

SUPREME COURT OF THE UNITED STATES

IN THE SUPREME COURT OF THE UNITED STATES

NORTH CAROLINA)
DEPARTMENT OF REVENUE,)
) Petitioner,)
) v.) No. 18-457
THE KIMBERLEY RICE KAESTNER)
1992 FAMILY TRUST,)
) Respondent.)

Pages: 1 through 69
Place: Washington, D.C.
Date: April 16, 2019

HERITAGE REPORTING CORPORATION
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1220 L Street, N.W., Suite 206
Washington, D.C. 20005
(202) 628-4888
www.hrccourtreporters.com

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P R O C E E D I N G S

(11:07 a.m.)

CHIEF JUSTICE ROBERTS: We'll hear argument next in Case 18-457, the North Carolina Department of Revenue versus the Kaestner Rice 1992 Family Trust.

Mr. Sawchak.

ORAL ARGUMENT OF MATTHEW W. SAWCHAK

ON BEHALF OF THE PETITIONER

MR. SAWCHAK: Mr. Chief Justice, and may it please the Court:

This case involves a statute that taxes trust income in proportion to the interests of in-state beneficiaries. Now, trust beneficiaries, it bears remembering, are the true owners of trust income under trust law.

Because of all the benefits and protections that states extend to their residents, the states' pro rata tax on trust income comports with due process. But --

JUSTICE GINSBURG: You couldn't -- you couldn't tax the beneficiaries on that accumulated income when they haven't received it?

1 MR. SAWCHAK: Well, Your Honor,
2 Stewart might be to the contrary. This Court's
3 affirmance in Stewart is a situation where the
4 opinion of the Pennsylvania Supreme Court that
5 was affirmed doesn't recite any receipt of
6 actual income, and yet the Court affirmed a tax
7 on the beneficial interests.

8 JUSTICE GINSBURG: But North Carolina
9 is not doing that.

10 MR. SAWCHAK: North Carolina is taxing
11 the --

12 JUSTICE GINSBURG: Yeah.

13 MR. SAWCHAK: -- accumulating income.

14 JUSTICE GINSBURG: But you want to use
15 the beneficiary's connection with North
16 Carolina to impose a tax on the trust that
17 doesn't have a connection?

18 MR. SAWCHAK: So, Your Honor, the
19 point that connects them is that the
20 beneficiary is part of the trust. Indeed,
21 under trust law, she is the key part of the
22 trust, its very heart. And because of that,
23 the whole --

24 JUSTICE SOTOMAYOR: Isn't the trust
25 for her and her children?

1 MR. SAWCHAK: She is the named
2 beneficiary. However, under Section 1.2 of the
3 trust instrument, the children may also receive
4 distributions.

5 JUSTICE SOTOMAYOR: So we've already
6 said in prior cases, and you distinguish them
7 as being inapposite today, that you can't tax
8 the whole trust; you've got to only tax that
9 which the beneficiary is an owner of.

10 So how do we know she's going to
11 receive anything any time? She could leave it
12 for her kids.

13 MR. SAWCHAK: She -- in -- in the
14 event of this case, first of all --

15 JUSTICE SOTOMAYOR: I mean, the
16 trustee could -- could decide to leave it for
17 the kids.

18 MR. SAWCHAK: That's true. But
19 several points. First of all, on the facts
20 here, Ms. Kaestner did, in fact, receive the
21 trust income, and the decanting occurred only
22 after consultation --

23 JUSTICE SOTOMAYOR: There was a loan,
24 \$250,000, after this tax period?

25 MR. SAWCHAK: Immediately after, there

1 was a loan, but, in addition --

2 JUSTICE SOTOMAYOR: But it still begs
3 the question, what makes it your right under
4 any circumstance to tax all of the trust income
5 where there's no guarantee that she is going to
6 receive all of it at any point?

7 MR. SAWCHAK: Several points. One is,
8 during the entire period when the income is
9 accumulating, the state is providing her with
10 protection and benefits --

11 JUSTICE SOTOMAYOR: But the trustee
12 doesn't have to pay for that. He's not
13 required to. The trust doesn't require it. It
14 gives him discretion to pay for some of her
15 expenses, but nothing in the trust says that
16 she has to pay for the benefits that you're
17 giving her as a state.

18 MR. SAWCHAK: But it is the very fact
19 that those benefits and protections are being
20 extended that enables the trustee to not give
21 distributions.

22 JUSTICE SOTOMAYOR: Now he has
23 absolute discretion. Whether she had a need or
24 not, he doesn't have to fulfill it.

25 MR. SAWCHAK: Under trust law, even

1 what -- what's called sole and absolute
2 discretion is qualified by the need to look out
3 for the needs of the beneficiaries. And that's
4 actually an express term of the trust
5 instrument here.

6 CHIEF JUSTICE ROBERTS: I probably
7 should know --

8 JUSTICE ALITO: Could you tax the --

9 CHIEF JUSTICE ROBERTS: -- I probably
10 should know this, but where is the trust
11 located? How do you decide that?

12 MR. SAWCHAK: The trust has no --

13 CHIEF JUSTICE ROBERTS: I mean, it's
14 just a -- yeah, it's just a contract, right?
15 So if you wanted -- if the home of the trust
16 wanted to tax the -- the same income that
17 you're trying to tax, where -- where would that
18 be?

19 MR. SAWCHAK: So the trust has no
20 situs. Since Quill and other decisions, the
21 focus really is on where are benefits and
22 protections being extended. And also, in
23 Americold, this Court -- Greenough as well, the
24 Court noted that a trust is a mere abstraction.
25 And that's why -- that's really what brings us

1 here.

2 CHIEF JUSTICE ROBERTS: So you would
3 -- you would say there's no state that could
4 say we are the home state of the trust and
5 we're the ones that have the primary claim on
6 the taxation of this income?

7 MR. SAWCHAK: So the -- under trust
8 law, a trust has something called a principal
9 place of administration. And one of the
10 arguments my friend is making is that that
11 and/or where the trustee lives are the only
12 contacts that count.

13 But that, first of all, I would point
14 out -- page 51 of the red brief is where they
15 make that argument -- that would have the
16 effect, adopting that rule, as my friend is
17 asking, would have the effect of striking down
18 the taxing criteria in 33 states.

19 JUSTICE BREYER: All right. We --

20 CHIEF JUSTICE ROBERTS: So do you
21 think --

22 JUSTICE BREYER: -- don't want to do
23 that, but, look -- sorry, go ahead.

24 CHIEF JUSTICE ROBERTS: No, no, go
25 ahead.

1 JUSTICE BREYER: Look, the trustee
2 lives in New York, okay? The settlor is in New
3 York. All the administration is in New York.
4 There is one thing that's going to happen in
5 North Carolina. The thing that's going to
6 happen in North Carolina is if she is there
7 when it's distributed, she'll get some money.
8 Okay? Which you're totally free to tax.

9 But that isn't what you want to tax.
10 You want to tax all these things which are
11 everyone except her is in New York, and
12 moreover, we don't even know if she'll ever get
13 the money.

14 Now there's something wrong with that.
15 I don't know, it doesn't say specifically about
16 trusts in the Constitution, but, thus, I mean,
17 lots of trusts say there are 10 beneficiaries,
18 each one lives in a different state, and I, the
19 trustee, have total discretion as to who give
20 this money to and maybe I'll give it to none of
21 them.

22 So here's a woman who might get none
23 of it, and you want to tax that. Is that
24 right? Do I have the facts right?

25 MR. SAWCHAK: I would -- I would point

1 out some additional facts, Your Honor. First
2 of all, Ms. Kaestner did actually receive this
3 money.

4 JUSTICE BREYER: Well, is that -- is
5 that -- I'm talking about the law of North
6 Carolina. And I'd only add to this that, by
7 the way, if the trust has a million dollars
8 extra income in year 4, and if you say she's
9 entitled to that, she isn't going to get it
10 'til year 14, at most, do you discount the
11 increased value of the trust by the time she
12 has to wait? Because she has nothing that
13 increased in value more than the million
14 discounted by the probability that she will
15 ever get it and when.

16 MR. SAWCHAK: So --

17 JUSTICE BREYER: Is that how the law
18 works in North Carolina, is what I'm asking.
19 And, of course, I suspect the answer is no, but
20 go ahead.

