New York Tax Department's Response to *Gaied* Misses the Mark

by Timothy P. Noonan


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Noonan analyzes the New York State Department of Taxation and Finance's recently revised nonresident audit guidelines, which largely were written to address the New York Court of Appeals decision in *Gaied*. He says the department's new rules don't follow the court's decision, and he hopes the department will consider revisiting the issue.

The New York State Department of Taxation and Finance recently issued a revised version of its nonresident audit guidelines, which are used by auditors and practitioners during the many residency audits that take place across the state — ordinarily not something to get all that excited about. But considering that the revised guidelines are the tax department's first truly public reaction to the landmark decision on residency by New York's highest court in *Gaied v. New York Tax Appeals Tribunal*, 22 N.Y.3d 592 (N.Y. 2014), it's a big deal to New York practitioners, many of whom deal address residency questions daily.

I know what you're thinking: "Tim, I know this was your case, but didn't you already write an article about *Gaied*?" Indeed I did, but I'm compelled to jump in again because, quite surprisingly — and despite all the fanfare and publicity regarding the game-changing nature of the decision — the department's view is essentially "business as usual."[1] In attempting to reconcile *Gaied* and assimilate the decision into department audit policy, the revised guidelines instead seem to treat the case as consistent with policy already being applied by the department.

I, of course, beg to differ. In this article, I will explain why the revised guidelines fail to reflect the critical holding by New York's highest court: that a person can't be deemed a resident of New York simply by having "relationship" to a dwelling there; the person must actually use that dwelling as a residence.

I. Setting Up the Dispute

Gaied dealt with New York's statutory residency test, under which a taxpayer becomes subject to tax as a resident of New York if he maintains a permanent place of abode in the state and spends more than 183 days in the state. The dispute in *Gaied* centered on the meaning of the term "permanent place of abode."

My firm and I argued that if you looked to the legislative intent of the statute, the 1922 law was designed to tax people who really were residents — that is, taxpayers who really lived in New York. Thus, we argued that for a dwelling to constitute a permanent place of abode, the taxpayer really has to use the place as its residence. We pointed out that the department made clear in its 1922 memorandum in support of the new law why such a measure was necessary: It was an alternative to the highly subjective common-law test of domicile, which had governed residency determinations up until then.[2]

As the department then noted, "We have several cases of multimillionaires who actually maintain homes in New York and spend ten months of every year in those homes . . . [but they] claim to be nonresidents: their offices are in New York; but they vote from their summer residences in New England or their winter residences in California or Florida and claim to be nonresidents."[3] The addition of the abode-plus-seven-months test, according to the department's memorandum, "would do away with a lot of this

[1]Noonan, "The Goods on *Gaied*: What It Means, From the Front Lines," *State Tax Notes*, May 19, 2014, p. 409; *see also* Josh Barbanel, "Lower Taxes Seen for Nonresidents Who Own Real Property in New York," *The Wall Street Journal*, Feb. 20, 2014; Richard J. Koreto "Landmark *Gaied* Residency Ruling Overturned by Courts," *The Trusted Professional* (Mar. 2014), at 4; Matthew Vilmer, "NY Residency Ruling Shortens Leash for Auditors," Law360, Feb. 20, 2014; Edward Zelinsky, "The *Gaied* Decision: A Rare Victory for Sanity in New York," Oxford University Press OUPblog, Mar. 3, 2014.

[2]The tax law had previously defined the term "resident" as "any person who shall, at any time during the last six months of the calendar year, be a resident of the state," but it did not define what constituted being a resident during that period (L. 1918 ch. 691, sec. 7).

[3]Mem. of Income Tax Bureau, Bill Jacket, L. 1922, ch. 425.

faking and probably result in a man's conceiving his domicile to be at the place where he really resides."[4] That is why we argued that the taxpayer actually had to reside at a place in New York to be taxed as a resident.

The department, on the other hand, argued that a person need not dwell in an abode for it to constitute a permanent place of abode, and that other relationship factors needed to be taken into account to determine whether an abode qualified as a permanent place of abode under the statute. Those factors included ownership, maintenance, access/use, relationship to cohabitants, and registration for government services. Notably, the department argued that a taxpayer could maintain a permanent place of abode in New York even if he did not use the abode, so long as some other relationship factors were present.

At oral argument, Chief Judge Jonathan Lippman summarized those competing views while questioning me as counsel for John Gaied:

JUDGE LIPPMAN: Your interpretation of the statutory language is that it means you really live here.

