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Should I Stay…Or Should I Go? Understanding Residency Rules

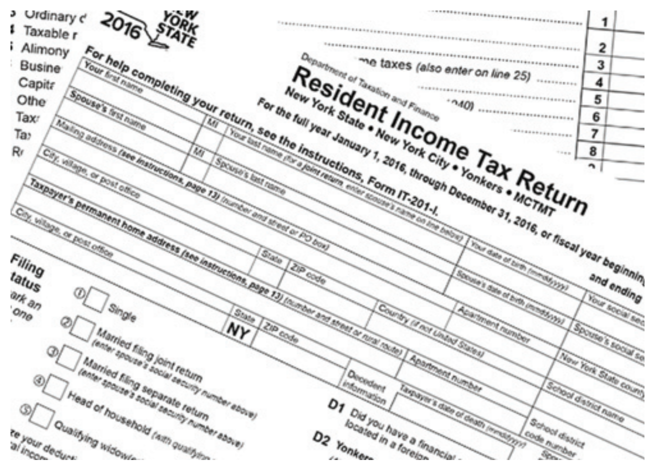
The actual process of ascertaining an individual's intentions regarding domicile—the crucial question in a residency audit—is a subjective inquiry for the auditor and often a difficult one.

By **Alvan Bobrow**

For many years, high net-worth taxpayers have been leaving New York and other high-tax Northeast states for low-tax states, primarily Florida. This exodus from New York and comparable states like California, Illinois and New Jersey has only accelerated starting in tax year 2018, after Congress changed the tax law to cap the annual deductions for state and local taxes paid at $10,000 for individuals. Moreover, the price of government is continuing to rise among high income earners as states consider a millionaire tax to close budget deficits. (States with no income tax: Alaska, Florida, Nevada, South Dakota, Tennessee, Texas, Washington, and Wyoming. A state with almost no income tax is New Hampshire.)

Asset manager Alliance Bernstein started its departure from New York to Nashville, Tenn. at the end of 2018. President and CEO Seth Bernstein in a press conference noted that moving the corporate headquarters will offer employees lower living expenses and housing costs, shorter commute time and of course no state income taxes on earnings (as compared to a New York state and city income tax rate of 13 percent and an estate tax rate of 16 percent).

Even former President Donald Trump tweeted last October 2019 that New York "will always have a special place in my heart" as he announced his relocation to Florida. Additionally, Elon Musk announced at the Wall Street Journal CEO Council Summit on Dec. 8, 2020, goodbye California (13.3% maximum personal income tax rate bracket), hello Texas (no income tax).



In New York State, like most states, a resident taxpayer is responsible for reporting and paying New York state personal income tax on income from *all* sources regardless of where the income is generated or the nature of the income. A nonresident taxpayer is given the opportunity to allocate income, reporting to New York state only that income actually generated in New York. In addition, the nonresident need only report to New York income from intangibles which are attributable to a business, trade or profession carried on in the state, not investment income. Thus, significant benefits may be derived from filing as a nonresident.

To be taxed as a resident, an individual must either be domiciled in New York or be a statutory resident (i.e., maintains a permanent place of abode in this state and spends more than 183 days of the taxable year in this state). (New York City rules are the same for determining who is a New York City resident.) As you see, the state gets two chances to make you a resident. For example, while I clearly changed my domicile to New Jersey and became a resident a number of years ago, if I maintained a pied-à-terre in Manhattan, I could still be treated as a resident of both states. While New Jersey would give me a credit for the personal service income initially taxed in New York, investment income would be subject to double taxation.

Domicile

In general, your domicile is:

• the place you intend to have as your permanent home;

• where your permanent home is located; or

• the place you intend to return to after being away (as on vacation, business assignments, educational leave or military assignment).

You can have only one domicile. Your historical domicile does not change until you can demonstrate that you have abandoned your old domicile and established a new one. There are frequent references to intent in the discussion of domicile. Intention is a decisive factor in the determination of whether any particular residence which a person may occupy is his or her domicile. Because the actual process of ascertaining an individual's intentions regarding domicile is a subjective inquiry for the auditor, an experienced negotiator is required to persuade the auditor on this crucial question.

The burden of proving a change of domicile is upon the party asserting the change, and in many states, the proof to effect a change of domicile is very high, requiring "clear and convincing" evidence. At times, the occurrence of a life event makes the domicile inquiry easier because it supports a typical pattern. Retirement, loss of job, the death of a spouse, a divorce and re-marriage or even the growing up of one's children often triggers a desire to change a lifestyle and domicile, which can reinforce a taxpayer's position.

Primary and Other Factors

To assist in determining whether the taxpayer's intentions are supported by his or her acts, the auditors consider five primary factors that allow them to make objective determinations. From these objective factors they draw an inference as to what the intent was.

The primary factors are:

(1) Home: The individual's use and maintenance of a New York residence for example, as compared to the nature and use patterns of a non-New York residence. Additionally, auditors consider the extent to which the taxpayer is involved with local community activities.

(2) Active Business Involvement: The active participation in a trade or business would imply that your domicile is the home nearby.

(3) Time: This factor is a quantitative and qualitative analysis of where the individual spends time during the year. The time spent in the departing state should not be the plurality of total days.

(4) Near and Dear: At which residence does the taxpayer keep sentimental items such as pets, antiques, fine art, etc.? Also, the location of medical records and financial records are a good indicator as to the location of one's domicile.

(5) Family Connections: An analysis of an individual's family connections (immediate family only) could be intrusive into one's private and personal lifestyle. The most important aspect of this inquiry is where minor children attend school since the inference is that the domicile is near the school.