21 (Laughter.)

22 MR. SAWCHAK: First of all, this is a
23 case in which 100 percent of the beneficiaries,
24 the current beneficiaries, as the complaint
25 itself says, are North Carolinians. So these

1 questions of -- of attenuated relationships
2 aren't presented.

3 JUSTICE BREYER: No, I'm talking about
4 only North Carolinians. And there are other
5 people in the trust who live in California.
6 And the North Carolinian may or may not get
7 some money in year 14. That's the hypothesis.

8 MR. SAWCHAK: Mm-hmm.

9 JUSTICE BREYER: Okay. And I'm saying
10 under this law, do you -- you tax that, what do
11 you tax? The million dollars in extra value
12 that came into the trust in year 4? And
13 what percent? And do you discount it? And
14 might she -- well, how does it work, that law
15 in North Carolina that you are defending?

16 MR. SAWCHAK: So the income is defined
17 with reference to the federal definition of
18 income. The -- the -- the taxing statute in
19 North Carolina essentially pulls in the federal
20 definition of distributable net income. And
21 that is going to be done on essentially an
22 accrual or a cash basis, depending on -- on how
23 it's approached in the federal law.

24 JUSTICE BREYER: Okay. So it goes
25 in -- \$1 million goes into the trust in year 4.

1 She will not see a penny of it, at best, 'til
2 year 14. And, not only that, she may never see
3 a penny of it.

4 So what you're saying is the trust,
5 which is in New York, has to pay Carolina tax
6 on a million dollars because there is a
7 beneficiary there who might never receive it
8 or, if they do receive it, will receive a
9 far -- you know, you could tax -- that -- have
10 I got the facts right?

11 MR. SAWCHAK: So she's -- the facts
12 are perhaps at some variance with what we're
13 discussing. First of all, she --

14 JUSTICE BREYER: But is what I said
15 right? That's -- I want to think about this
16 case and I can't think about it unless I get
17 the facts right.

18 MR. SAWCHAK: Let me lay out some --

19 JUSTICE BREYER: So do I have the
20 facts right?

21 MR. SAWCHAK: I would lay out some
22 additional facts that might be helpful.

23 JUSTICE KAVANAUGH: Isn't it a yes?

24 (Laughter.)

25 MR. SAWCHAK: She's currently

1 eligible for distributions.

2 JUSTICE KAVANAUGH: He has -- Justice
3 Breyer has the facts right?

4 MR. SAWCHAK: I believe you have them
5 right but perhaps not complete --

6 JUSTICE BREYER: Okay. So now --

7 MR. SAWCHAK: -- is what I meant to
8 say.

9 JUSTICE BREYER: Good, I got them
10 right so far. And now let's add to make even
11 more facts.

12 (Laughter.)

13 MR. SAWCHAK: She's currently eligible
14 for distributions, first of all, during the
15 years in question. Secondly, the -- the
16 trustee has a fiduciary duty to meet her needs,
17 page 51 of the Joint Appendix.

18 And as the Andrew C. case from New
19 York that we cite points out, in a situation
20 where the needs are not being met, a breach of
21 fiduciary duty is occurring. But, most
22 fundamental, I think, to --

23 JUSTICE ALITO: Now what -- where does
24 that go? So what are her -- what proportion of
25 this constitute her needs?

1 MR. SAWCHAK: North Carolina, the
2 statute is a pro rata statute, according to the
3 interests of the beneficiaries. So, if there
4 are two beneficiaries, for example, one in
5 state and one out of state, North Carolina will
6 first of all follow any allocation that's made
7 in the trust instrument but, failing that, will
8 go strictly pro rata.

9 JUSTICE ALITO: Can you -- could you
10 tax the children?

11 MR. SAWCHAK: They are eligible to
12 receive distributions so -- tax based on the
13 children, Your Honor, or tax them?

14 JUSTICE ALITO: Tax -- excuse me, tax
15 them. They might get the money.

16 MR. SAWCHAK: So Stewart upholds a
17 property tax levied directly to the
18 beneficiaries. And what all of this is really
19 reinforcing is that, under trust law, the true
20 owners of even accumulating --

21 JUSTICE KAVANAUGH: But other states
22 don't do it this way, right? Tennessee, but
23 they're ending the income tax. Maybe Georgia,
24 where the tax is based on a contingent
25 beneficiary in your state, which is all we have

1 here, right?

2 The only other states that do it that
3 way are Tennessee and maybe Georgia, is that
4 correct?

5 MR. SAWCHAK: Not quite, Your Honor,
6 in this respect. Fifteen states total --

7 JUSTICE KAVANAUGH: Based on a
8 contingent beneficiary in the state where you
9 tax the trusts or the trustee in another state.

10 MR. SAWCHAK: No, Your Honor. Let me
11 point out that, first of all, 15 states use
12 beneficiary residency as at least a criterion.

13 Second is --

14 JUSTICE GINSBURG: How about how many
15 states use that where the trust is administered
16 to tax the accumulated but undistributed
17 income?

18 MR. SAWCHAK: That -- fewer states use
19 the place of administration as a criterion than
20 use the criteria that are being challenged
21 here.

22 JUSTICE GINSBURG: But does North
23 Carolina tax a trust that's administered in
24 North Carolina on the accumulated but
25 undistributed income?

1 MR. SAWCHAK: Only in relation to the
2 shares of any in-state beneficiaries.

3 And, Justice Kavanaugh, if I may, I
4 want to follow up on one point. It is a
5 misconception by my friends to say that the
6 Kaestners are contingent beneficiaries. The
7 state supreme court, for example, called
8 Mrs. Kaestner the primary beneficiary.

9 JUSTICE KAGAN: So how can the trustee
10 change the beneficiary status? What does the
11 trustee have to do if the trustee wants to --
12 say, you're no longer a beneficiary? When can
13 the trustee say that under this trust?

14 MR. SAWCHAK: I'm not sure that the
15 trustee can do that.

16 JUSTICE KAGAN: Well, I thought -- I
17 mean, maybe I should know this, but when people
18 say contingent beneficiary, I'm assuming that
19 that means that she might never get the money
20 because the trustee might read her out of the
21 trust.

22 MR. SAWCHAK: Your Honor, no. I think
23 that the term "contingent beneficiary" is more
24 often used to describe a situation where
25 someone needs to die or some other life event

1 needs to occur before the person becomes
2 eligible.

3 JUSTICE KAGAN: So what do you
4 understand the contingency to be with respect
5 to this particular trust? What is the
6 contingency?

7 MR. SAWCHAK: There is none. And that
8 is -- that is very much our point, is that the
9 Kaestners -- Your Honor -- that the Kaestners
10 were currently eligible for distributions.

11 JUSTICE KAGAN: And what -- what, if
12 anything, can happen to make the Kaestner not
13 get that distribution? Or do you think the
14 Kaestners are just going to get that
15 distribution?

16 MR. SAWCHAK: So the Kaestners could
17 have died during the years in question. But
18 living long enough to receive distributions is
19 not seen as a contingency.

20 JUSTICE KAGAN: The trustee cannot
21 change the beneficiaries?

22 MR. SAWCHAK: Correct, Your Honor.

23 JUSTICE KAGAN: Can the settlor change
24 the beneficiaries?

25 MR. SAWCHAK: No, my understanding is

1 not. So --

2 JUSTICE KAGAN: The beneficiaries are
3 the beneficiaries in your view?

4 MR. SAWCHAK: Right. And there are --
5 in the case --

6 JUSTICE KAGAN: So, unless they die,
7 they're going to get this money?

8 MR. SAWCHAK: They are -- they're
9 going to get this money eventually, unless they
10 die, that's right. So --

11 JUSTICE BREYER: In -- in what shares?
12 Is there -- do they get it -- is there a
13 definite share that they now get no matter what
14 in the future, or can the trustee change the
15 shares?

16 MR. SAWCHAK: There's --

17 JUSTICE BREYER: Or can anyone change
18 the shares?

19 MR. SAWCHAK: There's not a recital in
20 the trust agreement of any shares.

21 JUSTICE BREYER: No. Look, there are
22 five people. Two of them live in North
23 Carolina. The trust earns a million dollars in
24 a particular year.

25 Are the two in North Carolina each

1 entitled to \$200,000 eventually, or is it
2 possible they'll get less, or is it possible
3 they'll get more?

