

FILED

JUL 7 3 11 PM '95

SUPERIOR COURT OF THE DISTRICT OF COLUMBIA  
TAX DIVISION

SUPERIOR COURT OF THE DISTRICT OF COLUMBIA  
TAX DIVISION

CHEMICAL BANK, Trustee of :  
the Esther L. Guth Trust, :  
: Petitioner :  
: :  
v. : Tax Docket No. 6028-94  
: Judge Cheryl M. Long  
: :  
DISTRICT OF COLUMBIA :  
: Respondent :

**MEMORANDUM OPINION AND ORDER**

This litigation presents a case of first impression concerning the constitutional, due process requirements for imposing District of Columbia income tax on a so-called "resident trust." This issue, and others, came before this Court pursuant to cross-motions for summary judgment and oral argument thereon. On most of the issues at hand, the petitioner's position must prevail. The only tax year for which relief will be denied is tax year 1990. In order to view the legal conflicts in the most practical light, it is necessary to set forth the factual and procedural background of the case and to summarize the competing conceptual arguments.

**I. BACKGROUND**

Petitioner, Chemical Bank, is a financial institution duly organized and existing under the laws of the State of New York. At all times relevant to the instant action,

Chemical Bank has served as trustee for the Esther L. Guth Trust (hereinafter "the Guth Trust"). Today, Chemical Bank continues to fulfill this role.

The Guth Trust is a testamentary trust that was established in 1934 under the Will of Willard A. Lalor, a resident of the District of Columbia at the time of his death.

From the period beginning in 1987 through 1991, the Guth Trust was taxed by the District of Columbia's Department of Finance and Revenue as a resident trust.

Respondent taxed the Guth Trust as a resident trust because at the time of his death, Willard A. Lalor was domiciled within the District of Columbia and any trust created by his will was classified as a resident trust pursuant to 47 D.C. § 1808.3 and § 47-1809.1 (1990).

Beginning in 1940, Chemical Bank as trustee of the Guth Trust filed accountings with the District of Columbia pursuant to Rule 305 of the Superior Court Probate Rules.

On December 1988, Chemical Bank filed a complaint in the District of Columbia Superior Court requesting court approval for the resignation of trustee Charles Lalor Burdick, for compensation of the resigning trustee, for increased allowance of compensation of trustee Chemical Bank, and for waiver of the accounting requirement.

On October 26, 1990, the Superior Court granted all relief requested by petitioner, including authorization to the trustee to discontinue filing accounts with the Court.

The final accounting for the Guth Trust was filed with respect to fiscal year 1989.<sup>1</sup>

On October 7, 1991, the trustee filed a second complaint in the District of Columbia Superior Court requesting a court ruling on whether a particular individual was the "lawful issue" of one of the beneficiaries of the Guth Trust. By order dated September 11, 1992, the Court determined that the trust instrument should be interpreted to construe that individual as a lawful issue of the beneficiary.

The parties have stipulated to the following facts with respect to income taxes paid on behalf of the Guth Trust and claims for refund filed by petitioner:

On or about April 14, 1988, the Guth Trust paid income tax to respondent in the amount of \$79,536.34 for tax year 1987.

On or about April 14, 1989, the Guth Trust paid income tax to respondent in the amount of \$75,475.00 for tax year 1988.

On or about April 14, 1990, the Guth Trust paid income tax to respondent in the amount of \$109,159.00 for tax year 1989.

---

<sup>1</sup> The Superior Court also indicated in its Order that it would not retain continuing supervision over the trust, but ordered Chemical Bank to continue providing monthly statements of the trust's financial activity and an annual summary account to the present income beneficiaries and contingent remaindermen.

On or about April 15, 1992, the Guth Trust paid income tax to respondent in the amount of \$81,288.00 and interest in the amount of \$14,632.00 for tax year 1990.

On or about April 15, 1992, the Guth Trust paid income tax to respondent in the amount of \$60,145.00 for tax year 1991.

On or about April 15, 1991, pursuant to § 1812.11(2), petitioner as trustee of the Guth Trust filed a timely claim with respondent for a refund of taxes paid for tax year 1987.

On or about August 30, 1991, pursuant to § 1812.11(2) (1990), petitioner as trustee of the Guth Trust filed a timely claim with respondent for a refund of taxes paid for tax year 1988. Notice of disallowance of the refund claim was received by petitioner on or about December 9, 1993.

On or about August 30, 1991, pursuant to § 1812.11(2) (1990), petitioner as trustee of the Guth Trust filed a timely claim with respondent for a refund of taxes paid for tax year 1989. Notice of disallowance of the refund claim was received by petitioner on or about December 9, 1993.

On or about March 10, 1993, pursuant to § 1812.11(2) (1990), petitioner as trustee of the Guth Trust filed a timely claim with respondent for a refund of taxes paid for tax years 1990 and 1991. Notice of disallowance of

the refund claim was received by petitioner on or about December 9, 1993.

On December 17, 1993, petitioner filed a Complaint in the Superior Court seeking (1) the refund of income tax assessments for tax years 1987, 1988, 1989, 1990, and 1991, (2) a permanent cancellation of the assessments against the Guth Trust retroactive to 1986, and (3) a declaration that the definition of resident trust as provided in the Code denies this petitioner due process of law and, as a precedent to taxation, is facially unconstitutional.

## II. ANALYSIS OF THE ARGUMENTS

For purposes of clarity, the Court will analyze each issue, i.e. nexus to the District of Columbia, statute of limitations and waiver, as it relates to the particular tax year in question.

