

NY, I Can't Seem To Quit You (As My Tax Domicile)

By **Lance Rothenberg** (March 26, 2018, 1:15 PM EDT)

Perhaps all tax audits are frustrating, but a New York personal income tax residency audit may be the most intrusive and frustrating type of audit to endure. A residency audit queries where a taxpayer lives, how she spends time, where she spends time and with whom she spends time. The questions and answers delve into the intimate, private life of a taxpayer to trace her comings and goings into and out of a jurisdiction. Cellphone records, credit card bills, family connections, business dealings, E-ZPass statements, details of home furnishings, bank statements, locations of vehicles, even medical records are all fair game in a residency audit.



Lance Rothenberg

The audit's purpose, of course, is to determine whether an individual taxpayer has properly reported her income and paid the correct amount of tax. Essentially, the state has three methods to impose taxation: (1) domicile taxation (i.e., the taxpayer's true home); (2) statutory residency taxation (i.e., domicile is elsewhere but the taxpayer's connections to the state are sufficient to treat her as a resident); and (3) nonresident taxation (i.e., taxation of in-state sourced income). More than most states, New York aggressively enforces its residency audit program and has enlisted a small army of residency auditors to verify the accuracy of a taxpayer's filing classification and calculation of tax.

Some taxpayers and their advisers mistakenly believe that obtaining a driver's license in a new state, for example Florida, and keeping travel in New York below six months will be enough to establish a new residency and save tax. Nothing could be further from the truth. These audits are necessarily highly fact-intensive. They require a painstaking review of voluminous records that document the taxpayer's intentions, whereabouts and movements. Let's take a brief look at the rules.

Domicile

A taxpayer may have more than one residence, but he can have only one "domicile." An individual's domicile is his true, fixed, permanent home. It's the place he returns to after having been absent.^[1] In effect, domicile requires both a subjective intention and physical presence within the jurisdiction. The critical question in a residency audit is to determine whether a taxpayer has changed his domicile from New York to a new state as of a given point in time.

A taxpayer's domicile does not change until he can demonstrate that he has abandoned New York and established a new, permanent, fixed home outside of New York. In other words, a taxpayer must both

“leave” New York and “land” in a new jurisdiction. This change must be supported by evidence that is clear and convincing. The burden of proof rests with the party asserting the change; typically, the taxpayer.

While domicile is a question of subjective intent, objective proof is required to satisfy an auditor. An individual can purchase a new home in Florida while keeping his historic home in New York, but which is his true home for tax purposes? As such, New York looks to five primary factors in evaluating a claim of a change of domicile.[2]

1. Home Factor: comparison of size, value and usage in each jurisdiction;
2. Business Factor: comparison of business ties in each jurisdiction;
3. Time Factor: comparison of days spent in each jurisdiction;
4. Near and Dear Items Factor: comparison of where a taxpayer keeps financially and sentimentally important items that make a home a home; and
5. Family Factor: comparison of family members in each jurisdiction.

An examination of these factors probes deeply into the taxpayer’s patterns and habits of living. Where does he work? Is he married? Where does his spouse live? Where do his children attend school? Where does he park his car? How does he use each home? Who else is using each home? What are his ties to each community? How much time is he spending in each jurisdiction? What is the quality and nature of the time spent in each jurisdiction? If you claim you live in Florida, but your children go to school in Westchester and you work in Manhattan, something might be wrong with your tax return.

Only after first examining the five primary factors, will residency auditors look to secondary factors, such as a taxpayer’s driver’s license, voter registration, auto registration, etc. These data points can be very important in telling a complete story, but they obviously can be more easily manipulated than the primary factors.

Statutory Residency

Where an individual is domiciled outside of New York, she may still be taxed as a “statutory resident” of New York where her connections to New York are of a certain caliber and exceed a certain threshold. Statutory residency is a two-prong test: (1) the individual must maintain a permanent place of abode in New York; and (2) she must spend, in the aggregate, more than 183 days of the year in New York.

A typical example might be an individual who is domiciled in New Jersey, who owns an apartment in Manhattan and commutes to Manhattan for work. This individual may very well meet both prongs of the statutory residency test, but, then again, maybe not.

What does it mean to maintain a permanent place of abode?[3] Does she use the city apartment or does she lease it out to a third-party? Is the third-party a stranger under an arm’s length lease or does she rent to her son? Is it a one-bedroom or a two-bedroom unit? Is the second bedroom a spare or is it occupied by someone other than the taxpayer? Was the unit fully habitable during the audit period? Was it undergoing major renovations such that it did not have running water or perhaps it lacked heat during winter months? Does the taxpayer receive mail at the city apartment? Does she have a key? Does

she have unfettered access?

What does her day count look like? Let's say she commutes from New Jersey to Manhattan for work. If she spends more than 183 days in New York, this element of the test is met. For these purposes, any part of a day counts as a day in New York. Overnights are not required; a casual lunch in Long Island on a Saturday or catching a Broadway musical on a Sunday will count as a day. Does she travel for work? How often? Does she telecommute? If she travels, what evidence exists to document that her day count is under 184 days?

Consider a different individual who is domiciled in Florida, but who owns an apartment in Manhattan and travels to New York for both work and pleasure frequently. This taxpayer would seem to have an abode in New York, but has she spent 184 days in New York? Her calendar, travel patterns, airline flights, cellphone calls and credit card statements, to name a few sources of information, will all be highly relevant to plotting her whereabouts on each day of the year under audit.

