Tax Department Reads Taxpayer Residency Victory Narrowly

By Mark Berg

Given New York's position as a financial and business center, many people who live outside New York regularly commute here for work. As a matter of convenience, certain of these people own or rent, say, a pied à terre in New York City or a beach house in the Hamptons, which although available to them all year and suitable for year-round use, are in many cases not actually used by them much if at all. Because New York's tax rules treat a nondomiciliary of New York who is in New York more than 183 days a year as a New York resident if he maintains a permanent place of abode (PPA) in New York, and because New York resident individuals are generally subject to New York income tax on their worldwide income, the critical question for someone in this situation is whether the place will be considered his PPA regardless of the amount of time actually spent there.

Earlier this year, the Court of Appeals, in Gaied v. Tax Appeals Tribunal,[1] provided these individuals with hope for a favorable result, holding that in order for a dwelling to be considered a PPA maintained by the taxpayer, the dwelling must be "utilized as the taxpayer's residence" and "the taxpayer must, himself, have a residential interest in the property." The New York State Department of Taxation and Finance recently revised its audit guidelines in light of Gaied,[2] but continues to instruct auditors to treat an individual who has access to an abode in New York as maintaining a PPA there irrespective of how much he actually uses the place. This article describes the PPA requirement and the Gaied case, analyzes the manner in which the guidelines interpret Gaied and concludes that the department's interpretation of Gaied may be subject to challenge.

An individual not domiciled in New York3 is considered a "statutory resident" for New York income tax purposes for a year, and therefore is generally subject to New York income tax on his worldwide income for that year,[4] if he spends more than 183 days in New York during that year and maintains a PPA in New York for substantially all of that year.[5] The regulations define a PPA as "a dwelling place of a permanent nature," whether or not owned by the taxpayer, other than a mere camp or cottage suitable and used only for vacations or a place that does not contain facilities ordinarily found in a dwelling such as cooking and bathing facilities, and require that the taxpayer maintain the abode "for substantially all of the taxable year (generally, the entire taxable year disregarding small portions of such year)."[6]

The New York State Tax Appeals Tribunal and the courts have held that whether an abode maintained by a taxpayer is a PPA is determined by reference to the physical aspects of the abode (suitability for year-round use and cooking and bathing facilities), the taxpayer's relationship to the abode (as owner, lessee or one who makes contributions to the household) and the taxpayer's use of the abode (such as whether the taxpayer has free and continuous access to the abode, has a dedicated room there, keeps clothing and other personal effects there

and uses the abode for convenient daily access to and from a place of employment).[7]

Prior to the Court of Appeals' decision in Gaied, the tax department, with the tribunal's and lower courts' approval, took the view that one need not spend much if any time at an abode in order to be considered to maintain it as a PPA.[8] Perhaps the most extreme example of this approach is Matter of Barker,[9] in which an individual who lived in Connecticut, worked in New York City and owned a beach house in the Hamptons where he and his family spent fewer than 20 days in each of the years in issue, was held to maintain a PPA at the beach house, even though his in-laws spent several days a week during the summers and many weekends during the rest of the year there.

In Gaied, the taxpayer, a New Jersey domiciliary who worked full-time at his business in Staten Island, owned an apartment in Staten Island that was his elderly parents' principal residence. The taxpayer had unfettered access to the apartment and paid all expenses, but had no bedroom, bed, clothing or personal belongings there. He came to the apartment at least once every month or two at his parents' request to provide them with physical support, only occasionally sleeping there (on the couch).

The department determined that the taxpayer maintained a PPA at the apartment and therefore was a New York state and city resident, which determination the taxpayer unsuccessfully challenged in the Division of Tax Appeals. The tribunal initially reversed, but then granted the tax department's motion for reargument and held for the tax department in a 2-1 decision, largely on the basis of its intervening Barker decision. A divided Appellate Division confirmed the department's victory, holding that while a contrary conclusion by the tribunal would have been reasonable, the tribunal's decision was amply supported by the record.