### **A. Petitioners' Position.**

#### Tax Years 1987, 1988, 1989, 1990 and 1991

Petitioner argues that the District of Columbia's tax on the Guth Trust's income "exceeded the District's power to tax under the Due Process Clause of the Fifth Amendment of the Constitution." See Petitioner's Memorandum of Points and Authorities in Support of Motion for Summary Judgment at 11.

The imposition of the tax on the Guth Trust, petitioner asserts, violates the Due Process Clause since

the nexus between the Trust and the District is insufficient to comprise the "definite link" or "minimum connection" between the taxing entity and the taxpayer required by the Constitution.

Specifically, petitioner contends that the only connections between the Guth Trust and the District consisted of the filing of annual accountings (through 1989) as required by the D.C. Superior Court probate rules, and some limited litigation relating to the administration of the Trust.

Petitioner argues that these limited contacts do not create a "connection" sufficient to satisfy due process requirements. Consequently, petitioner requests this Court to refund the taxes paid on income generated by the Guth Trust for tax years 1987 through 1991.

#### Tax Year 1987

Petitioner maintains that the Guth Trust timely paid its 1987 resident trust income tax and, through counsel, filed a timely claim for refund with the Department of Finance and Revenue.

First, petitioner argues that in its letter to petitioner dated July 25, 1991, the Department of Finance and Revenue failed to notify petitioner that the notice represented a "final" denial of petitioner's claim for refund for tax year 1987.

Petitioner contends that the specific language of the letter makes it reasonable for petitioner to have believed that a final determination with respect to its claim for refund for tax year 1987 had not been reached by the Department of Finance and Revenue.

Second, petitioner contends that, following the issuance of the July 1991 letter, the Department of Finance and Revenue acted contrary to its present assertion that the notice constituted a final determination of its claim for refund for tax year 1987. Petitioner alleges that respondent continued to consider facts and arguments made in connection with the 1987 claim for more than 28 months after the purported denial.

Third, petitioner argues that even if the 1991 determination were final, the ongoing consideration of the matter tolled the running of the statute of limitations.

Therefore, petitioner proffers, either because the 1991 letter was not a final denial or because the ongoing administrative consideration tolled the statute of limitations, the appeal of the 1987 claim is not barred as untimely.

**Tax Year 1990**

In its Memorandum of Points and Authorities in Support of Motion for Summary Judgment, petitioner makes only one reference to its request for a refund for tax

year 1990. In footnote one of its Memorandum, petitioner asserts that

[t]here is some question as to the status of the 1990 claim, because the available records suggest that Chemical Bank failed to pay a penalty that was assessed for late filing. Chemical is prepared to pay the penalty now in order to preserve the 1990 claim for appeal. Moreover, the Department can waive the payment of a penalty.

Petitioner's Memorandum of Points and Authorities in Support of Motion for Summary Judgment fn. 1 at 2.

In oral argument, petitioner stated its position regarding tax year 1990 as one in which it simply wishes to survive summary judgment so that discovery may be obtained, in the hope of finding some evidence of a waiver of penalty payments by the District. There is no existing evidence of any such waiver. In fact, Petitioner merely notes that the District "can" waive payment of a penalty. Chemical Bank has represented that if, after discovery, no evidence of waiver of the penalty by the Department of Finance and Revenue is revealed, petitioner will concede that the Superior Court is without subject matter jurisdiction to entertain the appeal for tax year 1990.

**B. Respondent's Position.**

**Tax Years 1987, 1988, 1989, 1990 and 1991**

Respondent argues that the District of Columbia has a sufficient nexus with the Guth Trust to assess taxes on the Trust's income to satisfy due process requirements.

Pursuant to Section 1809.1 of Title 47, the Guth



Trust is recognized as a "resident trust" in the District of Columbia. According to the statute, therefore, any income produced by the Guth Trust is subject to taxation in the District. 47 D.C. § 1809.3.

Respondent contends that for purposes of levying a tax, the District need only determine that it has provided the taxpayer "with anything for which it can ask return." Wisconsin v. J.C. Penney Co., 311 U.S. 435, 444 (1940).<sup>2</sup>

In other words, respondent argues that the Guth Trust has in the past and continues to receive "benefits" from the judicial resources of the District of Columbia. Specifically, the Government claims that there are two examples of such "benefits". First, the Government points to the fact that the Trust has filed annual accountings for many years. Second, the Government notes a provision in the settlor's Will in which he directs that

---

<sup>2</sup> In J.C. Penney Co., Respondent, a Delaware corporation having its principal offices in New York, challenged the Wisconsin Privilege Dividend Tax of 1935. The State of Wisconsin essentially levied an additional tax on all corporations "for the privilege of declaring and receiving dividends, out of income derived from property located and business transacted in" Wisconsin. Section 3, Chapter 505, Laws of Wisconsin, 1935, as amended by Chapter 552, Laws of Wisconsin, 1935. The Court held the tax to be valid as to both local and foreign corporations since the "incidence of the tax as well as its measurement is tied to the earnings **which the State of Wisconsin has made possible**". Wisconsin v. J.C. Penney Co., supra, 435 U.S. at 446 [emphasis supplied].

The Court found that the "substantial privilege of carrying on business in Wisconsin, which has here been given, clearly supports the tax, and the state has not given the less merely because it has conditioned the demand of the exaction upon happenings outside its own borders". Id. at 444-45.

any investments of the Trust must be "of the character permissible for trust investment under the laws of the District of Columbia. . . ."

Respondent argues that the above two examples establish the "continuing, affirmative beneficial relationship" of the Guth Trust to the District of Columbia. Id. at 7.

#### Tax Year 1987

In response to petitioner's claim for refund for tax year 1987, the Department of Finance and Revenue issued a letter on July 25, 1991 which denied petitioner's challenge on the basis that petitioner had not shown sufficient grounds to justify a refund.