4 MR. SAWCHAK: It is possible that
5 they'll get less or more. There is not a pro
6 rata --

7 JUSTICE BREYER: Then how do you know
8 how much of the share of the trust's income in
9 that year, the million dollars, North Carolina
10 should tax?

11 MR. SAWCHAK: Pro rata.

12 JUSTICE BREYER: What do you mean, pro
13 rata?

14 MR. SAWCHAK: If there are five
15 beneficiaries, for example, and two of them are
16 North Carolinians.

17 JUSTICE BREYER: Yeah, yeah.

18 MR. SAWCHAK: Assuming that the trust
19 instrument doesn't include any division there.

20 JUSTICE BREYER: Yeah, yeah.

21 MR. SAWCHAK: Forty percent.

22 JUSTICE SOTOMAYOR: But then you --

23 JUSTICE BREYER: Ah. So then, if, in
24 fact, there are 100 beneficiaries and there is
25 a person who lives in North Carolina who

1 eventually will get 1 millionth of 1 percent,
2 North Carolina is entitled to tax 1 percent?
3 That's your -- that's your view, is that right?

4 MR. SAWCHAK: That -- Your Honor, I'm
5 not sure where you're getting the 1.

6 JUSTICE BREYER: Let me make it
7 simpler. There are five beneficiaries. One
8 lives in North Carolina. As it turns out, that
9 one in North Carolina gets \$3. The others get
10 \$999,997. But North Carolina does not tax \$3.
11 What it taxes is 20 percent or \$200,000.

12 Do I have my facts right?

13 MR. SAWCHAK: You do have those facts
14 right. And what makes that fair, remembering
15 that the standard here is fundamental fairness
16 under the due process part of Quill, is that,
17 during that period, those beneficiaries were
18 eligible for distributions and all the while --

19 JUSTICE SOTOMAYOR: But you're
20 changing the trust instrument, because you as a
21 state are saying the trust must give them
22 20 percent each, because, regardless of what
23 the terms of the trust are, I'm going to tax
24 you on that 20 percent even though you might
25 get none, even though you might get more.

1 You're still a trust, you're being
2 charged for 20 percent because you should have
3 given her 20 percent. That's really what
4 you're saying, isn't it?

5 MR. SAWCHAK: That -- you're right,
6 Your Honor, to say there is a -- assuming
7 nothing's in the trust instrument, there would
8 be a full --

9 JUSTICE SOTOMAYOR: No, there is
10 something in the trust instrument here. The
11 trust instrument says that the trustee has
12 absolute discretion to give her something or
13 nothing, to give three people -- I think
14 there's two or three children; I don't know how
15 many there are here, but let's assume there's
16 four of them, her and three children, for using
17 even numbers.

18 The trustee could choose to -- if she
19 had a disabled child, to give it all to the
20 disabled child, or to divide it among the three
21 because she's very rich and they're not. The
22 trustee has a lot of discretion.

23 But you, the state, are changing the
24 terms of the trust instrument in saying each of
25 them must still pay 25 percent.

1 MR. SAWCHAK: That is correct, that
2 nothing else appearing, we make the pro rata.
3 And here's why that's fair. First of all,
4 throughout the period in question, those people
5 had true ownership of the accumulating assets.

6 Secondly, also essentially on a pro
7 rata basis, North Carolina is protecting each
8 of them.

9 CHIEF JUSTICE ROBERTS: You're not
10 taxing any of those people. You're taxing the
11 trust, right?

12 MR. SAWCHAK: We are taxing at the
13 trust level. Of course, the -- the trust
14 income fundamentally under trust law belongs to
15 them.

16 CHIEF JUSTICE ROBERTS: What do you do
17 about the problem I understand Justice Breyer's
18 question to be getting at, which is other
19 jurisdictions? Is there a -- an established
20 way of allocating the tax burden? You know, if
21 you have income from two states, they usually,
22 you know, divvy it up according to some
23 formula.

24 In the situation where you get 3 -- \$3
25 goes to North Carolina and the other number

1 goes somewhere else, if those other
2 jurisdictions want to tax the trust on those
3 same funds, is there a mechanism for allocating
4 that?

5 MR. SAWCHAK: There is, Your Honor.
6 Under Section 105-160.4 in North Carolina,
7 which is the credit statute, North Carolina
8 accords a credit for taxes paid to other
9 states, and I should --

10 JUSTICE GINSBURG: Does it have to?

11 MR. SAWCHAK: I'm sorry?

12 JUSTICE GINSBURG: Does it have to to
13 be constituted --

14 MR. SAWCHAK: There would come a point
15 where the second element of Quill could become
16 problematic in the absence of a credit.

17 I'd like to point out what the
18 propositions are on the other side --

19 JUSTICE BREYER: From the Chief's
20 question, I mean, yes, you -- you take if it's
21 other states. Now it happens that each state
22 -- each state wants to tax the same way you do,
23 and what happens?

24 MR. SAWCHAK: The pro rata would come
25 directly -- in a -- in a situation where,

1 imagine, all 50 states had the same scheme --

2 JUSTICE BREYER: Uh-huh.

3 MR. SAWCHAK: -- obviously, there
4 would be beneficiary --

5 JUSTICE BREYER: They don't all have
6 the same scheme. One of them taxes on the
7 basis of the money that the person who lives in
8 their state actually gets, and it turns out
9 that that person gets 80 percent of the income.
10 But the North Carolina person gets 3 percent.
11 What happens?

12 MR. SAWCHAK: In a situation where --
13 are you assuming in your question, Your Honor,
14 that distribution -- actual distributions have
15 occurred?

16 JUSTICE BREYER: Some states take on
17 the basis of actual distributions. Other
18 states have other ways of doing it. Some might
19 tax the trust on the basis of the fact that all
20 the administrators and the tax trustee and
21 everybody else is in New York. Okay?

22 There are many different ways. How do
23 they figure it out? Do they all meet and
24 figure it out? What happens? I'm just
25 curious.

1 MR. SAWCHAK: They don't meet to
2 figure it out. There are credit statutes in
3 most of the states that accord a credit. I'd
4 point out also, where actual distributions
5 occur, the trust level itself gets a
6 deduction -- this is through the incorporation
7 of Section 662 of the federal code -- for the
8 distributed amounts.

9 I'd like to draw attention, if I
10 might, to what the propositions are, first of
11 all, that the state supreme court founded us
12 on, and, secondly, what my friend is arguing,
13 because part of the attraction of what North
14 Carolina's doing here is verified by the
15 problems with -- with mandating under the Due
16 Process Clause a different approach.

17 First of all, the state supreme
18 court's reasoning was -- pages 13a and 18a of
19 the petition appendix -- beneficiary contacts
20 categorically don't count. Beneficiaries are
21 strangers to the trust income of which they are
22 the true owners under trust law.

23 Second, page 51 of the red brief, my
24 friend's proposition is that only trustee
25 contacts or trustee-related contacts, in terms

1 of the place of administration, count. That is
2 a recipe for tax avoidance.

3 The Fielding case that this Court has
4 on a petition, 18-664, is a graphic example.
5 Faribault Foods was a major Minnesota company,
6 was about to make a huge distribution of
7 profits to the beneficiaries. On the eve of
8 that distribution, the trustee was replaced
9 with a Texas trustee, a state which has no
10 state income tax, as I'm sure the Court knows.
11 And the trust, so far, has successfully taken
12 the position in Fielding that trustee contacts
13 are all that count.

14 JUSTICE GORSUCH: And, counsel, along
15 those lines, if I'm -- if I'm understanding
16 your position correctly, because you think that
17 rule's inequitable, you'd have us overrule Safe
18 Deposit and Brooke, two decisions of this Court
19 that suggest that that's the correct rule, is
20 that right?

21 MR. SAWCHAK: Not overrule them, Your
22 Honor. They could be --

23 JUSTICE GORSUCH: Well, what would you
24 have us do with them if it's not overruling
25 them?

1 MR. SAWCHAK: Two things, Your Honor.
2 First of all, they can be distinguished in
3 terms of being property tax cases versus income
4 tax cases, because this Court --

5 JUSTICE GORSUCH: Let's say I don't
6 find that distinction particularly significant.
7 It's slicing the baloney a little too thinly.
8 Then what?