These hypothetical scenarios can be as varied and nuanced as the real-world lives of each individual taxpayer. If an individual has the good fortune to have access to two homes, one in New York and one elsewhere, the details of her personal life can be opened up for examination by a residency auditor.

Nonresident Allocation

Where a taxpayer has successfully established that he is domiciled outside of New York and does not qualify as a statutory resident, he may still face scrutiny in a residency audit to determine whether he has properly reported any income generated within New York on his nonresident income tax return. Does he have rental income from realty in New York? Does he travel to New York for work? An income allocation audit may require the same level of detail of plotting days on a calendar to determine whether an individual was in New York for work and was earning income from services performed while in New York. There are numerous degrees of complexity depending upon the types of income earned during the audit period.

Recent Cases

Residency audits are often lengthy and grueling contests. They can become highly contentious. The auditors, essentially, are second-guessing, today, an individual's life decisions that were made last year or even three years ago. Perhaps more appropriately, the auditors would say, they are merely putting the taxpayer to his proof. Nevertheless, the potential tax exposure can range from substantial to tremendous. For these reasons, taxpayers frequently appeal audit findings, and many wind up in expensive and protracted litigation.

There are at least three noteworthy cases from 2017 that merit attention here to better illustrate the twists and turns common in a New York residency audit. One involves a beloved dog. Another involves a long-lost love. Another drills down on what is required for a second home to constitute an abode for purposes of statutory residency.

In *Matter of Blatt*,^[4] the taxpayer moved from New York to Texas for a new job. Gregory Blatt initially had reservations about leaving Manhattan, so he maintained a residence in each state. However, he soon adjusted and over time committed to "living" in Texas. After a relatively short period of time, though, he accepted a different position, which required he return to New York. While he was living in Texas, he stopped paying tax to New York as a resident for that period. Under the circumstances, the

auditors were skeptical of the bona fides of his change of domicile.

Among the various domicile factors listed above, one category addresses a taxpayer's "near and dear" items. In short, these are the contents of a house that make it a home. These items may be financially or sentimentally valuable. They are as peculiar to each taxpayer as the individual lives led. For Blatt, this was his dog. The court was particularly persuaded by evidence introduced at trial that once Blatt committed to living in Texas, he moved his beloved dog from New York to Texas. He prevailed at trial. Perhaps there is no greater love than that shared with man's best friend. Or, is there?

In *Matter of Patrick*,^[5] the taxpayer lived in New York, worked long hours at his job in Manhattan, and never forgot about his high school sweetheart, Clara, who had abruptly moved to Italy years earlier. After dealing with certain medical issues, Stephen Patrick reexamined his life, initiated divorce proceedings against his spouse, and promptly began searching for Clara, who it turns out had settled in Paris, also in an unhappy marriage. After tracing Clara down, the two reunited, and promptly made plans to marry. She lived in Paris, he in New York. Once their respective divorces finalized, they married, he retired, and he moved to Paris while keeping his Manhattan residence. If home is where the heart is, his heart was in France.

The residency auditors, however, looked at this set of facts and concluded that Patrick had not proven that he changed his domicile to France. As a general matter, overseas domicile changes are more complicated than moves within the U.S. Nevertheless, at trial, a judge ultimately agreed that Patrick had abandoned his New York domicile and had taken sufficient steps to establish Paris as his new home. A careful and nuanced presentation of the underlying facts, aided by credible testimony at a two-day trial, were required in order to defeat the auditors' assertions that they knew Patrick's heart better than he did.

The last case is perhaps not as dramatic but is equally as important. In *Matter of Mays*,^[6] the New York Tax Appeals Tribunal examined what it means to maintain an abode in New York for purposes of statutory residency. This has been a hotly contested issue in recent years. In 2014, New York's highest court decided the *Gaided* case^[7] and concluded that a taxpayer must have a residential interest in an abode before it can be counted against him. Since then, however, auditors have interpreted that case one way, while taxpayers have interpreted it another.

In summary, Leslie Mays was domiciled outside of New York City, and she argued that a temporary, corporate apartment available to her in Manhattan did not qualify as her abode for purposes of statutory residency. Examining prior case law, the Tribunal walked through the proper analysis to be used to make these determinations. Does the dwelling exhibit physical characteristics for year-round habitation? Does the taxpayer have a legal right to occupy the dwelling? If the taxpayer does not, does she nevertheless have access to and use of the dwelling? If she has a legal right, has she exercised that right by enjoying her residential interest in it? While Mays lost her case, this analysis will surely aid other taxpayers grappling with their own statutory residency audits.

Lance E. Rothenberg is of counsel with Tenenbaum Law PC. Rothenberg focuses on state and federal tax controversies and disputes.

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[1] See 20 N.Y.C.R.R. 105.20(d); see also *Matter of Newcomb*, 192 N.Y. 238 (N.Y. 1908).

[2] See, e.g., NY Nonresident Audit Guidelines (2014).

[3] See *Gaied v. New York State Tax Appeals Tribunal*, 22 N.Y.3d 592 (N.Y. 2014) (concluding a taxpayer must have a residential interest in the abode).

[4] *Matter of Blatt*, DTA No. 826504 (Div. Tax App. 2017).

[5] *Matter of Patrick*, DTA No. 826838 (Div. Tax App. 2017).

[6] *Matter of Mays*, DTA No. 826546 (Tax App. Trib. 2017).

[7] *Gaied*, 22 N.Y.3d 592, *supra*.