Petitioner reiterated the same basis for relief in a letter dated November 11, 1991. The District responded by issuing a letter dated July 27, 1992, which again denied petitioner's claim for refund.

Respondent asserts that pursuant to Section 1812.11(12), taxpayers who wish to challenge denials of refunds have six months from the time of receiving the denial to file an appeal with the Tax Division of the Superior Court. 47 D.C. § 1812.11(12).

Respondent argues that petitioner filed its case for tax year 1987 on December 17, 1993, approximately seventeen months after receiving the most recent denial of its refund request.

Respondent disputes petitioner's assertion that either the Code or the District of Columbia Municipal Regulations require a specific reference that a letter of denial is a "final determination" or that the District must provide a taxpayer with specific notice of his appeal rights.

Further, respondent contends that even if the Court agrees with petitioner that the July 11, 1991 letter appeared insufficiently final because of the suggestion that additional information was necessary, the July 27, 1992 letter is unambiguous in its finality.

Respondent requests this Court to deny petitioner's claim for tax year 1987 as untimely filed.

#### Tax Year 1990

Respondent asserts that the Court is without subject matter jurisdiction to entertain petitioner's appeal of the denial of the claim for refund for tax year 1990. The District argues that the Code requires the base tax and all penalties associated therewith to be paid prior to the filing of a Petition for Refund.

Respondent contends that petitioner failed to pay a penalty in the amount of \$20,322.00 assessed against the Trust for late payment of income tax for tax year 1990. Pursuant to Sections 1812.11(10) and 3303 of Title 47 of the District of Columbia Code, respondent argues that this

Court lacks subject matter jurisdiction to address the claim for refund for tax year 1990.

The District asserts that petitioner's offer to pay the penalties associated with tax year 1990 **at the present time** would have no effect on the Court's jurisdiction over the claim. Respondent takes the position that since petitioner failed to pay the penalties prior to the filing of the instant lawsuit, the Trust is estopped from raising the defense of waiver at the point of arguing cross-motions for summary judgment.

### III. RESOLUTION OF THE PETITION

#### A. The Constitutional Issue Regarding Tax Years

##### 1987, 1988, 1989, 1990 and 1991

The Code's definition of a resident trust status cannot alone establish a constitutionally sufficient nexus.

The first issue petitioner asks the Court to consider is whether Section 1809.3 as presently written authorizes the assessment of taxes on undistributed trust income without due process of law in violation of the Fifth Amendment of the United States Constitution.

#### **Basic Due Process Requirements**

The Due Process Clause "requires some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax." Quill Corporation v. North Dakota, 504 U.S. 298, 306, (1992)

(citing Miller Bros. Co. v. Maryland, 347 U.S. 340, 344-45 (1954)).

Further, the Supreme Court has held that the "income attributed to the State for tax purposes must be rationally related to values connected with the taxing State." Id. at 1909-10 (citing Moorman Mfg. Co. v. Bair, 437 U.S. 267, 273 (1978)). In other words, the courts must look to "whether the taxing power exerted by the state bears fiscal relation to protection, opportunities and benefits given by the state". Wisconsin v. J.C. Penney Co., supra, 435 U.S. at 444.

In 1992, in reviewing a North Dakota use tax for conformity with due process requirements, the Supreme Court stated:

Due process centrally concerns the fairness of government activity. Thus, at the most general level, the due process nexus analysis requires that we ask whether an individual's connections with a state are substantial enough to legitimate the State's exercise of power over him.

Quill Corp. v. North Dakota, supra, 504 U.S. at 312. The power of the District of Columbia to tax the undistributed income of a resident trust, therefore, is dependent on the existence of sufficient contacts with the District to satisfy constitutional due process requirements.

### **Interpretation of Section 1809.3**

The District imposes an income tax on "income from any kind of property held in resident trusts." 47 D.C.

§ 1809.3. According to the Code, a testamentary trust is deemed a resident trust if the settlor "was at the time of his death domiciled within the district." 47 D.C. § 1809.1.

Notably, there are three jurisdictions with resident trust statutes that are virtually identical to our own: Missouri, New Jersey, and New York. All of these jurisdictions have determined that, without more substantial contacts between the taxpayer and the taxing jurisdiction, the tax is unconstitutional as a violation of due process. See e.g., Swift v. Director of Revenue, 727 S.W.2d 880 (Mo. 1987) (en banc); Pennoyer v. Taxation Division Director, 5 N.J. Tax 386 (N.J. Tax Ct. 1983)<sup>3</sup>; Taylor v. State Tax Commission, 85 A.D.2d 821, 445 N.Y.S.2d 648 (3d Dept. 1981); Mercantile-Safe Deposit and Trust Co. v. Murphy, 19 A.D. 2d 765, 242 N.Y.S.2d 26 (App.Div.1963), aff'd 15 N.Y.2d 579, 255 N.Y.S.2d 96, 203 N.E.2d 490 (Ct.App.1964).

Section 605 of Article 22 of the New York's Tax Law defines a resident estate or trust as "a trust, or portion of a trust, consisting of property transferred by will of a decedent who at his death was domiciled in this state."

N.Y. CLS Tax § 605(3) (1994) [emphasis supplied].

Section 143.331(2) of the Missouri Code defines a resident trust as a "trust created by will of a decedent

---

<sup>3</sup> 1983 New Jersey Tax LEXIS 28.

who at his death was domiciled in this state." Section 143.331(2), RSMo 1994 [emphasis supplied].