9 MR. SAWCHAK: Then we would be really
10 within the proposition of the due process part
11 of Quill, where these are decisions that have
12 been superseded by the movement --

13 JUSTICE GORSUCH: Right. You're --
14 you're asking us to overrule them. I mean,
15 it's a polite way of saying overrule, isn't it?

16 MR. SAWCHAK: They've probably,
17 frankly, already been laid aside by other -- by
18 the due process decisions, as this Court's
19 noted in --

20 JUSTICE GORSUCH: But that's a --
21 that's a really nice way of saying overrule
22 them.

23 (Laughter.)

24 JUSTICE GORSUCH: Right?

25 MR. SAWCHAK: They've probably already

1 been --

2 JUSTICE GORSUCH: I've already been
3 overruled; we just haven't said so.

4 MR. SAWCHAK: That's probably right,
5 Your Honor, and let me say why that's --

6 JUSTICE GORSUCH: Okay. All right.
7 And -- and you'd have us overrule them in the
8 name of fundamental fairness, I think, is that
9 right?

10 MR. SAWCHAK: In the name of
11 fundamental fairness because --

12 JUSTICE GORSUCH: And -- and Justice
13 Breyer's problems notwithstanding, that -- that
14 fundamental fairness problem, we shouldn't take
15 into account?

16 MR. SAWCHAK: No, there are criteria,
17 a variety of criteria out there, and every one
18 of them --

19 JUSTICE GORSUCH: That's more
20 fundamentally fair than the existing rule of
21 this Court that's almost 100 years old?

22 MR. SAWCHAK: So query whether that
23 really is the existing rule, first of all.
24 Those are --

25 JUSTICE GORSUCH: Well, right, except

1 for the fact that we haven't overruled it, but
2 we really have. Okay.

3 But assuming we thought those were
4 still precedents of the United States Supreme
5 Court -- let's just spot me that for the
6 moment.

7 (Laughter.)

8 JUSTICE GORSUCH: You think it's more
9 fair to overrule them and proceed down the
10 track we've just illuminated with Justice
11 Breyer than to maintain them?

12 MR. SAWCHAK: Yes, Your Honor, for
13 several reasons. First of all, those are
14 physical-presence-based cases, which no longer
15 is the focus of due process analysis.

16 Secondly, the analysis in those cases
17 is completely unfaithful to the proposition of
18 trust law that beneficiaries are the true
19 owners of trust income.

20 JUSTICE SOTOMAYOR: By the way, may I
21 throw in a third case, Hanson?

22 MR. SAWCHAK: Yes, Your Honor.

23 JUSTICE SOTOMAYOR: Hanson, you would
24 be asking us to overrule, because I don't know
25 how you can tax somebody you have no

1 jurisdiction over, especially if they haven't
2 done anything like pay any money over or have
3 no contacts with the person in your state. All
4 the meetings were in New York.

5 So add a third case you want to
6 overrule.

7 MR. SAWCHAK: Certainly, there's no
8 need to overrule Hanson here for two --

9 JUSTICE SOTOMAYOR: Why? So how do
10 you -- the trustee is responsible for paying
11 this tax. You're dragging the trustee into
12 your court.

13 MR. SAWCHAK: The -- the taxed party
14 is the trust, first of all, not the trustee.
15 Two --

16 JUSTICE SOTOMAYOR: So how is the
17 trust in your state?

18 MR. SAWCHAK: Pardon me, Your Honor?

19 JUSTICE SOTOMAYOR: I thought the
20 trust is represented by the trustee. And the
21 trustee is not in your state.

22 MR. SAWCHAK: The -- the trust has its
23 presence --

24 JUSTICE SOTOMAYOR: It's not being
25 administered in your state.

1 MR. SAWCHAK: True, but its true
2 owner, its central figure, is in North
3 Carolina. Let me offer --

4 JUSTICE SOTOMAYOR: So why didn't we
5 say that in Hanson?

6 MR. SAWCHAK: So Hanson, first of all,
7 is a situation where the burden of
8 adjudication, by the way, not taxing, fell on
9 the person of the trustee. This Court in
10 Walden described --

11 JUSTICE SOTOMAYOR: The same thing
12 here. You're making the trustee liable for
13 paying the tax. You're doing exactly what
14 happened in Hanson.

15 MR. SAWCHAK: But it's not the
16 trustee's money. The trustee is entitled --

17 JUSTICE SOTOMAYOR: It wasn't in
18 Hanson either.

19 MR. SAWCHAK: Hanson is not a tax
20 case. The -- under this Court's decision in
21 Stone, the ultimate incidence of the tax, where
22 it will land, will be on the beneficiary. And
23 that makes all the difference for due process.

24 JUSTICE GINSBURG: Could North
25 Carolina on that basis impose a property tax on

1 the value of the trust assets because they
2 belong to the beneficiaries?

3 MR. SAWCHAK: Yes, Your Honor.

4 JUSTICE GINSBURG: You could -- you'd
5 impose a tax on all the property in -- in the
6 trust?

7 MR. SAWCHAK: If there is -- there
8 would be -- let me -- let me revise my answer
9 to say the analysis of property taxes for the
10 most part is more location-based than is the
11 analysis of income tax.

12 JUSTICE GINSBURG: But you said that
13 the beneficiaries are the true owners. It's
14 their property. So why not a property tax?

15 MR. SAWCHAK: So there would be an
16 argument for that, certainly, but that's not
17 this case.

18 If I may, I'd like to reserve the
19 balance of my time.

20 CHIEF JUSTICE ROBERTS: I'll afford
21 you additional rebuttal time.

22 MR. SAWCHAK: Thank you, Your Honor.

23 CHIEF JUSTICE ROBERTS: Mr. O'Neil.

24

25

1 ORAL ARGUMENT OF DAVID A. O'NEIL

2 ON BEHALF OF THE RESPONDENT

3 MR. O'NEIL: Thank you, Mr. Chief
4 Justice, and may it please the Court:

5 I'd actually like to begin where
6 Justice Ginsburg began because I think it
7 highlights one of the key features and critical
8 aspects of this case that the state's position
9 ignores and that dictates the outcome.

10 The first point is this was not really
11 the beneficiary's money during the tax years.
12 She didn't possess it or control it. She
13 didn't access it. She couldn't use it. She
14 couldn't buy anything with it, promise it to
15 someone else. She couldn't have any say in how
16 it was invested.

17 She didn't receive any of it, and she
18 had no guarantee that she would ever receive a
19 penny of it in North Carolina or anywhere else.

20 JUSTICE KAGAN: Was it the trustee's
21 money?

22 MR. O'NEIL: It was the trustee's
23 money.

24 JUSTICE KAGAN: He couldn't do any of
25 those things.

1 MR. O'NEIL: He is bound, of course,
2 by a fiduciary duty, but within those broad
3 limits, he does exercise the possession and
4 control that, as this Court has recognized for
5 decades --

6 JUSTICE KAGAN: He possesses it with a
7 fiduciary duty to -- to increase that money for
8 her.

9 MR. O'NEIL: He possesses it and
10 controls it with a duty to act out of loyalty
11 for a group of beneficiaries of which she is
12 part. And if we look at the actual control
13 that he exercised over the property and
14 contrast it with the beneficiary, it
15 demonstrates why the law treats him as the
16 owner. He can buy property with it. He can
17 sell it. He can incur liability based on how
18 he uses it. He can enter contracts.

19 JUSTICE KAGAN: So that she eventually
20 gets to enjoy it.

21 MR. O'NEIL: One of the fundamental
22 problems of this tax, as the Court noted in its
23 previous questioning, is that it's premised on
24 the prediction that she will receive this
25 money. But, in fact, at the time that this tax

1 was imposed, there -- that's unknown and
2 unknowable.

3 It's not known how many beneficiaries
4 there are. It's not known who will actually
5 receive the money. It's not known where they
6 will live when they receive the money, how many
7 people it's shared with.

8 JUSTICE ALITO: So -- so what if the
9 trust --

10 CHIEF JUSTICE ROBERTS: Well, but they
11 know -- they know what she's getting or has
12 gotten in a particular year. She knows
13 where -- where she lives in that year. The
14 hypotheticals that, well, she might not get
15 any, she might move somewhere else, those --
16 those are hypotheticals. For these tax years,
17 you know where she is and you know what she's
18 gotten.