In a unanimous opinion, the Court of Appeals reversed, concluding that there was "no rational basis" for the tribunal's determination that a taxpayer need not reside in a dwelling, but only maintain it, for the dwelling to be considered a PPA maintained by the taxpayer. The court (1) agreed with the taxpayer that "the question should turn on whether he maintained living arrangements for himself to reside at the dwelling"; (2) held that "in order for an individual to qualify as a statutory resident, there must be some basis to conclude that the dwelling was utilized as the taxpayer's residence"; (3) held further that the legislative history of the statutory residence provisions and the regulations "support the view that in order for a taxpayer to have maintained a permanent place of abode in New York, the taxpayer must, himself, have a residential interest in the property"; and (4) reversed and remitted the case to the Appellate Division with instructions to remand to the tribunal "for further proceedings in accordance with this opinion."[10]

Given the facts in Gaied, the court could have issued a narrow ruling that a dwelling cannot be a taxpayer's PPA if it is someone else's principal residence. Instead, it seems clear from the language quoted

above that the court went out of its way to hold more broadly that in order for a dwelling to be considered a taxpayer's PPA, the taxpayer himself must reside there, i.e., that owning, paying all expenses for and having unfettered access to the dwelling is not sufficient, irrespective of whether someone other than the taxpayer lives there. This conclusion is supported not only by the language used by the court but also by the legislative history cited by the court and the court's remittance order: The legislative history emphasized by the court indicates that the intended targets of the statutory residence provisions included "multimillionaires who actually maintain homes in New York and spend ten months of every year in those homes,"[11] which suggests that the statute requires that the taxpayer spend at least some time at the dwelling in order for it to be considered a PPA.

Moreover, had the court intended to limit its holding to dwellings occupied by someone other than the taxpayer, it could simply have reversed the Appellate Division without remitting the case with directions to remand it to the tribunal for further proceedings, since all of the facts necessary to determine that someone other than the taxpayer lived at the apartment were clearly in the record.[12] By remitting and remanding for further proceedings, the court appears to have been directing the tribunal to conduct a broad-based inquiry into whether the dwelling was "utilized as the taxpayer's residence," an inquiry that might include a qualitative comparison of the accommodations available to the taxpayer at the apartment and at his other residence and the number of nights the taxpayer spent at the apartment vis-à-vis his other residence.

In June 2014, the department revised the guidelines largely if not entirely in light of Gaied. In the revised guidelines, the department acknowledges that the Court of Appeals rejected as irrational the department's prior position that a taxpayer can maintain a PPA without actually dwelling there, and quotes the court's holding that in order for a dwelling to be considered a PPA maintained by the taxpayer, the taxpayer must have a residential interest in the dwelling and utilize it as his residence.[13]

In an example intended to clarify when a taxpayer is to be considered as having the residential interest required under Gaied, however, the department, citing an Advisory Opinion issued by the department some 20 years before Gaied,[14] asserts that "[a] residence that is owned and maintained by a taxpayer with unfettered access will generally be deemed to be a [PPA] regardless of how often the taxpayer actually uses it."[15] In the example, a couple domiciled in New Jersey rents an apartment in New York City that they use when they attend cultural events in the evening rather than driving home. Friends and relatives use the apartment occasionally but no one else lives there on a regular basis. The department concludes that the apartment constitutes the couple's PPA on the basis of their unfettered access. Similarly, among the factors auditors are instructed to use in applying Gaied's residential interest requirement is "whether the taxpayer uses the dwelling or has unfettered access."[16]

Where does this leave a non-domiciliary who owns or rents, but never or only sporadically uses, a dwelling in New York such as a New York City pied à terre or Hamptons beach house? As discussed above, the court in Gaied held that even where the taxpayer has unfettered access to the dwelling, he does not maintain a PPA there unless the dwelling is "utilized as the taxpayer's residence." Nonetheless, the tax department instructs its auditors in the guidelines that a dwelling to which the taxpayer has unfettered access is the taxpayer's PPA "regardless of how often the taxpayer actually uses it." It is submitted that at least in the scenario discussed herein, the department's position is inconsistent with what appears, for the reasons discussed above, to be the best reading of Gaied, and that the department's position in the guidelines appears to be the very position for which the court held there to be no rational basis.[17]