The New Jersey statute itself defined a resident trust as a trust consisting of "property transferred by will of a decedent who at his death was domiciled in this State . . . ." N.J.S.A. 54A; 1-2(o)(2)).<sup>4</sup>

In Pennoyer v. Taxation Division Director, the New Jersey Tax Court determined that a New Jersey deficiency income tax assessment against a trust, based on New Jersey's definition of resident trust, violated due process.

Like our own situation in the instant case, the New Jersey Tax Court found that no beneficiaries, trustees or assets were located in New Jersey. The only contact between the trust and New Jersey was the fact that the grantor was domiciled in New Jersey, that letters were issued in New Jersey, that the trustee was served in New Jersey and that the New Jersey courts were available to resolve issues relating to the trust. Pennoyer v. Tax Division Director, supra.<sup>5</sup>

The Court held that the creation of the trust in New Jersey in 1970, the probate proceeding in a New Jersey court, and the jurisdiction and availability of the New Jersey courts were all **insufficient** contacts to support

---

<sup>4</sup>1983 N.J. Tax LEXIS 28, at \*5.

<sup>5</sup>1983 N.J. Tax LEXIS at \*18.

taxation. Pennoyer v. Tax Division Director, supra.<sup>6</sup> Therefore, the provision of the New Jersey statute which defined "resident trust" could not constitutionally be applied to the facts at issue in Pennoyer. Id.

In a statutory scheme that is identical to the provision of the laws of New Jersey, New York, and Missouri, Section 1809.3 of the District of Columbia Code does not require any connection between the District and the taxpayer other than the mere fact that the settlor of the trust was domiciled in the District **at the time of his death.**

The creation of a trust in the District and initiation of probate proceedings prompting the transfer of assets to a trust are completed acts; they are certainly not continuing in nature.

In the absence of (1) trust assets being located in the District or (2) physical residence of either the trustee one or more beneficiaries here, the District cannot satisfy this Court that there is a "continuing" benefit to the trust to justify taxation of trust income.

Therefore, as applied to the facts of the instant case, this Court concludes as a matter of law that taxation of the Guth Trust **based solely upon its statutory definition as a resident trust, and without evidence of a continuing benefit,** is unconstitutional.

---

<sup>6</sup>1983 N.J. Tax LEXIS 28, at \*20.



**The Swift test.**

To determine if a constitutionally sufficient nexus exists between the Guth Trust and the District for taxation purposes, this Court adopts the multi-factor test set forth in Swift v. Director of Revenue, supra.

In Swift, the Supreme Court of Missouri held unconstitutional the taxation of a trust under a Missouri statute which defined a resident trust as "a trust created by the will of a decedent who at his death was domiciled in this state." Id. (citing Mo. Rev. Stat. § 143.331(2) (1986)).

The Swift court considered six points of contact by which to analyze the subject trust's connection with the taxing authority. To determine if a sufficient nexus existed, the Court prescribed the review of the following six factors:

- (1) the domicile of the settlor
- (2) the state in which the trust is created
- (3) the location of the trust property
- (4) the domicile of the beneficiaries
- (5) the domicile of the trustee; and
- (6) the location of the administration of the trust.

Further, the Court determined that to support an income tax, the first two factors "require the ongoing protection or benefit of state law only to the extent that one or more of the other four factors is present."

Swift v. Director of Revenue, supra, 727 S.W.2d at 882 [emphasis supplied].

In Swift, the Court determined that the only connections between Missouri and the trust were (1) that the decedent grantor was domiciled in Missouri and (2) that the administration of his estate occurred in Missouri. Id. Consequently, the Court held that Missouri did not have sufficient contacts with the trust to permit the imposition of a Missouri income tax. Id.

**Applying Swift : The District of Columbia's connections to the Guth Trust are insufficient to satisfy the nexus requirement**

Applying the multi-factor test set forth in Swift, this Court finds that the District of Columbia has not established a sufficient nexus with the Guth Trust to justify taxation of trust income.

First, it is undisputed that the Trustee of the Guth Trust is not located in the District, that no beneficiary resides in the District, and that no trust assets are located in the District.

Second, the District's four bases for arguing that a sufficient nexus exists between the Guth Trust and the District to justify the District's income taxation are unpersuasive:

- (1) the Guth Trust's status as a resident trust in that the decedent settlor was domiciled in the District at the time of his death,

- (2) the Guth Trust's filing of annual accountings in the District,
- (3) the Trustee's utilization of the District's courts for litigation; and
- (4) the decedent settlor's expectation that District of Columbia law would apply in the administration of the Trust.

For the following reasons, this Court determines that respondent's four bases, considered either separately or in the aggregate, do not create a sufficient constitutional nexus for taxation by the District of the Guth Trust's income.

**1. "Pre-Existing Connections" Creating Resident Trust Status**

As set forth earlier in this Memorandum Opinion, the fact that the decedent settlor was domiciled in the District at the time of his death cannot alone establish the necessary connection to the District required by due process considerations to warrant imposition of income tax on the Guth Trust.

The creation of the trust in the District of Columbia is an **historical** fact which, absent **subsequent, continuing contacts**, is not a sufficient constitutional nexus justifying income taxation of undistributed trust income.

Further, the trustee itself (which is not a resident of the District of Columbia) holds, in New York, all legal title to trust property. Therefore, neither legal nor beneficial ownership interests in the trust are present in the District.

Section 1809.3 of the District of Columbia Code taxes income generated by a resident trust solely on the basis of the settlor's domicile in the District at the time of his death and the fact that the trust instrument was created in the District. This momentary connection cannot withstand due process scrutiny and this Court finds Section 1809.3 of the Code to be unconstitutional as applied to the Guth Trust.<sup>7</sup>

## **2. Account Filing Requirement**

Pursuant to Probate Rule 305, the Guth Trust was required to file annual accountings. This requirement commenced in 1939, at which time the Trustee was appointed by the Court. The Trustee filed annual accountings through tax year 1989, whereupon a waiver was obtained at the Trustee's request in 1990.

