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Income Tax

Interest and Dividends of Nonresident Trust Beneficiaries

According to La. R.S. 47:300.3(2),

“Nonresident estates or trusts are subject to the tax upon the income earned within or derived from sources within this state. Income earned within or derived from sources within this state means income allocated and apportioned to Louisiana pursuant to R.S. 47:241 through 247.”

According to La. R.S. 47:243(A),

“Items of gross allocable income shall be allocated directly to the states from which such items of income are derived, as follows: ... (4) Other interest, dividends and profits from sales and exchanges of capital assets consisting of incorporeal property or rights shall be allocated to the state in which the securities or credits producing such income have their situs, which shall be at the business situs of such securities or credits if they have been so used in connection with the taxpayer’s business as to acquire a business situs, or, in the absence of such a business situs, shall be at the legal domicile of the taxpayer in the case of an individual or at the commercial domicile of the taxpayer in the case of a corporation; ...”

While it is theoretically possible for a security producing interest and dividends to acquire a business situs, such an eventuality is exceedingly rare. As such, in most instances, interest and dividends of trust beneficiaries will be allocated to the legal domicile of the individual taxpayer.

In addition, the stated intent of the legislature in enacting income tax on estates and trusts can be found at La. R.S. 47:300.4 which states,

“This part is intended to conform to the Louisiana income tax on estates and trusts law to the Internal Revenue Code of 1986, as amended (26 United States Code) except as otherwise provided, for the purpose of: (1) simplifying preparation of Louisiana income tax returns by taxpayers; (2) improving enforcement through better use of federal information; and (3) aiding interpretation of the income tax law through increased use of federal ruling, regulations, and jurisprudence, where applicable.”

As such, it can be seen that the legislature carved out an exception for the use of federal interpretations where state law is silent, as in this instance.

According to 26 C.F.R. 652(b), any amounts includible as gross income of the beneficiary “shall have the same character in the hands of the beneficiary as in the hands of the trust.” As such, for purposes of federal law, distribution to the beneficiaries does not change the status of the income. Federal regulations go on to state that the tax treatment of the amounts distributed

depends on the status of the beneficiary, not the status of the trust. As such, the domicile of the beneficiary is the deciding factor. In applying this to Louisiana law, the interest and dividends would retain their status even after it is distributed and in the hands of the beneficiary.

In conclusion, the designation of situs is properly based upon the characteristics of the taxpayer, including the taxpayer's domicile, not on the characteristics of the trust itself. With this in mind, a nonresident trust beneficiary would not have to pay taxes on Louisiana trust distributions as long as the income can be properly sourced to the nonresident beneficiary's domicile in another state.