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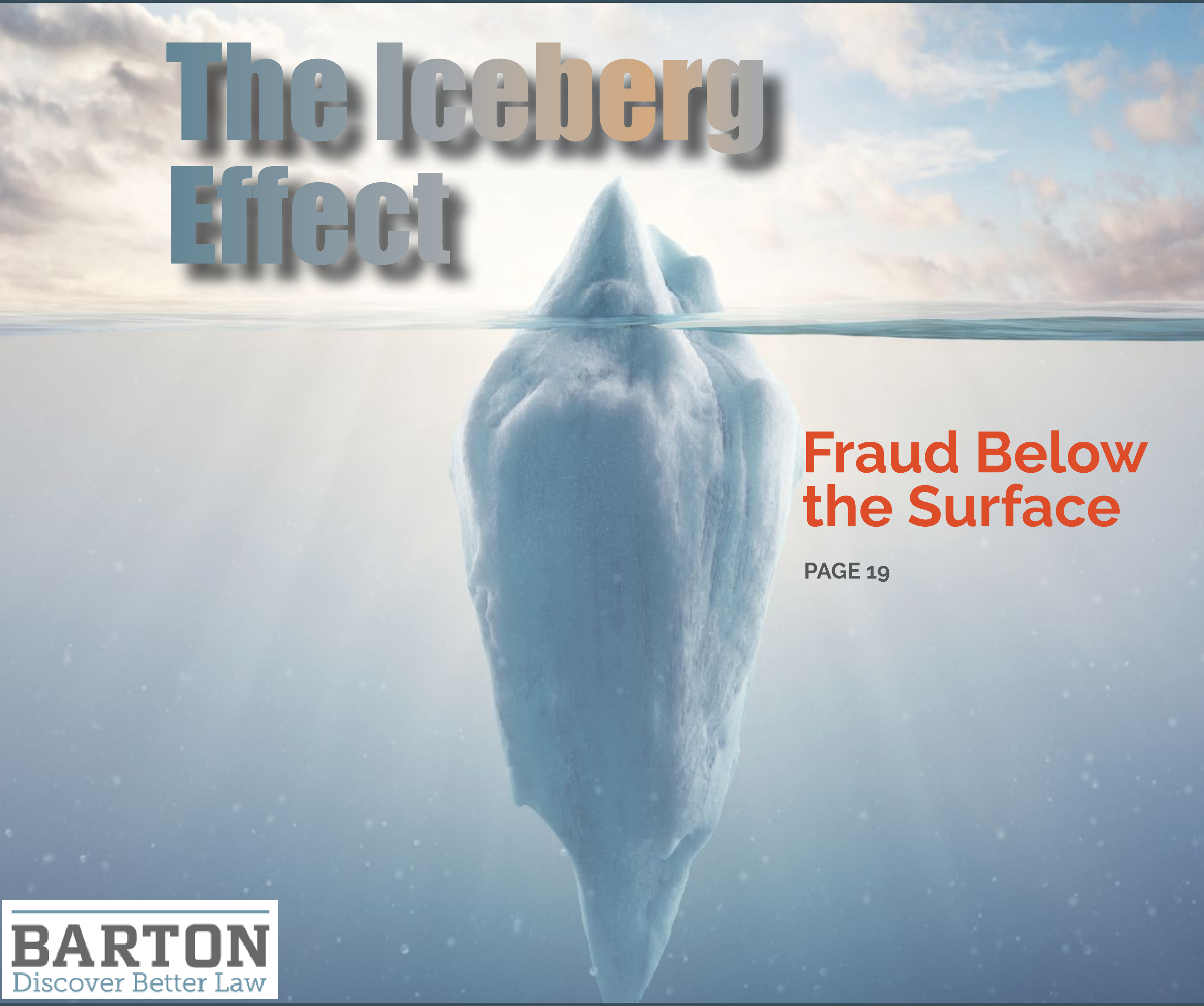