The District argues that the Trust's obligatory filing of annual accountings somehow bestowed a benefit upon the Trust, thereby creating a nexus between the Trust and the District for purposes of taxation. To the contrary, petitioner argues that the Guth Trust's compliance with the filing requirement arose only out of the probate administration of the Willard Lalor estate. As a result, petitioners contend that the filing of

---

<sup>7</sup>This connection is indeed "momentary" in the sense that only the decedent's domicile at the very moment of death can insure that his will can be probated in the District of Columbia. The length of time that he may have resided in the District of Columbia is of no importance at all under the current statutory scheme.

accountings is not a sufficient connection between the Guth Trust and the District to support the District's taxation of Trust income.

This Court agrees with petitioner's position.

First, this Court has obtained and reviewed the aged court jackets in the Matter of Charles Lalor Burdick et al. Eq. No. 63,271 (Vols. 1-16). Taking judicial notice of what lies in the official files of the Court, it is clear that the Guth Trust filed **forty-nine separate accountings** and paid all associated court costs in compliance with the reporting requirement of Rule 305. In 1991, after fifty years of filing trust accountings, the Trust sought and obtained a court order to relieve itself from further reporting requirements.

For all practical purposes, therefore, this Court agrees with petitioner that the District's reporting mandate is both an administrative and financial **burden** on the Trust rather than a **benefit** to the Trust itself.

While respondent argues that the Guth Trust received an implicit benefit during the tax years the District imposed the accounting requirement, i.e. the protection of trust assets, the more practical view is that the beneficiaries, not the Guth Trust itself, received the alleged benefit from such filings. The account filing requirement essentially provides notice of the filing to

the beneficiaries and the beneficiaries may inspect those documents.

Second, even if this Court were to accept the District's "implicit benefit" theory, the District of Columbia Government has already received due compensation in recognition of the judicial resources that were connected to the Trust. This occurred under a system that directly addresses the Court's relationship to the Trust. Such compensation has occurred in two ways: (1) payment of the estate tax paid to the District by the Lalor estate in 1934 and (2) the payment of **costs** paid to the court system when the annual accountings were filed. See, e.g., Potter v. Taxation Div. Director, 5 N.J. Tax 399 (N.J. Tax Ct. 1983) (finding that any benefit to the trust from New Jersey law was accounted for in payment of an inheritance tax).<sup>8</sup>

Long ago, the Supreme Court of Wisconsin held that Wisconsin was without authority to impose an income tax on trust income because that income "was not derived from property located or business transacted in the state of Wisconsin." Bayfield County v. Pishon, 162 Wis. 466, 156 N.W. 463, 464 (Sup.Ct. 1916). The Supreme Court of Wisconsin rejected the view that taxation of trust income

---

<sup>8</sup>This conclusion by the New Jersey Tax Court is highly persuasive, not only because it makes sense but because New Jersey's statute is identical to the District of Columbia statute that is subject to this litigation.

could be premised upon the fact that the Wisconsin courts required the trustee to file annual accountings. Despite its age, this appellate decision retains its vitality. The logic of Pishon applies in the instant case.<sup>9</sup>

This Court concludes as a matter of law that the payment of estate taxes and court costs are pivotal and persuasive in petitioner's favor. The District's whole underlying theory of levying a tax on trust income is to ensure that the District is compensated for whatever it provides as a benefit when it is called upon to take action or provide something to the trust. Here, the court system is the governmental entity that allegedly provided a "benefit." Nonetheless, all of the court costs eventually would land in the very same place where income taxes are deposited, i.e. the general fund of the District of Columbia.<sup>10</sup>

---

<sup>9</sup>The decision in Pishon is the only case cited by either party herein that precisely addresses the role of annual accountings as a basis for the taxation of trust income.

<sup>10</sup>Prior to the advent of home rule, revenue of the District of Columbia was deposited into the Treasury of the United States. However, beginning in 1975 the law provided that all funds (such as court costs) that previously were deposited into the United States Treasury henceforth would be channeled to the "General Fund of the District." Furthermore, any officer of the District of Columbia was required to pay all governmental income to the Mayor for deposit in the appropriate fund. See 47 D.C. § 130. The Fiscal Officer of the District of Columbia Courts historically was always required to turn over revenue from court costs to the United States Treasury. 11 D.C. § 1723(a)(2). The change was duly made by statutory requirement. Thus, the local taxing authority (i.e. the executive branch) has always received the governmental revenue that was generated by the Guth Trust in the same manner as it has received any other government revenue.

Based upon this Court's review of the Guth Trust's accounting records, it appears that the Trust timely paid all of the applicable court costs and estate taxes. Thus, the income taxes that are **now** in dispute are functionally a forcible double payment or double taxation. A doubling of such payments or taxation constitutes a denial of due process of law. This cannot be permitted.

In context, the Guth Trust's compliance with the annual filings in the Probate Division of the Superior Court certainly does not constitute a sufficient nexus to satisfy due process considerations.

### **3. Litigation Involving the Trust.**

The Trustee filed suit in the District of Columbia on behalf of the Guth Trust on two different occasions with regard to the administration of the Trust.

First, in 1988, the Trustee initiated a proceeding in the District of Columbia regarding the appropriate compensation for the trustees, acceptance of the resignation of the co-trustee, and waiver of the annual accounting and reporting requirements.

Second, in 1991, the Trustee sought declaratory relief from the Superior Court regarding the interpretation of the term "lawful issue" as set forth in the trust instrument.