19 MR. O'NEIL: She's gotten zero, and
20 that's a critical point for this case. She
21 received zero money during these tax years.
22 And she had no guarantee that she would ever
23 receive them.

24 Now, if and when she actually does
25 receive this property --

1 JUSTICE KAGAN: Well, she's seeing a
2 substantial asset of hers increase in value in
3 the bank, and even if she can't touch it right
4 now, she's getting richer and richer because of
5 it, and that's influencing her life choices
6 because she knows she's eventually going to
7 enjoy that money.

8 And if you compare her to -- I mean,
9 where -- who are the three states that could
10 tax this? One is the state where the trustee
11 lives, one is the state where the trust
12 administration is, and one is the state where
13 the beneficiary is. The person who is getting
14 the benefit of this increase in the asset is
15 only the beneficiary.

16 MR. O'NEIL: Justice Kagan, the
17 premise of the question is that this is a
18 source of wealth for her. That is not known at
19 this point. She does not have a current
20 interest in this trust asset.

21 As the brief for the American College
22 of Trusts --

23 JUSTICE KAGAN: Would your position be
24 different if she were -- if -- if the -- if the
25 trustee did not have this discretion as to

1 shares?

2 Suppose that the -- the trust
3 instrument simply said, here are the five
4 beneficiaries. The trust will be distributed
5 pro rata. You know, if one dies, then it will
6 be distributed pro rata as to the other four.

7 But -- but -- but the beneficiaries
8 all know that they're going to get a fifth of
9 this money. Would your answer be different?

10 MR. O'NEIL: If the trust instrument
11 gave her a vested current right to the income,
12 then we wouldn't --

13 JUSTICE KAGAN: Not a current right.
14 She's going to have to wait until she's
15 whatever years old, 30, 40, whatever. She
16 can't pull the money now. But she's going to
17 get the money one day.

18 MR. O'NEIL: No, that -- that case
19 would not be different because it would still
20 be based on the speculative possibility that
21 she will ultimately receive the money.

22 JUSTICE BREYER: We weren't
23 speculative; that is, imagine it's not. All
24 right? I wonder -- and I'm asking this not as
25 an argument or one way or the other. I just

1 wonder how it works.

2 The trust gets an extra million in
3 year 1. She will get a distribution of, say, a
4 million in year 30. Now just -- I think, as
5 Justice Kagan said, she is now worth more money
6 than she was before, but she's not worth more
7 money by a million.

8 She is worth more money by a million
9 discounted by her getting it 20 or 30 years in
10 the future. That's why we have interest rates,
11 that's why we have bank accounts, et cetera.

12 So how does it actually work?

13 MR. O'NEIL: She is only worth more
14 money that's measured by the accumulation of
15 the trust if she is guaranteed to receive that
16 income.

17 JUSTICE BREYER: Well, let's imagine
18 she is. I still have -- you may not know,
19 maybe nobody's ever looked into this question
20 -- but -- but I'm imagining that she is going
21 to get it eventually. Maybe this is an easier
22 case because she isn't, but I imagine that she
23 definitely is.

24 Still, there is a problem. Of course,
25 it will earn interest. But they'll tax the

1 interest each year. So she's not worth now
2 more. Try to sell it to somebody. A million
3 dollars in the future is -- 20 years from now
4 is worth a lot less than a million dollars --

5 MR. O'NEIL: I think it -- it's very
6 difficult --

7 JUSTICE BREYER: How does tax law deal
8 with this?

9 MR. O'NEIL: Tax law deals with it
10 based on the principle of possession, control,
11 and receipt. That is how income tax works.

12 You are taxed when you receive the
13 income. So in your --

14 JUSTICE KAGAN: But, I mean, just what
15 is the theoretical justification for, say,
16 all -- all of these measures are imperfect.
17 And -- and you can say with respect to any of
18 these states, well, why do they get to tax
19 undistributed income? But what you're saying
20 is that, as between two states, Connecticut and
21 North Carolina, we should put the taxing
22 authority for that undistributed income growth
23 in Connecticut. And -- and I have to say that
24 just doesn't make a whole lot of sense to me.

25 The trustee is not going to be the

1 beneficiary of that income growth. Whatever
2 income growth it is and however much it's
3 discounted, the beneficiary, who's getting
4 richer, is sitting in North Carolina.

5 MR. O'NEIL: Again, the premise is
6 that she's getting richer, which assumes that
7 she will get --

8 JUSTICE KAGAN: She's definitely
9 getting more richer than the trustee is. The
10 trustee's bank account is not changing.

11 MR. O'NEIL: The only thing we know at
12 time X when this tax is imposed is that the
13 trustee possesses and controls the property.
14 As you pointed out, he has a duty of loyalty,
15 so he can't spend it on himself and he can't
16 give it to his friends.

17 But, within those limits, he is the
18 owner of the property. We do not know that the
19 beneficiary will ever actually receive that
20 property.

21 JUSTICE KAVANAUGH: If -- I thought we
22 didn't need to answer the question raised by
23 Justice Kagan's previous hypothetical, and just
24 raised by you, which is, if we did know, in
25 other words, if it were guaranteed or certain,

1 that might or might not be a different case.

2 But this case is one where we don't
3 know based on the nature of the trust
4 contingent or discretionary beneficiary, and
5 for that case, the answer I thought you were
6 arguing should be that the state where the
7 beneficiary resides cannot tax, but we could
8 leave open the question raised by Justice
9 Kagan's hypothetical.

10 Is that not right?

11 MR. O'NEIL: You -- you could. The
12 case here involves one in which -- a trust
13 agreement in which the trustee has absolute
14 discretion to distribute this property as he
15 sees fit and where he also has discretion to
16 extend the trust into a new trust if he
17 believes that the beneficiary would --

18 CHIEF JUSTICE ROBERTS: Well, but if
19 we leave --

20 JUSTICE GINSBURG: Doesn't that
21 require her consent? Isn't that --

22 MR. O'NEIL: Under New York law, it
23 would not require her consent. In fact, he did
24 consult with her, because, as part of his
25 duties to ensure -- to determine whether she

1 was prepared to receive the money, he consulted
2 with her, but, under New York law, the
3 decanting statute does not require the consent
4 of the beneficiary.

5 JUSTICE GINSBURG: But if she decided
6 at age 40 she wanted -- she wanted all the
7 property?

8 MR. O'NEIL: If she decided that, then
9 it would be in the trustee's discretion to
10 decide whether, acting out of loyalty with her,
11 for her, and in good faith, whether her
12 interests were better served by an extension of
13 that trust and a decanting of that property
14 into a new trust.

15 JUSTICE KAVANAUGH: What states do
16 something like this? In other words, where
17 it's discretionary or contingent beneficiary
18 and impose the tax where the trust's trustee is
19 in another state?

20 MR. O'NEIL: So, Justice Kavanaugh,
21 you are correct about that. There are
22 currently three states that use the presence of
23 a beneficiary -- of a contingent beneficiary as
24 the sole factor on which they will tax the
25 accumulated income of a trust.

1 As you pointed out, Tennessee has
2 eliminated its income tax as of 2021. Georgia
3 may or may not do it. Practitioners disagree
4 about that. So that leaves North Carolina
5 alone as the state that actually imposes a full
6 tax on the accumulated income of a trust
7 based on -- based only on the fact of a
8 contingent beneficiary.

9 JUSTICE SOTOMAYOR: You're adding
10 differently than I am. Tennessee's done away
11 with income tax. Which was the other one?

12 MR. O'NEIL: Georgia and North
13 Carolina.

14 JUSTICE SOTOMAYOR: I thought there
15 were four states. Am I wrong?

16 MR. O'NEIL: We believe there are
17 three.

18 JUSTICE SOTOMAYOR: So just the --

19 MR. O'NEIL: We believe there are
20 three.

21 JUSTICE KAGAN: Mr. O'Neil, do you
22 think that New York can tax this income?

23 MR. O'NEIL: For periods of time in
24 which the trust was administered in New York,
25 yes, New York could tax the income.

1 JUSTICE KAGAN: So the state of
2 administration can tax the income?

3 MR. O'NEIL: Yes, Justice Kagan.

4 JUSTICE KAGAN: And the state of the
5 trustee can tax the income?

6 MR. O'NEIL: That's correct.

7 JUSTICE KAGAN: And the only state
8 that can't tax the income is the state that is
9 providing services to the person who's going to
10 benefit from the income growth?