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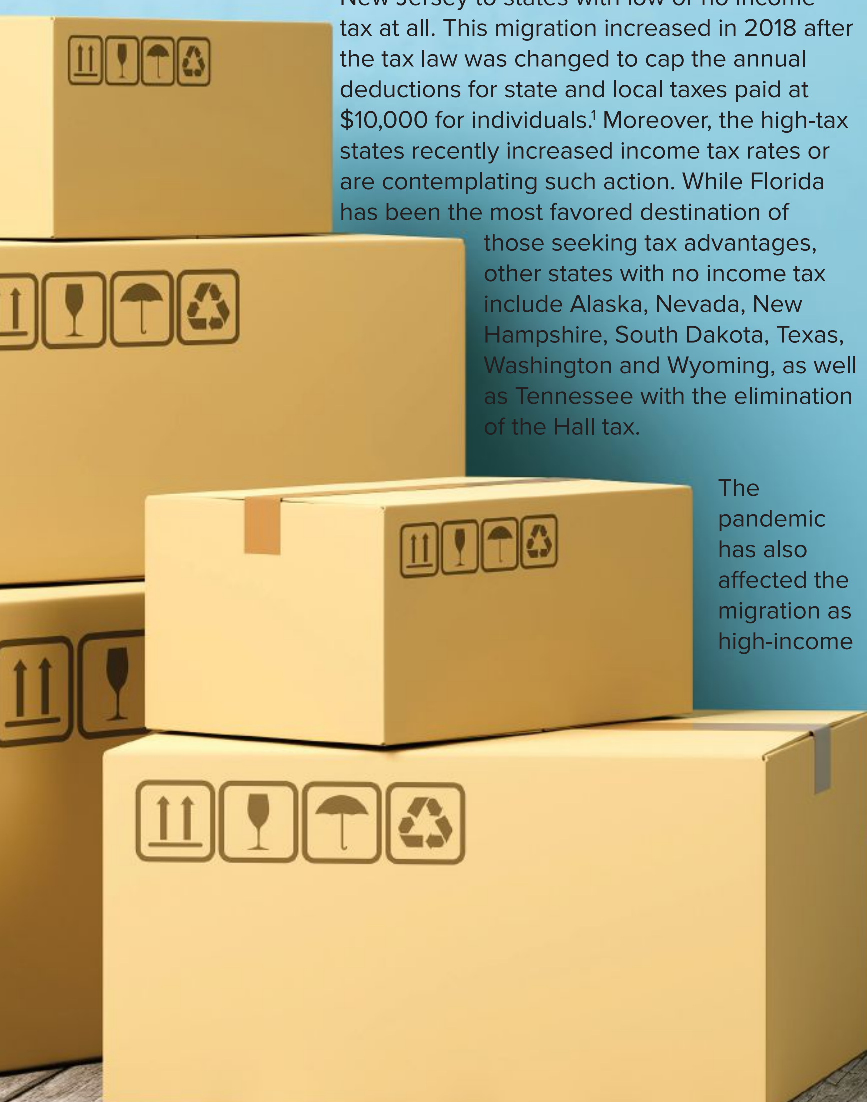
From New York to Tennessee: Residency and Tax Issues - Alvan L. Bobrow

# From New York to Tennessee
# Residency and Tax Issues

By ***Alvan Bobrow, Esq.***

Your newest client has just moved from New York to Tennessee to take advantage of the state's absence of income tax. However, they still own an apartment, have business contacts, and make frequent trips back to New York. At the risk of continuing to be taxed as a New York resident, your client rings you up and asks for help navigating New York's residency audit program, the most sophisticated in the nation. How can you assist your client in avoiding being deemed a New York resident?

Traditionally, high-net-worth individuals have often relocated from high tax states such as New York, California, Illinois and New Jersey to states with low or no income tax at all. This migration increased in 2018 after the tax law was changed to cap the annual deductions for state and local taxes paid at $10,000 for individuals.[1] Moreover, the high-tax states recently increased income tax rates or are contemplating such action. While Florida has been the most favored destination of those seeking tax advantages, other states with no income tax include Alaska, Nevada, New Hampshire, South Dakota, Texas, Washington and Wyoming, as well as Tennessee with the elimination of the Hall tax.