The mere availability of courts in a taxing jurisdiction has never been considered a sufficient nexus



for purposes of taxation. See, e.g., Pennoyer v. Taxation Division Director, supra.<sup>11</sup> The District cites no authority to support the contrary position.

As petitioner correctly points out, the anecdotal, serendipitous, or occasional use of our local court cannot be considered sufficient nexus to permit permanent taxation of income.<sup>12</sup>

#### 4. Directive of the Settlor with Regard to Choice of Investment Standard

Respondent argues that another constitutionally sufficient nexus to the District is found in William Lalor's apparent expectation and directive in his will that the law of the District of Columbia would be the standard for selecting the quality of the investments that would be purchased by the Trust. Specifically, the District relies on language set forth in paragraph two of Article VII of the decedent's will:

At the risk of the trust estate and without responsibility to my Trustee to continue to hold any stocks, bonds or other investments, in which at the time of my death any part of my estate shall be invested, although the same shall be of the **character permissible for trust investment under the laws of the District of Columbia**, and likewise in respect of

---

<sup>11</sup>1983 N.J. Tax LEXIS 28, at \*18-19.

<sup>12</sup>To be sure, the District has taken the extremely broad approach of arguing that past resort to our local courts is a basis on which to tax all present and future income of the Trust on a permanent basis, not merely to tax the income during a particular tax year in which a lawsuit or petition is filed.

such trust investments my Trustee shall have full power and authority to dispose of, call in or change any and all investments and to make investments of such trust funds in any security, stocks, bonds or other investments which in its discretion may be deemed by my trustee safe and for the best interests of my estate but only, however, in such stocks and bonds of the character **permissible** for trust investments under the laws of the District of Columbia. [emphases supplied].

Petitioner correctly points out that the above-quoted language only references the District's legal standard for trust investments (whatever that standard might become in the future). This language does nothing more than require the Trust to abide by certain criteria. The necessary research to learn and apply the criteria, whatever that might entail, does not require anyone to be present or to reside inside the District of Columbia. Accordingly, this passage in the settlor's will refers to nothing more than the future thought processes of the Trustee. It does not create a tangible nexus between the Trust and the Government of the District of Columbia itself.

No significant, permanent ties to the District of Columbia Government are erected in the will. For example, nowhere in the trust instrument does the settlor specify the District of Columbia as the sole choice of jurisdiction or venue for purposes of future litigation involving the Trust. Clearly, the trust instrument is devoid of any reference to the District of Columbia as the

jurisdiction to which the settlor requires his executors and trustees (who were then located in New York and Delaware) to "carry to the Court of last resort any contest to this will."

The sixth component of the Swift test provides that the location of the trust administration may create a sufficient nexus with a taxing jurisdiction.

Clearly, administration of a trust consists of more than the filing of annual accountings. The underlying work in producing the income and making the disbursements is, in practical effect, the real **daily business** of the Trust. In the instant case, it is undisputed that hands-on, actual management of the Guth Trust is performed on an **exclusive, ongoing basis** in solely New York by trustee Chemical Bank.<sup>13</sup> The facts of the instant case easily can be distinguished from the those in Wisconsin v. J.C. Penney Co., supra. In J.C. Penney, the applicable statute carefully specified that the taxable income is income "derived from property located and business transacted in" the taxing jurisdiction. Here, the income is obviously not earned in the District of Columbia. Thus, the sixth form of substantial nexus, recognized in Swift, is absent in the instant case.

---

<sup>13</sup>The real business of the Trust is the purchase and sale of securities. No securities of the Trust are maintained, deposited, or held in any custodial manner inside the District of Columbia. Also, there is no District of Columbia real property to be liquidated as any sort of Trust investment.

B. Tax Year 1987 - The Issue of  
Timeliness of Appeal

The dispute between the parties concerning the 1987 refund claim centers on one inquiry: whether the Department of Finance and Revenue issued a "final" denial of the claim on July 25, 1991, as claimed by the District, or whether the District issued its "final" denial on December 9, 1993, as claimed by petitioner.

The relevant statute of limitations provides that an appeal must be filed "within six months from the date of the assessment of the deficiency or from the date of the denial of a claim for refund, as the case may be." 47 D.C. § 1815.1. Consequently, if the letter issued to petitioner in 1991 is deemed by this Court to constitute a "final" denial of the claim for refund, the appeal of the 1987 claim is clearly untimely unless the appeal period was tolled.

A review of the pertinent correspondence between the parties is warranted. By letter dated July 25, 1991, the Department of Finance and Revenue informed counsel for the Trustee, in relevant part:

In reviewing the fiduciary return for Esther Guth, we have no information that has come to our attention that would justify a refund at this time. We must deny the refund request made by you on behalf of Esther Guth ET.A2.TR U/W **until you can provide additional information to us.** [emphasis supplied]

See McAvoy Affidavit (hereinafter "Aff."). Ex. E.

Petitioner argues that the letter neither stated that it was a "final determination" nor included any information either about the Guth Trust's right to appeal or any applicable time limitations on appeal.

Accepting the opportunity to pursue the matter further, the Trustee (through counsel) sent a letter dated November 11, 1991, providing therein additional information to the Department of Finance and Revenue in support of the Trust's refund claim. See McAvoy Aff. Ex. F.

By letter dated July 27, 1992, nearly eight months after the provision of the additional information, the Department of Revenue responded to the November 11, 1991 letter by stating:

We are without authority to issue a refund for the 1988<sup>14</sup> Form D-41, Fiduciary return filed for Esther L. Guth Et. Al. Trust U\W. If you have any questions, please call me . . . .

See McAvoy Aff. Ex. G.

