STATE OF NORTH CAROLINA	**IN THE GENERAL COURT OF JUSTICE SUPERIOR COURT DIVISION 12 CVS 8740**
The Kimberley Rice Kaestner 1992 Trust,)) **Plaintiff,**)) **v.**)) **North Carolina Department of Revenue,**)) **Defendant.**)	**DEFENDANT'S MOTION FOR SUMMARY JUDGMENT**

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EXHIBIT 1

Joseph Lee Rice, III Family 1992 Trust
EIN #[redacted]6609
Form IT-205 Amended
FYE 12/31/05

Explanation of Changes

The Joseph Lee Rice, III Family 1992 Trust (the "Trust") was established on December 30, 1992 by Joseph Lee Rice, III, then a resident of the State of New York. Since 1995, the Trust has been administered solely by a trustee domiciled outside of the State of New York. The entire corpus of the Trust consists of intangible assets. During the tax year 2005, the Trust received a negligible amount of New York source income from certain of its investment assets. The return for the tax year 2005 is being amended to reflect that

the Trust was not required to file a New York resident fiduciary return for that year. Instead, this return now reports only the amount of New York source income, $2,165, received by the Trust in the period from January 1, 2005 through December 31, 2005.

Based on the doctrine established by *Mercantile-Safe Deposit and Trust Company* v. *Murphy*, 15 N.Y.2d 579, 203 N.E.2d 490, 255 N.Y.S.2d 96 (1964) and its progeny (as acknowledged by the New York Department of Taxation and Finance with the adoption of 20 NYCRR §105.23(c) (2003), and thereafter by the New York Legislature with New York Tax Law §605(b)(3)(D)), the Trust is not required to pay income tax on the non-New York source income collected from January 1, 2005 through December 31, 2005.

In the past, courts in New York and elsewhere have carefully examined whether a state's taxation of a trust satisfies the requirements of the Due Process Clause of the U.S. Constitution. Beginning with *Mercantile-Safe Deposit & Trust Co.* v. *Murphy*, 15 N.Y.2d 579, 203 N.E.2d 490, 255 N.Y.S.2d 96 (1964), New York courts have struck down resident taxation of trust based solely on the domicile of the donor or beneficiaries of the trust. We are aware of no court decision supporting the taxation of the Trust as resident (and therefore subjecting to New York income tax all of the worldwide income of the Trust) based on the Trust's indirect receipt of a negligible portion of its income from New York sources even though the Trust has no trustees or assets located in New York State.

Taxation of the Trust as a resident would violate the two requirements under the Due Process Clause for resident taxation of all the Trust's worldwide income. First, the Trust did not have sufficient contacts with New York from January 1, 2005 through December 31, 2005 to permit such taxation. The Trust's only contacts with the State in 2005 were the domicile of its donor at the time the Trust was created many years earlier and a negligible amount of income from intangible assets – both contacts that New York courts have held to be constitutionally insufficient to support taxation as a resident trust. The State did not provide any benefits to the Trust, much less benefits sufficient to support the resident taxation of all of the Trust's worldwide income.

Second, unless applied to the Trust's income in the manner reported in this amended return, the State's tax regime (and in particular, Tax Law §605(b)(3)(D)) would not provide for any apportionment to take into account the extent of the Trust's activities in the State. Under the Due Process Clause, a taxing jurisdiction may constitutionally tax an entity's income only in proportion to that entity's activities in that jurisdiction. The taxation of 100% of the Trust's worldwide income in 2005 – when only .092% (.00092) of such income was indirectly received from New York sources – would not in any way even attempt to correspond to the true value of the Trust's income derived indirectly from activities in New York. In fact, the tax paid on the original return was 131 times the amount of New York source income.

We urge the Department to avoid these constitutional difficulties by refunding the total payments made on account to date, consistent with the application of Tax Law §605(b)(3)(D) in a manner respectful of the requirements of the Due Process Clause.