If the five primary factors are inconclusive, the auditors are instructed to evaluate secondary or other factors such as voting and auto registrations, drivers' licenses, addresses used for tax returns and other legal documents (including testamentary documents), the location of safe deposit boxes, etc. I advise clients that taking care of these activities will generally not improve your position on domicile, but the failure to do them will be used against you.

Comment: To help them, the auditors are also looking for taxpayers who have claimed a Manhattan Parking Tax Exemption and submitted an application for a school tax relief exemption under the New York STAR program, which requires the applicant to be a resident.

The determination of an individual's domicile can often be facilitated by applying the accounting principle of a "T" account to the primary factors. By aligning the factors favoring one state (say, New York) on one side of the account and the factors favoring a domicile in another state (say, outside New York) on the other side, the taxpayer or an auditor is provided with a visual summary of the factors that will assist in coming to a conclusion. Auditors often need to be reminded to be open-minded and fair in evaluating all factors in a balanced and reasonable manner. (The tax law provides for certain statutory exemptions to the general rules discussed above. The rules known as the 30-Day Rule, N.Y. Tax Law §605(b)(1)(A)(i), and the Foreign Country Rule, N.Y. Tax Law §605(b)(1)(A)(ii), can eliminate liabilities for tax in New York.)

Statutory Residency

Even if a taxpayer succeeds on the domicile issue, any individual who maintains a permanent place of abode in the state is required to maintain records to show that he or she did not spend more than 183 whole or part days in the taxing state during the year. The burden of proof is on the taxpayer to show that he or she was present in New York for less than 184 days.

Residency planning is to avoid a situation where the taxpayer is domiciled say, outside New York but on audit is held to be a statutory resident of New York or another state. Both the state of domicile and the state of statutory residency will impose personal income tax on the taxpayer's entire income, without any credit for taxes paid to the other state on income from intangible assets. (Courts have ruled that taxing an individual twice on the same income does not violate the Commerce Clause of the U.S. Constitution nor New York's own constitution. See *Tamagni v. Tax Appeals Tribunal*, 91 N.Y.2d 530 (1999). As previously noted, the state of domicile would provide a credit for tax on wages paid to the other state.) Moreover, if found to be a statutory resident on the 184th day, all your compensation income and your investment income will be taxable for the full year.

Permanent Place of Abode. A permanent place of abode is defined in part as a "dwelling place of a permanent nature maintained by the taxpayer, whether or not owned by him," and will generally include a dwelling place owned or leased by his or her spouse. The dwelling place must be maintained for "substantially all of the taxable year" and the taxpayer must have "unfettered access" to the residence. An attorney can assist you in clarifying whether your living quarters constitute a permanent place of abode as well as clarifying issues relating to habitability and corporate apartments. The living quarters only have to be available for use, not actually used.

183 Day Test. A taxpayer who maintains a permanent place of abode must always be cognizant of his or her New York days to avoid the second part of the statutory residency test. That is, the taxpayer must prove that he or she spent less than 184 days in New York or the taxing state. Spending even one minute in New York is counted as a full New York day.

There are two instances where presence in New York does not count as a day:

- *Travel Days:* Presence in New York is disregarded if it is solely for "boarding a plane, ship, train or bus for a destination outside of New York State." As a caveat, auditors will attempt to disallow an exempt day if you shop in the airport stores on the way to the boarding gate.
- *Medical Days:* Inpatient care for an involuntary illness at a New York medical facility will not count as a New York day for statutory residency purposes. This is a limited exemption that does not extend to the spouse of an inpatient.

These exceptions are replete with special requirements which may also be clarified by consulting with an attorney.

Comment: Flying into New York at 9 p.m. to conduct business the next day and then flying out of New York at 5 p.m. still counts as two days.

Allocation

If successful and found to be a nonresident, the taxpayer can still be taxed on income that is derived from or connected with New York sources. Generally, this includes all items of income gain, loss and deduction that are attributable to: (1) the ownership of any interest in real or tangible property located in New York or (2) a business, trade, profession or occupation carried on in New York.

Even though not domiciled in or a resident of New York, if the above rules are applied to former President Trump, more likely than not he will still have an income tax liability to New York for income from personal services or generated by property he owns. But sooner rather than later he will learn that New York state has the most sophisticated residency audit program in the nation. If you are claiming to be a nonresident, be prepared for a personally intrusive examination that will keep going for some time. If you answer a knock at the door and the visitor says, "I'm from the Tax Department and I am here to help you," don't believe him or her. Say "No thanks!" and lock the door.

Key Takeaways

As previously stated, domicile is defined as the place an individual intends to be his or her permanent home, the place he or she intends to return to whenever he or she may be absent. Intention is a decisive factor in the determination of whether any particular residence which a person may occupy is his or her domicile. The actual process of ascertaining an individual's intentions regarding domicile—the crucial question in a residency audit—is a subjective inquiry for the auditor and often a difficult one. To help you learn the best practices when planning for a change in residency and to avoid pitfalls, a consultation with an attorney well-versed in residency issues is a logical first step. (To the courts, it is deeds and not words that generally matter. See *Matters of the Estate of James A. Trowbridge*, 266 N.Y. 283 (1935).)

Finally, a taxpayer that wishes to establish a new residency outside New York or another state need not sever all ties or contacts with New York or the former state. Once you understand the residency rules and how they operate, you will also understand the level of contacts that may be retained in the state you are leaving.

Alvan Bobrow *is a partner at Barton LLP based in New York with a focus on state and local, federal, and international taxation for clients.*