On November 23, 1992, counsel for the Trustee corresponded with the Department of Finance and Revenue requesting a hearing with regard to its refund claim for tax year 1987. This letter also explicitly stated,

Chemical Bank wishes to appeal the denial of its refund claim to the Tax Division of the Superior Court of the District of Columbia because it believes it is entitled to a refund for the

---

<sup>14</sup> The Department of Finance and Revenue's letter erroneously made reference to the claim for refund made for the 1988 tax year, rather than the 1987 tax year at issue.

reasons set forth in the [November 11, 1991 letter].

See McAvoy Aff. Ex. H.

The Department of Finance and Revenue did not reject this letter by treating it as a previously closed issue. Rather, the Department responded by letter dated January 5, 1993 in which it indicated that no opportunity for a formal hearing before the Department of Finance and Revenue was available, but that

[u]pon receipt of our final determination, the taxpayer may petition the Superior Court of the District of Columbia within six (6) months. (emphasis added).

See McAvoy Aff. Ex. I.

Petitioners contend that "a series of oral communications then ensued" thereafter in which Trustee's counsel requested that the Department of Finance and Revenue review the claims for refund for tax years 1987 through 1991 and issue whatever constituted a final determination as referenced in the January 5, 1993 letter. See McAvoy Aff. para. 18 and 19.

On December 9, 1993, counsel for Trustee received a written response from the Department of Finance and Revenue denying the Trustee's claims for 1988, 1989, 1990 and 1991. With regard to tax year 1987, the Department of Finance and Revenue implied for the first time that it had denied the claim for refund in tax year 1987 in 1991:

Regarding the denied refund claim for 1987, an appeal can not be filed with the D.C. Superior Court because the denial refund notification letter was mailed on July 25, 1991 to Mr. Edward F. Rover, an attorney with White & Case. This appeal must be filed with the D.C. Superior Court within six months from the denial date of the refund claim.

See McAvoy Aff. Ex. J.

Petitioner maintains that the December 9, 1993 letter for the first time specifically discussed appeal rights and included an "appeal rights information sheet" as an enclosure. See McAvoy Aff. Ex. J.

Upon review of the series of correspondence between petitioner and respondent, this Court concludes that the District did not issue a "final determination" with respect to the claim for refund for tax year 1987 until December 9, 1993.

Clearly, the respondent's letter of July 25, 1991 did not constitute a "final determination" of petitioner's claim for refund due to its clear, internal, conditional language, i.e. "[w]e must deny the refund request . . . . **until you can provide additional information to us.**" [emphasis supplied]

As a matter of common sense interpretation, the District official who signed the letter could not have meant for the July 25, 1991 letter to finally determine the matter if the Government was still willing to consider "additional information" regarding petitioner's claim for

refund. The Department of Finance and Revenue thus created a situation in which it manifestly left the claim for refund open for further discussion. The opportunity for further discussion means that there was an opportunity for the petitioner to obtain relief from the agency.

Without a doubt, the letter of July 25, 1991 virtually invited the taxpayer to continuing pursuing the issue of a refund at the agency level for this particular tax year. If the official who signed the letter had seriously thought that the matter was at an end, it would have been superfluous and meaningless for him to offer to consider new arguments on the same subject at some unspecified time in the future.

Similarly, the agency's letters of July 27, 1992 and January 5, 1993 did not effectively communicate to petitioner that the claim for refund for tax year 1987 had been conclusively determined. In particular, the District advised petitioner by letter of January 5, 1993 that "**[u]pon receipt of our final determination**, the taxpayer may petition the Superior Court of the District of Columbia within six (6) months". [emphasis supplied] Here, it is obvious that the writer of the letter knew that a so-called "final determination" had not yet been sent out to the taxpayer. The letter talked about an appeal in the future that would be triggered once the final determination had been sent.



The ambiguous nature of the agency's correspondence easily demonstrates that a final determination had not been issued by the District as of January 5, 1993.

In contrast, respondent's letter of December 9, 1993 clearly indicates that "the refund claims on 1988, 1989, 1990 and 1991 D.C. fiduciary income tax returns . . . . **are hereby denied.**" [emphasis supplied] It did not state, "**were or have already been denied.**" Further, the agency for the first time enclosed an appeals rights information sheet as an enclosure with the December 9, 1993 letter.

This Court concludes as a matter of law that the unequivocal language of respondent's letter dated December 9, 1993 constituted a final determination of petitioner's claim for refunds in tax years 1988, 1989, 1990, 1991 **as well as tax year 1987.**

Petitioner had six months from receipt of the December 9, 1993 final determination to file its appeal for tax year 1987. Consequently, this Court concludes that petitioner's appeal for tax year 1987, filed December 17, 1993, was filed within the time specified by statute of limitations.

### **C. Tax Year 1990- Failure to Pay All Tax Penalties**

Petitioner seeks a refund of income tax paid for tax year 1990 pursuant to Sections 1812.11(10) and 3303 of the Code. The statute requires that in order to pursue a claim for refund of income tax, a litigant must first pay

all tax "along with penalties due thereon." 47 D.C. §§ 1812.11(10), 3303.

Petitioner concedes that, although income taxes for tax year 1990 were due on April 15, 1991, the trust did not file its 1990 income tax return nor pay its income taxes until approximately April 15, 1992. See Joint Stipulation of Facts at para. 14.

As a result of the late payment, the Department of Finance and Revenue assessed a penalty in the amount of \$20,322.00 pursuant to Section 1813.1 of the Code. Petitioner fully acknowledges that the penalty was not paid prior to the filing of the instant appeal. See Petitioner's Memorandum of Points and Authorities in Support of Motion for Summary Judgment at 2 footnote 1.

