Protecting Your Snowbird Clients from a New York Residency Audit

By Karen Tenenbaum and Lance E. Rothenberg

As winter sets in, we envy those who can easily travel to warmer climates. However, snowbirds may pay a steep cost if they aren't careful. A New York personal income tax residency audit may be the most difficult and personally intrusive type of audit to endure. The purpose of the audit is to establish whether a taxpayer accurately filed a New York personal income tax return as a nonresident, part-year resident, or resident. However, these audits are very fact-intensive, requiring a detailed review of voluminous records to determine the taxpayer's intentions, whereabouts, and movements.

More than most states, New York aggressively enforces its residency audit program. New York residents are required to pay tax on all worldwide income, while nonresidents are subject to tax only on income allocable to New York, such as wages earned for services provided within the state, rents from property located within the state, or income attributable to a New York trade or business. Accordingly, a determination that a taxpayer is a New York resident has significant tax consequences. To protect against an audit, it is essential to understand New York's two tests for determining residency for income tax purposes:

1. Domicile

A taxpayer may have more than one house, but he can have only one "domicile." Under New York's rules, an individual's domicile is his true, fixed, permanent home. It's the place he returns to after having been absent.[1] Legal domicile requires both a subjective intention and physical presence within the jurisdiction.

Once established, a domicile continues until the taxpayer can demonstrate that he has abandoned one domicile and established a new one outside of the state. 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.

New York looks to five primary factors in evaluating a claim of a change of domicile.[2]

a) Home Factor: comparison of size, value, and usage in each jurisdiction;

b) Business Factor: comparison of business ties in each jurisdiction;

c) Time Factor: comparison of days spent in each jurisdiction;

d) Near & Dear Items Factor: comparison of where a taxpayer keeps his financially and sentimentally important items that make a home a home; and

e) Family Factor: comparison of family members in each jurisdiction.

A good example of these factors at work is the 2017 Tax Court decision in *In re Blatt*.[3] The case involved a taxpayer who moved from New York to Texas for a new job. He initially maintained a residence in each state, but over time committed to living in Texas. He subsequently returned to New York for a new position. While he was living in Texas, he stopped paying tax to New York as a resident. Among the various domicile factors weighed by the court were the taxpayer's "near and dear" items. The court was particularly persuaded by evidence introduced at trial that Mr. Blatt moved his beloved dog from New York to Texas. While he maintained a home in each jurisdiction, the fact that he brought his dog to Texas was compelling evidence of his intention to commit to Texas as his domicile.

Additional factors may be relevant. However, only after first examining the five primary factors listed above will residency auditors look to secondary factors, such as a taxpayer's driver license, voter registration, auto registration, etc. These data points can be very useful and important in telling a complete story, but they can be more easily manipulated than the primary factors.

It should be noted that there are two exceptions when a taxpayer will not be taxed as a resident for personal income tax purposes, even though domiciled in New York.

> **Exception 1:**
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> Taxpayers who (1) do not have a permanent place of abode in New York and (2) spent fewer than 30 days in New York will not be considered a resident for income tax purposes.

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Exception 2:

A taxpayer who (1) is in a foreign country for at least 450 of any 548 consecutive day period and (2) neither he nor his family spends more than 90 days in New York will not be treated as a resident for income tax purposes. This exception typically applies when New York residents are positioned in overseas offices of their multinational employers.

2. Statutory Residency

Where an individual is domiciled outside of New York, he may still be taxed as a "statutory resident" of New York if he meets a two-prong test: (1) the individual must maintain a permanent place of abode in New York; and (2) he must spend, in the aggregate, more than 183 days of the year in New York.

A typical audit case might involve an individual who is domiciled in Florida, but who maintains an apartment in Manhattan and travels to New York for both work and pleasure frequently. Would this taxpayer meet both prongs of the statutory residency test?

a) **Permanent place of abode.** New York defines *a permanent place of abode*[4] as a residence (building or structure in which a person can live) that is maintained by the taxpayer for substantially all of the year and is suitable for year-round use. It doesn't matter whether the taxpayer owns the place or stays there during visits to New York. Even if others are using the place (relatives, renters, etc.), it could still be considered the taxpayer's abode under certain circumstances.

   The auditor would consider factors such as whether the taxpayer uses the apartment or leases it out to a third-party? Is the third-party a stranger or is it rented to a relative? Does the taxpayer have a key and unfettered access to the place? Is it habitable and being maintained for more than 11 months of the year?

   In the recent case of *In re Mays,*[5] New York's Tax Appeals Tribunal examined what it means to maintain an abode in New York for purposes of statutory residency. The taxpayer was domiciled outside of New York City, and argued that a temporary, corporate apartment available to her in Manhattan did not qualify as her abode for the statutory residency test. Examining prior case law, the Tribunal set forth the proper analytical decision-tree: Does the dwelling exhibit the 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?

b) **Day count.** Let's say the taxpayer commutes from New Jersey to Manhattan for work. If he spends greater than 183 days in New York, this element of the test is met. When it comes to counting days spent in New York, generally the rule is that a partial day counts as a full day, with some limited exceptions. Overnights are not required so even catching a Broadway musical on a Sunday will count as a day.

   The difficulty with day count is establishing evidence to document the taxpayer's daily whereabouts. New York may ask to analyze documentation including diaries, appointment logs or calendars, credit card and bank statements, detailed cell phone bills, EZ Pass records, ATM receipts, passport records, and data from building security or swipe cards. Furthermore, smart phone applications have been developed (two such examples include TaxDay and Monaeo) to track and record an individual's location using GPS signals. This is why proper recordkeeping is essential and can help avoid or fight a tax audit.

Successfully defending against a residency audit may also include an examination of whether a nonresident has properly computed and reported tax to New York on income from New York sources. Nonresident allocation audits can involve complex issues over the proper sourcing of deferred compensation, employee stock options, and pass-through business income, among other issues.

New York State residency audits can be burdensome, complex and invasive. If your client has or is considering moving or purchasing a second home, careful planning is critical. In the event they receive a residency questionnaire or audit notice, they should speak to a qualified tax advisor for help in responding to the state.

Endnotes

1. *See* 20 N.Y.C.R.R. 105.20(d); *see also In re Newcomb*, 192 N.Y. 238 (N.Y. 1908).
2. *See, e.g.,* NY Nonresident Audit Guidelines (2014).
3. *In re Blatt*, DTA No. 826504 (Div. Tax App. 2017).
4. *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).
5. *In re Mays*, DTA No. 826546 (Tax App. Trib. 2017).