The SALTy Exodus: Tax Cuts and Jobs Act

By Hana M. Boruchov*

Hana M. Boruchov discusses the problems created at the state and local level, with emphasis on her home state of New York.

Arguably, one of the most salient and contentious modifications to the tax code under the Tax Cuts and Jobs Act ("TCJA") has been the limitation of individual taxpayer deductions for state and local taxes ("SALT") to $10,000 ($5,000 for married filing separate) per year. On February 22, 2019, the Treasury Inspector General for Tax Administration ("TIGTA") released its audit report *Review of the Issuance Process for Notice 2018-54*.[1] The Chairman of the U.S. House of Representatives Committee on Ways and Means requested TIGTA to conduct an audit "concerning the prioritization and issuance of IRS Notice 2018-54, *Guidance on Certain Payments Made in Exchange for State and Local Tax Credits*."[2] According to TIGTA findings, for the 2018 tax period, an estimated 10,880,570 taxpayers would be subject to the SALT limitation, totaling $323,127,515,630 paid above the SALT limitation.[3] Although final figures are not available yet for this filing season, taxpayers in states such as New York, California and New Jersey, with proportionately higher property, state and local income taxes likely felt the effects of the SALT limitation.

Concerns about the potential effect of TCJA in New York were voiced before and after the law's enactment. On February 4, 2019, in a press release on New York State Revenues and the Impact of SALT, New York Governor Cuomo announced that New York State had experienced a $2.3 billion decrease in revenues from December 2018 to January 2019.[4] According to Governor Cuomo, the shortfall was a causal effect due to the TCJA SALT limitation, ultimately costing New York $14.3 billion in revenues. Governor Como noted that the federal SALT changes have resulted in numerous states suffering diminished revenues, adding that revenues have decreased by 50% in New York, 35% in New Jersey, 55% in Connecticut, 50% in Massachusetts and 24% in California.[5]

Governor Cuomo stated "SALT encourages high-income New Yorkers to move to other states … [t]axpayers are adjusting in response to SALT. These are educated, financial people by definition. They are investors, they've earned a lot of money, they're working with accountants, they're working with investment

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advisors. They're making informed decisions. We have been hearing all along from the major accounting firms, to major individuals, that this is going to be the tipping point and that people now will be making a decision to make a geographic location change."[6]

According to the United Van Lines' 42nd Annual National Movers Study, which tracks domestic migration of its customers, 61.5% of moves were outbound from New York in 2018.[7] In 2018, New York ranked fourth in the highest percentage of outbound moves as compared to other states.[8]

It is important for practitioners to be aware of New York residency rules or to consult a tax professional who is familiar with the rules to avoid potential pitfalls.

There is anecdotal evidence that points to the shortfalls experienced by high SALT states attributable to reduced tax revenues historically collected from high income earners proximately coinciding with the enactment of TCJA. However, there is no direct correlation linking taxpayer migration to SALT caps. At least for New York, there may be other pertinent factors causing wealthy taxpayers to leave the state such as the high cost of living, overcrowding, weather, family, employment relocation, *etc*. Significantly, as of January 2019, the New York estate tax threshold exemption was raised to $5,740,000.[9] New York estate tax rates are graduated from 3.06% up to 16%. Larger estates exceeding the 105% threshold exemption risk falling off "the cliff" and paying tax on the entire estate. The estate tax alone may be adequate incentive for a wealthy New Yorker to avoid New York residency status (only domicile is determinative for estate tax purposes).

As seemingly increasing numbers of high income earning New Yorkers flee to states with more favorable state and local tax rates, tax practitioners should anticipate that New York State may up the ante on its residency audits. As a tax practitioner, you may find yourself in the position to advise your clients on statutory residency or domicile rules. Pursuant to New York Tax Law §605(b), a New York resident is an individual either domiciled within the state or an individual "who is not domiciled in [the] state but maintains a permanent place of abode in [the] state and spends in the aggregate more than one hundred eighty-three days of the taxable year in [the] state …." These residency rules can be confusing and handling a residency audit can be quite a *taxing* process. Having a basic understanding of how the rules are applied can make a difference between whether or not your client is classified as a New York resident for tax purposes during your next audit.

I. Domicile

New York defines domicile as the place where the taxpayer intends to have as his fixed, permanent home and where the taxpayer returns after a period of absence.[10] Taxpayers may have multiple residences at one time, but only one domicile at a time.

The party asserting the change in domicile bears the burden of proof through clear and convincing evidence. The party asserting the change must demonstrate that the taxpayer has abandoned the New York residence and has established a new, fixed, permanent home outside of New York.