11 MR. O'NEIL: The state where the
12 beneficiary resides is really no differently
13 situated from any other state. The fact that
14 the beneficiary lives there is just -- it's --
15 it's advantageous from the perspective of the
16 trustee. The beneficiary can move from state
17 to state to state during each of these years
18 and nothing about the trust administration
19 would change.

20 JUSTICE KAGAN: But, meanwhile, it's
21 -- I mean, well, if she moves from state to
22 state to state, then each state for those
23 particular years where she lives in the state
24 can tax it, but eventually she's going -- and I
25 know you say, well, maybe she won't, and -- but

1 you answered my hypothetical, where you said,
2 even if there were no contingency, the state of
3 residency couldn't tax.

4 For these tax years, North Carolina is
5 providing services to a person who and the only
6 person who is going to benefit from the income
7 growth of this trust.

8 MR. O'NEIL: First, I want --

9 JUSTICE KAGAN: And, again, nothing's
10 perfect. But as between those -- as among
11 those three choices, I would think North
12 Carolina has by far the greatest interest in
13 taxation.

14 MR. O'NEIL: First, I want to make
15 sure I was clear that if there is no
16 contingency, if the beneficiary has an absolute
17 right to the income in a particular year, the
18 state of residence absolutely can tax that.

19 JUSTICE KAGAN: I wasn't talking about
20 contingency. And you -- you keep changing it,
21 as like I have a right to the income. But I'm
22 -- I'm presuming that nobody can touch this
23 corpus for a while, for five years, for 10
24 years, but, eventually, you said, if somebody,
25 you know, somebody was going to be able to

1 access both the income and maybe the body of
2 the trust, and still North Carolina couldn't
3 tax it, notwithstanding that Connecticut and
4 New York can tax it, where, you know, they just
5 have some officers who are pushing a lot of
6 paper.

7 But all the benefit of this trust is
8 going to this person who lives down in North
9 Carolina.

10 MR. O'NEIL: I think you actually have
11 to look at what benefits are being provided.
12 So during her tax -- the tax years, during the
13 years in which she's living in North Carolina,
14 she is paying income tax on all of the money
15 she actually receives for the benefit of being
16 a North Carolina citizen, just as every other
17 citizen does.

18 Now she is not being taxed on income
19 that she doesn't have, that she can't demand,
20 that she has no right to.

21 JUSTICE KAGAN: Yeah, Mr. O'Neil, if I
22 can say, I mean, suppose she's making \$100,000
23 a year. A person in North Carolina who's
24 making \$100,000 a year and a person in North
25 Carolina who's making that exact same amount of

1 income and has a \$20 million trust are really
2 in two different positions.

3 MR. O'NEIL: That rationale, though,
4 it's not limited to trusts. Of course, you
5 could have a child whose parent -- who has a
6 very wealthy parent in another state and you
7 could say, well, that child is differently
8 situated from one that does not have family
9 resources of that kind.

10 But, in the eyes of the law, they are
11 not in any different situation. Neither one of
12 them can demand that money. Neither one of
13 them actually gets it. And it would not allow
14 the state where the beneficiary lives to go and
15 tax a parent who has a large amount of income
16 because it would someday be destined for the
17 kid or --

18 JUSTICE ALITO: But I thought this
19 case was simpler than your argument seems to be
20 making it. I thought this was a case about a
21 state imposing a tax on someone for money that
22 that person may never get. And if -- and if
23 the person ever gets some money, we'd have no
24 idea how much that money would be. Isn't that
25 what this case is about?

1 MR. O'NEIL: So that's exactly right.
2 I was -- that's exactly right.

3 JUSTICE GINSBURG: What -- what is the
4 uncertainty, other than she has to stay alive?

5 MR. O'NEIL: She has to stay alive.
6 The assets could be dissipated because of poor
7 investments. The trustee could decide that
8 she's not ready to receive the money. The
9 trustee could decide that the money should go
10 to some other beneficiary.

11 There are a number of ways in which --

12 JUSTICE GINSBURG: I thought she was
13 the first-line beneficiary, the primary
14 beneficiary?

15 MR. O'NEIL: She's among a group of
16 primary beneficiaries that at the point in time
17 of the tax years included her and her children.
18 Of course, something could happen to her
19 children, and the money would then need to be
20 devoted to that purpose.

21 But, Justice Ginsburg, even if it is
22 very likely, even if we assume it's very likely
23 that this money will go to her, it is not hers
24 until it goes to her. And when it goes to
25 her -- and I think this is a critical part of

1 -- of the response to the state here, when it
2 goes to her, the state is free to tax it. And
3 it can tax it not only --

4 JUSTICE KAVANAUGH: She might be in a
5 different state when it goes to her. That's
6 part of your point too, isn't it?

7 MR. O'NEIL: She may well live in a
8 different state. And if she lives in a
9 different state --

10 JUSTICE KAVANAUGH: In other words,
11 when she gets the benefit of the money, if she
12 ever gets the benefit --

13 MR. O'NEIL: Right.

14 JUSTICE KAVANAUGH: -- if the
15 beneficiary ever gets the benefit, they might
16 not live in North Carolina.

17 MR. O'NEIL: That's exactly right.
18 And if she no longer lives in North Carolina,
19 then North Carolina, with no legitimate basis
20 whatsoever, will have been -- have taken
21 property from the corpus of the trust.

22 CHIEF JUSTICE ROBERTS: You -- do I
23 understand you to say that the trust can be
24 taxed in the years -- by North Carolina in the
25 years when it actually distributes money to the

1 North Carolinian?

2 MR. O'NEIL: That's correct.

3 CHIEF JUSTICE ROBERTS: Well, but it
4 won't happen that way, because the North
5 Carolina resident is going to be taxed on that
6 money by North Carolina as income.

7 MR. O'NEIL: So, if the question is
8 can the beneficiary be taxed on the
9 distribution in the year it's actually made,
10 the answer is yes.

11 CHIEF JUSTICE ROBERTS: Sure. Right.

12 MR. O'NEIL: Can the trust? No, at
13 that point, it won't be trust property. At
14 that point, it will be the beneficiary's
15 property.

16 And this -- you know, the federal
17 government has the same issue. U.S. citizens
18 can have trusts that are located abroad, and
19 what the federal government does is impose a
20 throw-back tax so that when the beneficiary
21 actually receives the money, the beneficiary
22 can be taxed not only on that distribution but
23 also on -- on income that had accumulated in
24 previous years and that the trustee did not pay
25 taxes on.

1 JUSTICE KAVANAUGH: And throw-back
2 taxes are -- are permissible, constitutional?
3 You're not challenging those in any way?

4 MR. O'NEIL: We are not. We believe
5 throw-back taxes are permissible because they
6 are taxing the beneficiary resident on money in
7 their hands at that point.

8 JUSTICE BREYER: Are there other
9 instances in tax law where a resident of state
10 B -- state A, is taxed by state A, on the basis
11 of an increase of value of property that is
12 located in state B?

13 In other words, I own some property, a
14 piece of land in New Hampshire or let's say
15 Maine, and I am a resident of Florida or North
16 Carolina. Can North Carolina impose a tax upon
17 me because the land that I now own in Maine is
18 worth more this year than it was last year?

19 MR. O'NEIL: The state where the --
20 where the owner lives in that hypothetical
21 could tax on the income received from the
22 property.

23 JUSTICE BREYER: No, I understand.
24 I'm not asking that.

25 MR. O'NEIL: Yeah.

1 JUSTICE BREYER: I'm asking whether --
2 to repeat what I said -- a North Carolina
3 resident owns a piece of land in Maine. This
4 year, that piece of land is worth more than it
5 was last year.

6 Can North Carolina tax that increase
7 in value?

8 MR. O'NEIL: If the North Carolina
9 resident has a current right --

10 JUSTICE BREYER: Well, of course, she
11 has a current right to go up to Maine and sit
12 on her own land.

13 MR. O'NEIL: Well, under this Court's
14 decision, North Carolina can't tax property
15 that's located in a different state. I take
16 your question to be --

17 JUSTICE KAGAN: Can't tax real
18 property.

19 MR. O'NEIL: Can't tax real property.
20 So --

21 JUSTICE KAGAN: Right, but suppose
22 somebody owns a stock portfolio.

23 MR. O'NEIL: Yes. So the answer --

24 JUSTICE KAGAN: Now mostly people --
25 you know, mostly we wait until somebody sells

1 the stock.