NOONAN: Yeah, yes.[5]

JUDGE LIPPMAN: That's basically what you say the test — you interpret the statute to be. . . . If you really live here, you get taxed. While your adversary, I think, is arguing, if you maintain a place that you could conceivably use, you have to pay the tax.

NOONAN: Yes Judge . . . that's the exact dichotomy.[6]

A. The Court's Ruling

No spoiler alert here. By now, readers know what the court said. Relying on the legislative intent underlying the statute, it found no rational basis for the department's position. And again, the judges made clear during argument that they disliked the department's statutory interpretation. As Lippman asked department counsel:

> But there's got to be some rhyme and reason to it. And what I'm saying to you — what makes sense is, if you don't really reside there, that's the ultimate test, and no one . . . who doesn't actually reside. . . . I can make sense of the statute if that's the test.[7]

Judge Eugene Pigott, who wrote the court's unanimous decision, said the department's position just doesn't make sense. The statute "reads like if you intend to live in New York, we want to tax you," he said.[8]

But in making its decision, the court didn't examine the particular facts in the case and try to apply them to a settled legal rule. Instead, it plainly and simply set forth the new rule: To be subject to tax as a New York resident, there must be some basis to conclude that the dwelling was used as a taxpayer's residence.

B. June 2014 Audit Guidelines

I've said it before and I'll say it again: The department deserves credit for stepping up and making public its position on complex residency issues. Its audit guidelines are very helpful to practitioners, and its June 2014 revision, which dealt almost exclusively with *Gaied*, provides a useful roadmap.

But that doesn't mean we have to agree with the guidelines.

The department's views are set out in pages 53-58 of the guidelines. In a nutshell, the department makes three points:

- First, the department says the court's finding in *Gaied* — that there must be some basis to conclude that the dwelling was used as a taxpayer's residence — is consistent with current audit policy requiring that the taxpayer must have a "relationship to the dwelling" for it to constitute a permanent place of abode.
- In a series of examples, the department explains its interpretation of *Gaied*. In Example 1, looking to taxpayers who occasionally used an apartment in New York City for social engagements, it states generally that "a residence that is owned and maintained by a taxpayer with unfettered access will generally be deemed to be a permanent place of abode regardless of how often the taxpayer actually uses it." In Example 2, a taxpayer moves to Florida, lists her apartment for sale, and no longer resides there. The department still concludes that the place can constitute a permanent place of abode if the taxpayer continues to have unfettered access to it and no one else is using it.
- Finally, the department says the same relationship factors included in its 2012 audit guidelines still control and satisfy "the Court of Appeals' requirement in *Gaied* that the taxpayer have a 'residential interest' in the dwelling in order to be maintaining a permanent place of abode."

II. Counterpoint: 'It Just Doesn't Make Sense'

There are two fundamental problems with those points.

A. The Tests Are Not the Same

First is the idea, summarized in the first and third bullets above, that the 2012 "relationship test" is the same as or even consistent with the test set forth by the New York Court of Appeals. That is incorrect. Again, the court's ruling was premised on the legislative intent of the statute, which was designed to tax people who really are residents of the state — that is, those people who really live in New York. Judge Lippman's words at oral argument ring true: "There's got to be some rhyme and reason to it." If you don't reside in New York, you don't get taxed by New York. And the court

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[4] *Id.*

[5] Note to self: Don't say "Yeah" to the chief judge of New York's highest court.

[6] Transcript of oral argument, at 35-36, *Gaied*, 22 N.Y.3d 592. The entire transcript as well as a webcast of the oral argument is available at http://www.nycourts.gov/ctapps/arguments/2014/Jan14/Jan14_OA.htm.

[7] *Id.* at 13-14.

[8] *Id.* at 28.

clearly said in the first paragraph of its decision that the taxpayer has to use the place as a residence in order to be taxed.

The court did not say the taxpayer simply has to have a relationship with the dwelling to be taxed. The department's relationship test is not the same test articulated by the court — not by a long shot. Many taxpayers can have a relationship with a dwelling in New York and not actually live or reside in New York. But you can't live here if you don't reside here in one fashion or another.

Let's look at the various relationship factors in the 2014 guidelines, which, incidentally, are the same factors used in the pre-*Gaied* version of the guidelines. They include such things as ownership, maintenance, relationship to cohabitants, use or access, location of personal items, and registration for government services. The department concludes that by applying those factors, it will satisfy the court's requirement that the taxpayer has a residential interest in the dwelling. But most of those factors — notably, ownership, maintenance, relationship to cohabitants, and registration for government services — have nothing to do with whether the taxpayer actually resides at the dwelling.