When establishing the taxpayer's intent to change domicile, the taxpayer's subjective intent is proven through objective means. New York utilizes five primary factors in assessing a change of domicile claim.[11] The five primary factors are home, active business involvement, time, items near and dear, and family connections. The home factor analyzes the nature of the use of as well as the physical and fiscal characteristics of the taxpayer's New York residence in contrast to the taxpayer's out of state residence. The active business involvement factor examines the taxpayer's employment patterns and whether he or she actively or passively participates in business activities. The time factor compares the amount of time the taxpayer spent in New York as against all other places the taxpayer spent time in throughout the year. The items near and dear factor considers the physical location of the taxpayer's most valuable items. Value can be sentimental or monetary. The family connections factor assesses the physical location of the taxpayer's spouse, minor children and other close family members.

No single factor is determinative in whether a taxpayer will be considered a domiciliary of New York. Rather, the factors are used to illustrate the taxpayer's pattern of lifestyle that establishes whether a change from the prior domicile to the new domicile occurred.

Although not as heavily weighted, New York will also consider other ancillary factors in its domicile analysis. Some other factors include the taxpayer's state driver's license registration, affiliation with local religious

organizations or clubs, location of the taxpayer's banking institutions, homestead exemptions, as well as voter and vehicle registration.

II. Statutory Residency

Even if domicile is proven to be outside of New York, the taxpayer may still qualify as a statutory resident under New York Tax Law §605(b)(1)(B). A taxpayer may qualify as a statutory resident if (1) the taxpayer maintains a permanent place of abode in New York, and (2) spends more than 183 days of the year in New York.[12]

Under New York Tax Law, a permanent place of abode is a dwelling place that is suitable for year round habitation and is maintained for substantially all of the year by the taxpayer. Under New York case law,[13] ownership interest in the property is irrelevant for purposes of a statutory residency audit analysis; rather it is the taxpayer's residential interest in the dwelling place that is closely scrutinized. Further, case law has shown that the taxpayer must have unfettered access to the permanent place of abode. This means that if the taxpayer is unable to access the residence at any time, such as in the case with landlord/tenant or sublet situations, as to that taxpayer, the residence may not qualify as a permanent place of abode. Similarly, if the taxpayer utilizes a corporate apartment and can prove that he or she does not have a dedicated room or space in the apartment and that the apartment is utilized by numerous individuals, the taxpayer may be able to avoid, a permanent place of abode. With respect to maintaining the abode, it should be noted that historically, New York has interpreted 11 months as substantially all of the year.[14]

A taxpayer's day count of the aggregate 183 days includes any portion of the day, no matter how short of a time the taxpayer stayed in New York. During an audit, New York may request or even subpoena the following documents for all periods involved: cellphone records, bank and credit card records, building swipe card records, personal diaries, schedules and calendars, and travel records. The burden of proof is on the taxpayer to demonstrate his or her location on any day. Further, any days that lack evidentiary substantiation may be counted in favor of New York. Therefore, it is imperative that a taxpayer maintains good records. However, certain exceptions may apply toward counting a day in New York, such as inpatient medical care and travel.

In summation, whether or not the TCJA SALT cap has had an effect on New York residency status has yet to be proven. Nonetheless, statistics do illustrate a large number of New York taxpayers migrating out of the state. It is important for practitioners to be aware of New York residency rules or to consult a tax professional who is familiar with the rules to avoid potential pitfalls.

ENDNOTES

* *Disclaimer: The information contained in this article does not constitute tax advice and is for informational purposes only.* Hana M. Boruchov is a tax attorney with Tenenbaum Law P.C., which is based in Melville, N.Y. Hana focuses on state and federal tax controversies and has experience assisting in the resolution of a wide variety of corporate and individual income, sales and use, payroll and employment tax matters. You can reach her at *hboruchov@litaxattorney.com* and at (631) 465-5000.

1 Review of the Issuance Process for Notice 2018-54, February 22, 2019, Reference Number: 2019-14-019. *See www.treasury.gov/tigta/auditreports/2019reports/201914019fr.pdf.*

2 *Id.*, at 2

3 *Id.*

4 *See www.governor.ny.gov/news/video-audio-photos-rush-transcript-governor-cuomo-and-comptroller-dinapoli-deliver-update-state.*

5 *Id.*

6 *See www.governor.ny.gov/news/video-audio-photos-rush-transcript-governor-cuomo-and-comptroller-dinapoli-deliver-update-state.*

7 United Van Lines' 42nd Annual National Movers Study 2018 *www.unitedvanlines.com/contact-united/news/movers-study-2018.*

8 *Id.*

9 Threshold amount is adjusted for inflation. *See www.tax.ny.gov/pit/estate/etidx.htm.*

10 20 N.Y.C.R.R. 105.20(d); *Matter of Newcomb*, 192 N.Y. 238 (N.Y. 1908).

11 NY Nonresident Audit Guidelines (2014) *www.tax.ny.gov/pdf/2014/misc/nonresident_audit_guidelines_2014.pdf.*

12 NY Tax L §605 (2015).

13 *Gaied*, 22 NY3d 592, *supra.*

14 *See www.tax.ny.gov/pubs_and_bulls/tg_bulletins/pit/permanent_place_of_abode.htm.*