the scope of *Fielding*:

- *Fielding* did not address the constitutionality of the “resident trust” statute as applied to irrevocable testamentary trusts created on or after January 1, 1996 (*i.e.* trusts under will).
- Minn. Stat. § 290.01, subd. 7b(b) continues to govern trusts, whether *inter vivos* or testamentary, that became irrevocable prior to January 1, 1996, and provides that such a trust is a “resident trust only if two or more of the following conditions are satisfied:

- (1) *a majority of the discretionary decisions of the trustees relative to the investment of trust assets are made in Minnesota;*
- (2) *a majority of the discretionary decisions of the trustees relative to the distributions of trust income and principal are made in Minnesota;*
- (3) *the official books and records of the trust, consisting of the original minutes of trustee meetings and the original trust instruments, are located in Minnesota.”*

While changing the tax residence of a post-1995 irrevocable testamentary trust is an uncertain proposition, the utilization of a grantor trust, rather than a will, to implement an estate plan involving one or more post-mortem irrevocable trusts would appear to be one possible approach to prospectively avoid the uncertainty.

Although the bright-line certainty of the “resident trust” definition applicable to pre-1996 irrevocable trusts is unavailable, a sound post-*Fielding* strategy for either changing Minnesota tax residence or avoiding it altogether presumably would have as its starting point satisfying not just two of the foregoing conditions, but all three of them and otherwise tracking the *Fielding* facts as closely as possible. In any event, it certainly would be prudent, if not imperative to replace Minnesota trustees, whether corporate or individual, with a corporate trustee chartered in a state like South Dakota and individual trustees who are not residents of Minnesota.

First Trust Company is a South Dakota-chartered trust company with trust service offices in St. Paul and Omaha. First Trust does not provide tax and other legal advice, but our experience and expertise as a fiduciary is accompanied by a commitment to work collaboratively with lawyers and other tax, legal, and financial advisers to serve our mutual clients. We welcome the opportunity to participate in discussions of how we can play an integral role in the effective execution of strategies for changing the tax residence of a trust from Minnesota to South Dakota or establishing South Dakota residence in the first place.

Our Locations:

SOUTH DAKOTA: Suite 200 | 909 St. Joseph Street | Rapid City SD 57701 | 605.791.5133

MINNESOTA: Suite W2900 | 332 Minnesota Street | St. Paul MN 55101 | 651.330.5910

NEBRASKA: Suite 100 | 9300 Underwood Avenue | Omaha NE 68114 | 402.397.5241

E-mail inquiries to info@firsttrustcompany.com
<https://firsttrustcompany.com/>