2 MR. O'NEIL: That's correct. But we
3 can --

4 JUSTICE KAGAN: But we could --

5 MR. O'NEIL: We could impose --

6 JUSTICE KAGAN: -- do it otherwise.

7 MR. O'NEIL: A state could enact a
8 wealth tax if the -- if the person that they
9 are taxing has a current vested right to that
10 and it's something that they could sell. It's
11 alienable. In that instance, the state could
12 impose a tax for the wealth that is in the
13 resident's hand.

14 And that's the situation in the
15 Commonwealth versus Stewart case that the state
16 relies on, the 1940 Pennsylvania Supreme Court
17 decision that the state relies on. That is a
18 tax on the resident for property in the
19 resident's hands.

20 And that is a fundamentally different
21 situation from the tax here, which is a tax on
22 the trustee, who is a non-resident, for income
23 that the beneficiary has not received.

24 So the short answer --

25 JUSTICE SOTOMAYOR: I thought in your

1 brief you conceded that if this trust was a
2 demand trust, the beneficiary could say: I
3 want X, that that could be taxed by North
4 Carolina?

5 MR. O'NEIL: That's correct, whether
6 she actually receives it or not.

7 JUSTICE SOTOMAYOR: So the thing that
8 Justice Kavanaugh and Justice Alito were
9 reserving, and I assume Justice Kagan, was on
10 the question of what happens if she is a
11 guaranteed distributor -- distributee, meaning
12 she can't call it today, but at age 40 or at
13 the end of the trust life, at some point, she's
14 going to be the 100 percent owner or going to
15 be a fixed 10 percent owner, whatever it might
16 be, they're saying we should reserve on that
17 question?

18 MR. O'NEIL: I think that would be a
19 different case. I think -- I think the -- the
20 trust instrument here is important to the facts
21 of this case and to the outcome.

22 Here, the trustee has absolute
23 discretion, and what that means is that she is
24 not guaranteed ever to receive --

25 JUSTICE SOTOMAYOR: All right. So

1 give me the argument the other way. Let's
2 assume she was the 100 percent distributee at
3 the end of the trust life, which will be in
4 five or 10 years, or she's 20 percent or she's
5 30 percent, whatever it is.

6 Why do you think the state might have
7 more purchase to tax then?

8 MR. O'NEIL: If the beneficiary had a
9 vested right in a certain percentage of the
10 trust, then we would treat her as having a
11 current interest in that trust.

12 So I would say they still could not
13 tax her for the income, but that's a situation
14 in which -- that would implicate Justice
15 Breyer's question where, if she has a current
16 right to that, the state could, if it wanted,
17 impose a wealth tax and tax her for that
18 portion of it because that would be money that
19 is in her hands currently and that she could
20 sell, she could promise to someone else.

21 But this trust agreement is critically
22 different in two respects. First, her receipt
23 of anything is dependent on the trustee's
24 decision to give it to her, period.

25 Second, she had -- has no right to

1 promise, sell, or do anything with the -- with
2 the possibility that she may someday receive
3 these assets. This is a spendthrift trust, and
4 that means she has no right that she can sell
5 or alienate. And that makes it fundamentally
6 different from a situation in which a
7 beneficiary has a current vested right that the
8 state could -- if it -- if it passed a law that
9 allowed that, that the state could tax through
10 a -- through a wealth tax.

11 I'd like to just focus, if I could, on
12 the -- on the point of the throw-back tax
13 because I do think -- I do think it is an
14 answer to why -- to the state's concern about
15 all of the potential loss of revenue that it
16 may -- may -- may lose out on here.

17 If and when this money is actually
18 distributed to the beneficiary, if she is a
19 North Carolina resident at that time, the state
20 can get all of this income tax back by taxing
21 the beneficiary.

22 JUSTICE KAVANAUGH: Well, but they're
23 assuming she or people in that position are
24 going to move before that happens.

25 MR. O'NEIL: States have --

1 JUSTICE KAVANAUGH: To -- to pick up
2 on --

3 MR. O'NEIL: Right.

4 JUSTICE KAVANAUGH: -- Justice Kagan's
5 point.

6 MR. O'NEIL: Yeah.

7 JUSTICE KAVANAUGH: That's -- that's
8 the issue, right?

9 MR. O'NEIL: Well, state --

10 JUSTICE KAVANAUGH: The real-world
11 issue is she's not going to be around in North
12 Carolina or -- and I don't want to talk about
13 particular people, but people in this position
14 won't be around in the state because they'll go
15 to Florida or Texas or Nevada.

16 MR. O'NEIL: So states have all the
17 tools they need to address that. There are
18 anti-abuse doctrines in the tax laws that will
19 look through and discount a sham change in
20 residency.

21 JUSTICE KAVANAUGH: A sham change, but
22 a lot of people can change residence, as you
23 well know. That's the -- I mean, states
24 actually advertise on that basis.

25 MR. O'NEIL: Including --

1 JUSTICE KAVANAUGH: Come to our state.
2 Don't pay the income tax.

3 MR. O'NEIL: Right. And, in fact,
4 North Carolina --

5 JUSTICE KAVANAUGH: That's what North
6 Carolina's worried about.

7 MR. O'NEIL: Right. North Carolina
8 itself advertises on the basis of its low tax
9 burden.

10 If it's a true change in residency,
11 Justice Kavanaugh, that is not a tax -- a
12 trust-specific issue. People move from state
13 to state all the time, and when they do, there
14 are tax consequences, but we don't call that a
15 judicial tax shelter; we call that federalism.

16 That is basically the interstate
17 federal --

18 JUSTICE BREYER: Well, the interesting
19 question here -- I guess we don't -- and it's
20 -- this doesn't happen, it hasn't happened that
21 way, except maybe in North Carolina -- no, not
22 even North Carolina.

23 State A decides that its current
24 residents will be taxed on the basis of their
25 wealth, and it includes in wealth increased

1 value of out-of-state property.

2 Now we know, if it's real property,
3 they can't do it. But what about intangible
4 property?

5 MR. O'NEIL: If --

6 JUSTICE BREYER: And it could happen,
7 you know. States could decide we're going to
8 impose wealth taxes. They could.

9 And then we'll be faced with that
10 problem. But your view is that is not this
11 case because this case, we don't know exactly
12 what the beneficiary will get, when she'll get
13 it, or perhaps even if she will get it. Do I
14 -- have I summarized that correctly, so I can't
15 reach the really interesting legal question?

16 MR. O'NEIL: You -- you have that --
17 you have that correct. It's also different
18 from this case because, you know -- and this is
19 another key point that the state overlooks --
20 the tax here was not on the beneficiary.

21 The tax here was on the trustee. The
22 state's laws on this are crystal-clear. The
23 statute at issue says "the fiduciary shall pay
24 the tax." In -- in a section that --

25 JUSTICE KAGAN: Well, the fiduciary

1 shall pay the tax, but wouldn't the state say
2 that the tax is on the trust itself?

3 MR. O'NEIL: The state could say that,
4 but -- but that ignores the practical operation
5 of the tax. If this tax is not paid, the state
6 is going to come after the trustee, not the
7 beneficiary, for the consequences.

8 If, as happened here, the trustee
9 believes that the tax is unlawful, then the
10 trustee needs to hire a lawyer, defend against
11 the liability, subject himself to discovery,
12 and, in general, as the brief for the Chamber
13 of Commerce explains, subject himself to all of
14 the same burdens that a defendant does in a
15 civil case. It is the equivalent of receiving
16 a summons in a civil action.

17 CHIEF JUSTICE ROBERTS: Does it matter
18 to the trustee in administration of the trust
19 where the money's going to go?

20 MR. O'NEIL: The trustee has a duty of
21 loyalty to act in the best interests of the
22 trust -- of the trust beneficiaries.

23 CHIEF JUSTICE ROBERTS: No, but, I
24 mean, let's say one of the children is in North
25 Carolina; the other's in Pennsylvania. Are

1 they in any way treated differently by the
2 trustee given their state of residence?