The pandemic has also affected the migration as high-income taxpayers have realized that they can work remotely. This is especially true of hedge funds. Carl Icahn (Icahn Partners) has already left New York. Dan Sundheim (D1 Capital) is planning to depart, while Larry Fink (BlackRock) is worried tax increases will cause workers to leave. Wall Street's most prominent funds - including Goldman Sachs Group, Inc., Apollo Global Management Inc., and Point72 Asset Management - are taking steps to expand elsewhere. Asset manager Alliance Bernstein had the foresight to depart New York for Nashville in 2018. Additionally, former President Donald Trump changed his residency from New York to Florida at the end of 2019, and Elon Musk fled California for Texas in December 2020.

Tennessee has now joined the lineup of no-tax states. Over the last 20 years, Tennessee has enjoyed an impressive rate of population growth due to below-average living costs and a high quality of life. This success is only expected to accelerate now that the Hall tax on dividend and interest income is gone, eliminating all personal income taxes. Considering the growing commercial link between New York and the cities of Middle Tennessee, it stands to reason that an increasing number of high-net-worth New Yorkers will be setting their sights on the Volunteer State.

In New York, a taxpayer who is a resident 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 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 that are attributable to a business, trade or profession carried on in the state. Thus, significant benefits may be derived from filing as a nonresident.

However, the New York State Department of Taxation and Finance conducts more residency audits than any other state. These audits are highly intrusive and can take an extended period of time to complete. The burden of proof in a residency audit is on the taxpayer to prove by clear and convincing evidence that they changed their residence. There are three separate and distinct areas to be examined during the audit of a nonresident individual: domicile, statutory residency and income allocation. This article will provide an overview of each area. While references will be made to the New York State and New York City law, the rules in many other states are similar.

## DOMICILE

In general, a domicile is:

- the place one intends to have as their true, fixed, permanent home;
- where one's permanent home is located; or
- the place to which one intends to return whenever absent.

An individual can have many residences but only one domicile. Once established, a domicile continues until the taxpayer abandons the old and moves to a new location with the bona fide intention of making the new location their fixed and permanent home. Intention is a decisive factor in the determination of domicile. Since the actual process of ascertaining an individual's intentions regarding domicile is a subjective inquiry, an experienced residency negotiator is usually needed to persuade the auditor on this crucial question.

As mentioned before, the burden of proving a change of domicile is upon the party asserting the change. At times, a life event makes the domicile inquiry easier if it supports a typical pattern. Retirement, loss of job, the death of a spouse, a divorce and remarriage, or even the growing up of one's children often triggers a desire to change a lifestyle and domicile, which can strengthen a taxpayer's position. It is immaterial that a person is motivated by self-interest or even a desire to get a tax advantage.

### *Primary and Other Factors*

Since one's domicile can be subjective, the auditors in New York and elsewhere look at five primary factors in order to make an objective determination:

1. Home: The individual's use and maintenance of a New York residence compared to the nature and use patterns of a non-New York residence. Also considered is the extent to which the taxpayer is involved with local community activities.
2. Active business involvement: The active participation in a local business would insinuate that the domicile is the home that is nearby. Business involvement also includes active participation in a New York State trade, business, occupation or profession and/or substantial investment in, and management of, any New York closely held business.
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. The presence of a daily suburban commuter at work in New York is not necessarily negative evidence, as long as the morning and evening commute is to and from another state.
4. Near and dear: The location of pets, valuable personal items or other sentimental possessions—such as fine art and collectibles—that the taxpayer holds dear is a significant fact. The location of medical records and financial records is also a good indicator as to the location of one's domicile.
5. Family connection: An analysis of family connections should generally be limited to the taxpayer's immediate family. The location where minors attend school is the most important inquiry for this factor because one may infer that the taxpayer is domiciled near the school.

Each of the five primary factors are to be evaluated to determine whether it points to New York or points to the newly claimed place of domicile. Where the primary factors are inconclusive, auditors are instructed to consider secondary or other factors. Other factors include voting and auto registrations, drivers' licenses, addresses used in legal documents, tax returns and the location of safe deposit boxes. Taking care of these activities will not necessarily improve the chances with the auditor, but the failure to do them will be used against the taxpayer.

