

Tax Audits

New Case Clarifies Approach to New York Residency Audits

BNA Snapshot

- This helped convince court: Taxpayer moved his dog to Texas
- In aggressive residency-audit state, the going can get tough



By John Herzfeld

A decision by the New York Division of Tax Appeals illustrates the importance of “telling a compelling story” to prevail in establishing the domicile for a residency tax audit in the most aggressive U.S. state for such audits, a leading practitioner said.

The taxpayer in the Feb. 2 case won his administrative challenge to an adverse state finding in a residency audit for 2009 and 2010 by fully demonstrating the change in lifestyle that came with his domicile move to Dallas, even though he had retained his New York City apartment and other ties to New York, Timothy P. Noonan of Hodgson Russ LLP in Buffalo, said during a Feb. 3 Bloomberg BNA webinar.

The testimony of the taxpayer, Gregory Blatt, paired with recordkeeping and other supporting evidence, convinced the court that he had changed his domicile to Texas, Noonan said. His testimony as to his state of mind, backed up by e-mail correspondence, showed that he was relocating (*In re Blatt*, N.Y. Tax App. Trib., No. 826504, 2/2/17).

The gist of his case was, “This was my intent, and this is how I accomplished it,” said Noonan, whose firm represented the taxpayer. In particular, Blatt had brought his dog with him to Texas, which helped satisfy the test of where he kept things near and dear to him. He also had told all his friends of his plans to move, he said.

‘Compelling Story’ Made Difference

Even in the Blatt case, where the state could count several New York factors that might add up against the taxpayer on paper, Noonan said that “it was the compelling story that carried the day.”

Many former residents continue to have strong ties to New York, “so the problem is how to demonstrate that someone who still happens to own an apartment in New York City has nevertheless moved on,” Leah Robinson of Eversheds Sutherland (US) LLP in New York told Bloomberg BNA in a Feb. 6 e-mail. “I often ask for holiday and birthday photographs, particularly for kids’ birthday parties and the December holidays. That’s one way to show where home is.”

The resolution of one case Robinson handled, she said, ultimately turned on where the taxpayer “got his hair cut every other Saturday morning” and where he and his wife had their anniversary dinners.

Most Aggressive in U.S

The Blatt determination, which the state may still appeal, was a fresh reminder of the lengths to which a taxpayer may have to go to support a position in the New York Taxation and Finance Department residency audit program, the most advanced and aggressive in the U.S., Noonan said.

As state and city tax rates in New York continue to rise, he said, “you can expect to see more taxpayers attempting to change their residency status and, consequently, more audit activity in this area.”

New York, with the state handling audits for both state and city taxes, conducts some 5,000 income tax audits a year and has about 300 field auditors dedicated to residency audits, he said, adding: "They're hiring people, and there's a lot of action."

Madonna, Derek Jeter

The audits can be particularly sensitive when they involve detailed facts about where and how certain high-income, high-profile taxpayers live, he said, noting that celebrities audited in New York have included Derek Jeter, Madonna and Martha Stewart.

"If you take it to the appeals unit, the decision gets published," he said. "That's something you have to take into account."

Robinson warned that "people have to balance the expense of the potential tax at issue against the complete intrusion into their privacy that the audit defense will involve."

The terrain gets rough when the audit enters into the "very subjective, very fuzzy" questions of what constitutes a domicile, Noonan said during the webinar.

Evidence such as driver's licenses and voting registrations matter, but those "self-serving ministerial acts" won't carry the day, he said. The audit will probe into the taxpayer's lifestyle, he warned.

Close Case Not Good Enough

The taxpayer, moreover, has the burden of proof to demonstrate nonresident status by the standard of clear and convincing evidence, Noonan said. "So a close case won't pass."

Noonan represented the taxpayer in one of the few New York residency cases to reach New York's highest court, Matter of Gaied v. N.Y. State Tax Appeals Tribunal, which resulted in a February 2014 decision for the taxpayer.

In that case, which centered on the secondary test of "statutory" residency, the taxpayer lived in New Jersey but commuted to work across the New York border in nearby Staten Island, where he owned a multifamily apartment building in which his parents and other tenants lived.

To show statutory residency, the state must find that a taxpayer spent 183 days a year or more at the New York property as a permanent place of abode.

Broader Picture Needed

The court agreed that the taxpayer had provided enough evidence to show that—although he sometimes stayed overnight with his parents on a couch and paid the bills there in his own name—he lived in New Jersey and hadn't used the New York property as a residence, or permanent place of abode.

The taxpayer's case looked beyond the objective evidence of his ownership and number of days he was physically present in New York to evaluate the broader evidence of where he actually lived, Noonan said. Legislative history going back 100 years showed that the law was aimed "at people who really lived in New York," and Gaied "really lived in New Jersey."

Noonan added that, "unfortunately, the tax department has taken a pretty narrow view" of the implications of the Gaied decision. The state maintains that a New York property can still be a permanent place of abode if no one lives there and it's available for use by the taxpayer, and that "someone else has to live there" for it to be ruled out as a permanent place of abode, he said.

"We think that's wrong," he said, alluding to a continuing "tug of war" over the issue.

Precedential Value?

Adding to the challenges of residency audits, Noonan said, is the fact that the state isn't bound in future audits by the determinations of administrative law judges, which have no precedential value.

Thus, for example, the state continues to take its long-held position that it can count days toward the 183-day statutory residence threshold even from the part of the year after a taxpayer has moved to New York and established domicile there, he said.

That's contrary to an administrative law judge's decision in a 2015 case that found support for the taxpayers' argument that the state can't count days in a year toward statutory residency that fall within the domicile-based resident portion of the same year, said Noonan, who represented the Sobotkas (*In re David and Karen Sobotka*, N.Y. Tax App. Trib., No. 826286, 8/20/15).

The state didn't appeal that decision but still holds to its position in audits, he said, presenting the case as an example of how tricky residency determinations can get in audits.

Richard Pomp, a law professor at the University of Connecticut who is a past director of a New York legislative tax study panel, said in a Feb. 6 e-mail message that although the focus of audits is often on taxpayers who leave New York for states with no income tax, he's had clients who had moved to New York City to enjoy its offerings for a year or so after selling a business in a high-tax state, "with every intention" of then moving back home.

They faced the risk of being claimed as a resident by both states simultaneously, with neither state crediting the other's tax, Pomp said. New York "unconstitutionally" doesn't provide credit for income taxes paid to other states by residents of the city, he said.

In general, he told Bloomberg BNA, "New York auditors have trouble believing that anyone would want to move out of the Big Apple."

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For More Information

The Blatt determination is at <http://src.bna.com/l0c>.

The Sobotka order is at <http://src.bna.com/l0b>.

The Gaied decision is at <http://src.bna.com/l0a>.