More to the point, those relationship factors formed the basis of the assessment against Gaied, as well as the rationale behind the Tax Appeals Tribunal's final decision against him.[9] The department argued that Gaied had the requisite relationship to the dwelling because his circumstances met several of the different relationship factors in its 2012 audit guidelines.

But the New York Court of Appeals disagreed. It said the tax department was applying the wrong test and went so far as to say the department had no rational basis for its position. The court then proceeded to set forth a new test.

Now the department is basically claiming that the new test is consistent with the test it was applying all along. How can that be? If that were true, why did it lose the case? And how can the department continue to say that the test it used to sustain its assessment against Gaied remains correct? It's an incredible assertion, and one that essentially defies the clear directive laid down by New York's highest court.

So, far from being consistent with the court's position, the audit policy set forth in both the 2012 and 2014 audit guidelines is much broader than that set forth by the court. As Judge Pigott said during the oral arguments, "It doesn't make sense."[10]

B. Use as a Residence Means Actually Residing There

The other point relates specifically to the examples in the new guidelines. For instance, in Example 1, the facts are as follows:

> The Browns rent an apartment in New York City which they use in connection with attending cultural events during the evening rather than driving back to their home in New Jersey where they are domiciled. They let friends and relatives use the apartment occasionally but no one else lives there on a regular basis.[11]

The department says those taxpayers have a residential interest in the property and that it is their permanent place of abode. It reasons that a "residence that is owned and maintained by a taxpayer with unfettered access will generally be deemed to be a permanent place of abode regardless of how often the taxpayer actually uses it."[12] In other words, unfettered access to a dwelling is generally enough regardless of how often (or presumably, if) the taxpayer actually uses it.

But that is not a fair interpretation of *Gaied*. The court quoted the language from the 1922 memo in support of the new law and referenced "'several cases of multimillionaires who actually maintain homes in New York and spend ten months of every year in those homes . . . but . . . claim to be nonresidents.'"[13] With that as its backdrop, the court concluded that to be taxed as a resident of the state, there must be some basis to conclude that the taxpayer used the dwelling as a residence.

That reasoning isn't really that confusing. If someone is not using a place at all, even if he has unfettered access to it, how can we say he is using it as a residence? Even so, the department concludes in Example 1 that a place can be a permanent place of abode regardless of the taxpayer's use of it.

The department's conclusion in Example 2 is similarly inconsistent with *Gaied*. The facts are as follows:

> In connection with her change of domicile to Florida, a taxpayer listed her New York home for sale. The home remained fully furnished and the taxpayer had unfettered access although she no longer resided there.[14]

The department concludes that the taxpayer "retained a residential interest in the home and it would constitute a permanent place of abode despite the fact that it was listed for sale."[15] Thus, the department would treat the taxpayer as a resident even though she is no longer residing at the dwelling. How can a taxpayer be deemed to be using a place as a residence without actually residing there? That directly contradicts the rule set forth by the court. The dwelling must be used by the taxpayer as a residence.

III. Conclusion

When the New York Court of Appeals speaks, we are obliged to listen — especially when it speaks in a clear and

[9] *See Matter of Gaied*, DTA No. 821727 (N.Y. Tax App. Trib. 2011).
[10] *Supra* note 6, at 35-36.
[11] New York State Department of Taxation and Finance, "Nonresident Audit Guidelines" (June 2014), at 54.
[12] *Id.*
[13] *Gaied*, 22 N.Y.3d at 597, quoting *Tamagni v. Tax Appeals Tribunal*, 91 N.Y.2d 530 (1998), *cert. denied*, 525 U.S. 931 (1998).
[14] *Id.*
[15] *Id.* at 55.

unanimous voice. The test it set forth in *Gaied* is straightforward: To be taxed as a statutory resident of New York, the taxpayer must use a place in New York as a residence. That interpretation is consistent with the legislative intent and is the one that, according to the judges, simply makes the most sense.

The department's interpretation, on the other hand, really doesn't make much sense. And it's really quite bold of the department to conclude that the very test that was unanimously rejected by the court is still the right test.

Or course, this is the perfect time to remind readers that the department's nonresident audit guidelines are just that: guidelines. They do not have the force and effect of law. But quite frankly, that won't be all that helpful for taxpayers ensnared in difficult residency audits when this issue of permanent place of abode arises. Those taxpayers are experiencing something quite different — when department auditors are using the new audit guidelines as the rule of law, rather than following New York's highest court.

It might be that the department has set the stage for yet more litigation on the topic. Or perhaps cooler heads will prevail, and the department will work with practitioners to come up with an interpretation that is more consistent with the rule set forth by New York's highest court. ☆