The tax law also provides tax relief for certain individuals who are New York State domiciliaries. A domiciliary who meets the criteria of one of two rules would not be deemed a resident. The rules are known as the 30-day rule, New York Tax Law § 605 (b)(1)(A)(i) and the Foreign Country Rule, New York Tax Law § 605 (b)(1)(A)(ii).

## Statutory Residency

If the taxpayer is successful and the auditor agrees on the issue of domicile, they still must show that they are not a statutory resident. An individual is a

statutory resident if they maintain a "permanent place of abode" in the state for substantially all of the taxable year and spend in the aggregate more than 183 whole or part days a year in the state. If found to be a statutory resident, their compensation income and investment income would be fully taxable for the entire year.

***Permanent Place of Abode***

A permanent place of abode is a dwelling place permanently maintained by the taxpayer (whether or not owned by them) and will generally include a dwelling place owned or leased by a spouse. The dwelling place must be maintained for substantially all of the taxable year in order to be considered a permanent place of abode for statutory residency purposes. Maintaining a permanent place of abode means doing whatever is necessary to continue one's living arrangement in a particular dwelling place. This includes making contributions to the household in money or otherwise. Also, it does not matter whether the taxpayer actually uses the dwelling as long as it is available, and they have unfettered access. An attorney can assist in classifying whether certain living quarters constitute a permanent place of abode as well as clarifying issues relating to habitability and corporate apartments.

***183-Day Test***

A taxpayer who maintains a permanent place of abode bears the burden of proving that they spent less than 184 days in New York State or City for each year of the audit period. The taxpayer is required to keep and have available for examination clear and convincing evidence to substantiate this requirement. Spending any part of a day within the taxing state counts toward the 183-day rule. Even crossing into New York for only 10 minutes to purchase gas would count as a "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 the purpose of boarding a "plane, ship, train or bus for a destination outside of New York State." As a caveat, activities and transactions en route to the transportation terminal should be incidental and limited to avoid an auditor's attempt to disallow the exception on the grounds that nonrelated commercial activities were engaged in. (Note: Staying overnight always counts as two days. Flying into New York at 11 p.m. to conduct business the next day and then flying out of New York at 4 p.m. still counts as two days.)
- Medical days: Confinement to a medical institution in New York generally does not constitute a day spent in New York. While an involuntary illness would clearly qualify for this exception and days spent as an outpatient or visiting doctors would not, it would be wise to consult a residency attorney to clarify the policy in this area. This is a limited exception that does not apply to the spouse of an inpatient.

**Income Allocation**

A finding that a taxpayer is a nonresident of New York does not necessarily end the inquiry in a residency audit. This is because all taxpayers can still be taxed on income that is derived from New York sources. New York source income of a nonresident is usually attributed to one of the following:

1. The ownership of any interest in real or tangible property located in New York
2. A business, trade, profession or occupation carried on in New York

In determining the number of days worked outside New York for allocation purposes, New York applies a convenience versus necessity test. Days worked at home (outside of New York State) for the employee's own convenience should be treated as New York workdays. If the taxpayer's home office qualifies as a "bona fide employer office," different rules would apply, and the day could be treated as a non-New York day.

**Key Takeaways**

As stated earlier, domicile is defined as the place an individual intends to be their permanent home, the place they intend to return to whenever they may be absent. Intention is a decisive factor in the determination of whether any particular residence that a person may occupy is their domicile.

The actual process of ascertaining an individual's intentions—the critical question in a residency audit—is a subjective inquiry for the auditor and often a difficult one. Since the audit would be conducted in New York, it is critical to engage a local attorney well versed in the residency policies of the departing state. The local residency attorney can help outline the steps to follow when contemplating a change in tax residency.

Finally, the good news is that an individual can become a Tennessee resident and completely avoid income tax and estate tax in New York State while still maintaining a home and a level of contacts in New York once they understand the residency rules and how these rules operate.

Engage a local tax attorney that specializes in litigating residency cases, because they will be able to advise on what truly works and what steps do not.

## About the Author

**Alvan Bobrow, Esq.** is a tax partner at Barton LLP with offices in Nashville and New York. His practice focuses on state and local taxes, including residency consulting and litigation for clients. He can be reached at *abobrow@bartonesq.com*.