



Tax Court Confirms Constitutionality of Minnesota Estate Tax

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On December 12, 2022, the Minnesota Tax Court released an opinion in *Estate of Anderson v. Commissioner of Revenue* addressing the constitutionality of Minnesota's estate tax structure as applied to an estate that consisted mostly of non-Minnesota assets. As the first court case to address Minnesota's estate tax scheme in many years, the court's opinion provides a valuable primer for professional fiduciaries and others on the fundamentals of state estate taxation.

Background

The case involved the Estate of Jeanette Anderson, who died as a Minnesota resident in 2018. The Estate consisted entirely of a revocable trust valued at approximately \$6.9 million — significantly above the Minnesota estate tax exemption then in effect (\$2.4 million). However, only a little over \$1 million of the assets held in the revocable trust had a Minnesota situs. The rest were located in South Dakota, where Ms. Anderson had previously resided.

The Estate paid Minnesota estate tax but subsequently requested a refund, arguing that it was improperly taxed on property located out of state. The Commissioner of Revenue denied the request for a refund, and the Estate duly appealed the dispute to the Minnesota Tax Court, raising both due process and dormant commerce clause constitutional challenges to Minnesota's estate tax scheme.

The Opinion

The court began its analysis of the dispute by outlining in general terms how Minnesota's estate tax is calculated. First, the court noted that the basis of Minnesota estate tax is the "Minnesota taxable estate," which is related to but ultimately distinct from the federal taxable estate. Second, the court observed that the actual estate tax paid must be calculated based on the "apportionment ratio." This ratio serves to separate out that portion of the decedent's overall gross estate that is insufficiently connected to Minnesota to allow state taxation. Once the apportionment ratio has been determined, calculating the estate tax imposed is a simple matter of multiplying that ratio by the Minnesota taxable estate and the applicable tax rate.



The court next turned to address the Estate's constitutional arguments. With regard to due process, the Estate contended that the Minnesota estate tax scheme is unconstitutional because it imposed an estate tax that would not have been imposed if non-Minnesota property was wholly excluded in calculating the Minnesota taxable estate. In other words, had the \$5.9 million of Ms. Anderson's estate that was located in South Dakota been excluded from the taxable estate, the remaining portion (\$1 million) would have slid comfortably below the Minnesota estate tax exemption amount.

While acknowledging that tangible personal property and real property may only be constitutionally subjected to taxation in the state of situs, the court entirely rejected the Estate's argument. In so holding, the court centered in upon the key role played by the apportionment ratio in determining the estate tax due. In the court's view, although the Minnesota taxable estate includes the value of out-of-state property, the apportionment ratio serves to ensure that the end tax is applied only to the proportional share of the estate that is tied to Minnesota. At bottom, the court found that although 84 percent of the Estate's value was due to property located in South Dakota, the apportionment ratio properly ensured that the actual tax was only based on the value of the remaining 16 percent. Thus, the Minnesota estate tax scheme did not violate the Estate's due process rights by improperly taxing out-of-state assets.

Finally, the tax court examined the Estate's argument that Minnesota's estate tax places an undue burden on the national economy in violation of the dormant Commerce Clause. Applying a detailed, four-prong analysis, the court concluded that the tax carefully excludes out-of-state property from taxation through the apportionment ratio and thus passes constitutional muster.

Conclusion

As the first Minnesota court case to address the estate tax in many years, *Estate of Anderson* provides a valuable look at the constitutional basis for state estate taxation. By addressing a frequent source of misunderstanding among taxpayers with extensive assets out of state — how Minnesota accounts for the value of those assets without directly taxing them — the opinion also provides important clarity to a technical subject. This serves as an important reminder to advisors to be cautious about explaining the Minnesota estate tax to clients as the "fine print" can have a huge impact on the overall estate plan.

The full text of the court's opinion may be found here, or on Westlaw at 2022 WL 17588033. If you have questions about *Estate of Anderson* or about Minnesota estate tax generally, please contact Jim Thomson or your regular Lathrop GPM Trust, Estates & Legacy Planning contact.