If the tax department's auditors implement this narrow reading of Gaied, taxpayers will inevitably challenge the department's position. It remains to be seen whether the tribunal and the courts will agree with the department's position or instead adopt the broader interpretation of Gaied suggested herein and require that a taxpayer actually use the dwelling as his residence in order to treat it as a PPA maintained by the taxpayer. If the tribunal and/or the courts take the latter approach, the next question would be where to draw the line between a taxpayer who spends so much time at the New York dwelling that he can fairly be said to be using it as his residence and one who really resides elsewhere and makes only limited or sporadic use of the New York dwelling. Meanwhile, certain taxpayers in this situation who previously filed tax returns as statutory residents might wish to consider filing claims for refund for open years (generally, years for which the original return was filed no more than three years earlier).

Endnotes:

[1] 22 N.Y.3d 592 (2014), rev'g and remitting 101 A.D.3d 1492 (3d Dept. 2012), confirming Matter of Gaied, DTA No. 821727 (Tax App. Trib. 2011), withdrawing DTA No. 821727 (Tax App. Trib. 2010), rev'g DTA No. 821727 (Div. Tax App. 2009). For a more detailed discussion of Gaied, see Berg, "New York's High Court Eases Residency Trap," 72 State Tax Notes 335 (May 12, 2014).

[2] New York State Department of Taxation and Finance, Income Franchise Field Audit Bureau, Nonresident Audit Guidelines (June 2014) (the guidelines).

[3] With limited exceptions, a New York domiciliary is considered a New York resident. Tax Law §605(b)(1)(A); NYC Admin. Code §11-1705(b)(1)(A). New York state and city impose separate personal income taxes, both administered by the tax department, and have identical tax residency rules.

[4] Tax Law §601(a)-(d); NYC Admin. Code §11-1701. Certain income that is not included in gross income for federal income tax purposes, such as the non-U.S. source, non-effectively connected income of a nonresident alien

as to the U.S., is not subject to New York tax, even in the hands of a New York resident. See Tax Law §612(a); TSB-A-10(7)I.

[5] Tax Law §605(b)(1)(B); NYC Admin. Code §11-1705(b)(1)(B); 20 N.Y.C.R.R. §105.20(a)(2).

[6] 20 N.Y.C.R.R. §105.20(a)(2), (e)(1). Under the tax department's audit policy, "substantially all" generally means more than 11 months. Guidelines at 63-64.

[7] See, e.g., Matter of Evans, DTA No. 806515 (Tax App. Trib. 1992), confirmed, 199 A.D.2d 840 (3d Dept. 1993).

[8] See, e.g., Matter of Roth, DTA No. 802212 (Tax App. Trib. 1989); Smith v. State Tax Commission, 68 A.D.2d 993 (3d Dept. 1979).

[9] DTA No. 822324 (Tax App. Trib. 2011). In response to Barker, the New York State Senate on two occasions passed a bill providing that a PPA does not include a dwelling that is not used as the taxpayer's principal residence, that is located more than 50 miles from the taxpayer's place of employment and at which the taxpayer stays overnight on no more than 90 days during the taxable year. See S.3642-A; S.3998-C. Neither bill was passed by the General Assembly.

[10] 22 N.Y.3d at 594, 598 (emphasis in original).

[11] Id. at 597 (quoting Income tax bureau mem., bill jacket, L.1922, ch. 425) (emphasis added).

[12] See CPLR §5613 (requiring Court of Appeals to remit when questions of fact were not considered by Appellate Division).

[13] Guidelines at 54.

[14] Freundlich & Company, TSB-A-94(14)I.

[15] Id. at 54, Ex. 1.

[16] Guidelines at 56, 58 (emphasis added); see also id. at 54-55, Ex. 2.

[17] Indeed, it is not even clear from the guidelines how the tax department would come out on the facts of Gaied itself. See id. at 55, Ex. 4.