This Court concludes as a matter of law that an absolute prerequisite to filing an appeal of a tax is the full payment of all penalties associated with the base tax. Perry v. District of Columbia, 314 A.2d 766, 767 (1974).<sup>15</sup> Where a petitioner files an appeal without full payment of the base tax and all associated penalties, the Court is deprived of subject matter jurisdiction of the appeal.

---

<sup>15</sup>The District of Columbia Court of Appeals specifically adopted the identical principle as enunciated by the United States Court of Appeals for the District of Columbia Circuit in District of Columbia v. Berenter, 151 U.S.App.D.C. 196, 466 F.2d 367 (1972).

Further, the District of Columbia Court of Appeals has declared that a petitioner cannot cure a subject matter jurisdiction defect by paying the penalty subsequent to filing the appeal. First Interstate Credit Alliance, Inc. v. District of Columbia, 604 A.2d 10, 12 and n.3 (1992).<sup>16</sup>

The law is firm: all taxes, interest, and penalties must be paid prior to the filing of an appeal in the Superior Court. This is a bright line rule that epitomizes "the principle of 'pay first and litigate later' . . . ." Allen v. Regents of the University System of Georgia, 304 U.S. 439, 456 (1938); see First Interstate Credit Alliance, Inc. v. District of Columbia, supra, 604 A.2d at 13 n.5.

Petitioner has presented no evidence whatsoever to substantiate its conjecture that the Department of Finance and Revenue might have waived the penalty assessed for tax year 1990. As a result, petitioner has not proffered any admissible evidence of a disputed material fact so as to warrant denial of the Government's motion for summary judgment for tax year 1990.

The law is clear that in order to defeat a motion for summary judgment, the opposing party must proffer

---

<sup>16</sup>In First Interstate Credit Alliance, Inc., the issue was the failure to completely pay interest, rather than penalties, as such. However, the legal principle is the same when applied to both tax-related obligations.

"competent evidence admissible at trial. . . ." Nader v. de Toledano, 408 A.2d 31, 48 (D.C. 1979). It is insufficient to provide merely a prediction or bald claim that evidence will be forthcoming at trial or that it might exist. The opposing party must produce something more than a mere statement that the factual issue is disputed. Id., citing Bushie v. Stenocord Corp., 460 F.2d 116, 119 (9th Cir. 1972).

In the instant case, the petitioner has never actually stated that the Government waived payment of penalties -- only that the Government can do so as a discretionary matter, if it so chooses.

The petitioner has never provided anything so brief as an affidavit in which an affiant states under oath that he or she recalls a particular letter or conversation in which any government official purportedly executed such a waiver. If any such thing actually happened, the incident would have been clearly articulated by now.

The whole notion of permitting discovery at this point would be nothing more than sanctioning a fishing expedition. In the context of opposing a motion for summary judgment, that is a weak and inappropriate setting in which to deny the motion.

Therefore, petitioner's appeal for tax year 1990 must be dismissed for lack of subject matter jurisdiction.<sup>17</sup>

WHEREFORE, it is by the Court this 7<sup>th</sup> day of July, 1995


ORDERED that petitioner's Motion for Summary Judgment with regard to tax years 1987, 1988, 1989 and 1991 is GRANTED; and it is

FURTHER ORDERED that petitioner's Motion for Summary Judgment with regard to tax year 1990 is DENIED; and it is

FURTHER ORDERED that respondent's Motion for Summary Judgment with regard to tax years 1987, 1988, 1989 and 1991 is DENIED;

FURTHER ORDERED that respondent's Motion for Summary Judgment with regard to tax year 1990 is GRANTED; and it is

FURTHER ORDERED that judgment shall be entered according to a proposed judgment embracing all refund calculations, to be submitted by petitioner to the Court, within 30 days hereof, pursuant to Rule 15 of the Tax Rules.

  
Cheryl M. Long  
Judge

---

<sup>17</sup>This turn of events is unfortunate for the petitioner. In light of this Court's interpretation of the constitutional issue on the merits, there should be no tax liability whatsoever for 1990. The Court, however, cannot ignore a jurisdictional defect and the District ironically reaps the financial benefit of how these issues now collide.

Therefore, petitioner's appeal for tax year 1990 must be dismissed for lack of subject matter jurisdiction.<sup>17</sup>

WHEREFORE, it is by the Court this 7<sup>th</sup> day of July, 1995

ORDERED that petitioner's Motion for Summary Judgment with regard to tax years 1987, 1988, 1989 and 1991 is GRANTED; and it is

FURTHER ORDERED that petitioner's Motion for Summary Judgment with regard to tax year 1990 is DENIED; and it is

FURTHER ORDERED that respondent's Motion for Summary Judgment with regard to tax years 1987, 1988, 1989 and 1991 is DENIED;

FURTHER ORDERED that respondent's Motion for Summary Judgment with regard to tax year 1990 is GRANTED; and it is

FURTHER ORDERED that judgment shall be entered according to a proposed judgment embracing all refund calculations, to be submitted by petitioner to the Court, within 30 days hereof, pursuant to Rule 15 of the Tax Rules.

  
Cheryl M. Long  
Judge

---

<sup>17</sup>This turn of events is unfortunate for the petitioner. In light of this Court's interpretation of the constitutional issue on the merits, there should be no tax liability whatsoever for 1990. The Court, however, cannot ignore a jurisdictional defect and the District ironically reaps the financial benefit of how these issues now collide.

Copies mailed to:

John J. McAvoy, Esq.  
White & Case  
1747 Pennsylvania Avenue, N.W.  
Washington, D.C. 20006

Joan Stentiford Ulmer, Esq.  
Assistant Corporation Counsel  
441 Fourth Street, N.W.  
Suite 1060  
Washington, D.C. 20001