3 MR. O'NEIL: No, no. The trustee does
4 not care where the beneficiaries live. He has
5 no control over where they live. And that's
6 another reason why the forum here, North
7 Carolina, really just is not relevant to the
8 operation of the trust, the trustee's duties,
9 or the way in which he administers it.

10 Again, the beneficiaries here could
11 have moved to a whole range of different
12 states, and nothing about the operation of this
13 trust or the relationship among the parties
14 would change.

15 JUSTICE KAGAN: Could -- could you
16 just say a few words as to what the theoretical
17 justification is for why New York and
18 Connecticut can tax the growth of these assets?

19 MR. O'NEIL: This Court supplied the
20 theoretical basis for that in the Greenough
21 case, and the basis is that, for -- for tax
22 purposes and for viewing who is the actual
23 owner, control and possession equals ownership.

24 So the state where the trustee owns
25 the property, in this case Connecticut,

1 protects the trustee's ownership of those -- of
2 that property. And -- and, in addition,
3 states, including North Carolina, provide that
4 the courts are open to the trust in the state
5 in which it's administered.

6 So the -- the trustee has access to
7 the courts. The courts can adjudicate the
8 rights among the parties. And that is a state
9 interest that justifies the taxation of the
10 trust property.

11 JUSTICE GINSBURG: You say there are
12 two states, the one where the trustee resides
13 and the one where the trust is administered.

14 MR. O'NEIL: That's correct, Justice
15 Ginsburg. I'd like to say --

16 JUSTICE GINSBURG: Could both impose a
17 tax? And I guess they have credit mechanisms.

18 MR. O'NEIL: That would be a separate
19 -- that's a separate Commerce Clause problem,
20 whether there are -- there's allocation,
21 whether they're internally inconsistent.

22 I would -- I would point out that, in
23 fact, North Carolina says it provides
24 allocation. It -- it provides a credit only
25 for source income in a different state. So, in

1 fact, if another tax -- state taxed this trust
2 as a resident, North Carolina would not credit
3 that property.

4 JUSTICE KAVANAUGH: What about your
5 colleague's argument that the precedent which
6 you say would have to be upended here has
7 already been overturned in some fashion or
8 another? Can you respond to that?

9 MR. O'NEIL: Safe Deposit, Brooke,
10 Guaranty Trust, all turn on the same principle
11 of actual possession and control and look at
12 the reality of the relationships among the
13 trust -- trust participants. They are every
14 bit as valid today as they were then.

15 The -- the -- the argument in those
16 cases was we can tax the beneficiary as if she
17 owned the property because she really did. And
18 the -- and the Court said, using the same
19 principles of trust law that apply today, she
20 really -- the beneficiary really isn't the
21 owner of the property there, so we're not going
22 to allow taxation of that.

23 Before I sit down, I would like to
24 respond very briefly to the state's argument
25 about Wayfair. Wayfair is irrelevant to this

1 case except in one important respect. An
2 accurate analogy to the facts of Wayfair shows
3 why the tax here is unconstitutional. In
4 Wayfair, the state pointed to the taxpayer's
5 own forum-directed conduct and said that was
6 sufficient.

7 In this case, what the state is doing
8 is pointing not to the taxpayer's own conduct
9 but to the conduct of some other person. And
10 so, if North Carolina were right in its
11 position today, it would mean that any one of
12 the C corporations in Wayfair could have been
13 taxed anywhere that a beneficial shareholder
14 lived based solely on the fact of the -- of
15 their residence. And that is not the rule that
16 this Court has applied.

17 This case presents a straightforward
18 and textbook application of the settled rule
19 that the unilateral activity of a third-party
20 does not create jurisdiction. This Court has
21 resolved the question presented twice, both in
22 Safe Deposit and in the canonical case of
23 Hanson v. Denckla, Justice Sotomayor, as you
24 pointed out, and there is no reason to
25 reconsider those cases here. The Court should

1 affirm them.

2 CHIEF JUSTICE ROBERTS: Thank you,
3 counsel.

4 Five minutes, Mr. Sawchak.

5 REBUTTAL ARGUMENT OF MATTHEW W. SAWCHAK
6 ON BEHALF OF THE PETITIONER

7 MR. SAWCHAK: Thank you, Your Honor.

8 Just to begin with first principles,
9 this is a due process challenge to a state tax
10 on the proposition that beneficiary contacts,
11 beneficiary residency categorically doesn't
12 count.

13 Now many members of the Court have
14 raised questions about the amount that can be
15 taxed. That's fundamentally a point under the
16 second element of Quill. And as this Court
17 said in -- in MeadWestvaco, as long as there
18 are minimum connections to the state, whether
19 the amount that could be taxed is -- is a
20 separate inquiry. All that really the Court
21 might have occasion to do here is to reject the
22 proposition of the state supreme court that
23 beneficiary contacts don't count.

24 After all, this is the first trust tax
25 case since 1947. It might be well to leave to

1 the state courts to sort out complexities under
2 the second element of Quill.

3 JUSTICE GINSBURG: What do you do with
4 Mr. O'Neil's canonical case of Hanson against
5 Denckla?

6 MR. SAWCHAK: Two major points I'd
7 make about Hanson, Your Honor. First of all,
8 Hanson is a situation where the burdens fell on
9 an out-of-state party, namely, Wilmington
10 Trust, the out-of-state Delaware trustee.

11 Here --

12 JUSTICE GINSBURG: What kind of burden
13 was on the trustee? That was a fight between
14 three sisters for the ownership of the
15 settlor's assets.

16 MR. SAWCHAK: It was, Your Honor. But
17 the point that ended up driving the Rule 19
18 analysis in that case was effectively or it was
19 exactly an adjudicative jurisdiction challenge.

20 JUSTICE GINSBURG: I thought that was
21 just because Florida decided to make the -- the
22 Delaware trustee an indispensable party.

23 MR. SAWCHAK: That's correct. And
24 what drove the indispensability analysis and
25 what my friend cites is the internal part of

1 the decision where adjudicative jurisdiction of
2 the trustee is -- is rejected.

3 And, here, the burden of taxation
4 falls not on an out-of-state party. The
5 economic burden falls on an in-state party,
6 100 percent of it. The North Carolina
7 Kaestners, under Stone, they are the parties
8 who ultimately feel the pinch of taxation. And
9 that's a fundamental distinction of Hanson.

10 In addition, I'd point out that on
11 pages 247 and 252, the Court in Hanson twice
12 distinguished between adjudicative jurisdiction
13 and other forms of jurisdiction. Choice of law
14 and also distinguishing the taxing cases.

15 So Hanson is distinguishable both in
16 terms of this fundamental reality of who's
17 burdened and also concerning what the burden
18 is.

19 JUSTICE GORSUCH: Well, we've never
20 suggested, though, that tax jurisdiction
21 exceeds adjudicative jurisdiction, have we?
22 It's usually the other way around.

23 MR. SAWCHAK: So the Court, I don't
24 think, has made a directional statement one way
25 or the other. The nature --

1 JUSTICE GORSUCH: Are you aware of a
2 case where we've said that tax jurisdiction is
3 broader than adjudicative jurisdiction?

4 MR. SAWCHAK: I'm not. On the other
5 hand, nor have I seen a case where the Court
6 has said the opposite thing. But, in Hanson,
7 the Court makes a bit of a distinguishing
8 statement about tax jurisdiction.

9 What I'd say, Justice Gorsuch, to your
10 question is the -- the whole paradigm is
11 different in tax jurisdiction cases. The focus
12 is on benefits and protections.

13 To conclude, I might say this: We're
14 asking, picking up on my colleague's federalism
15 theme, that North Carolina's choice of taxing
16 criteria be respected. We're not casting any
17 doubt on any other state's taxing criteria.

18 Fundamentally, this is a due process
19 challenge. And I would -- I would drive home
20 again that the point that my colleague is
21 promoting in terms of a rule under the Due
22 Process Clause would invalidate the trust tax
23 criteria in 33 states. That would be an
24 aggressive deployment of the Due Process
25 Clause.

1 Indeed, we ask instead this Court to
2 take the approach called for by federalism and
3 fundamental fairness, truthfully, and to
4 reverse the judgment below.

5 Thank you.

6 CHIEF JUSTICE ROBERTS: Thank you,
7 counsel. The case is submitted.

8 (Whereupon, at 12:09 p.m. , the case
9 was submitted.)

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