The Nuts and Bolts of a New York Residency Audit, Revisited

by Timothy P. Noonan and Daniel P. Kelly

As regular readers of this column know, the New York State Department of Taxation and Finance has one of the most sophisticated and aggressive residency audit programs in the country. Every year, it conducts thousands of audits that lead to dozens of new cases and rulings, many of which we regularly cover in this column.

But given the prevalence of those audits, a good practitioner not only needs to know the law, he also has to know how to navigate the actual audit. In 2008 I published an article with that in mind,1 but with all the changes over the past six years, I thought it time to revisit the topic. There obviously have been new cases and rulings, and new technologies affect those cases. The tax department has issued two new versions of its nonresident audit guidelines, including a major 2012 rewrite,2 and there have been approximately 30,000 more residency audits in which many new techniques and issues have arisen.


So there’s much to consider. When your clients get a friendly letter from the tax department congratulating them on being selected for a residency audit, you need to be prepared for what’s next. This article should help you through the process.

Although the focus will be on New York’s rules and procedures, the New York tax department generally follows the outlines of the 1996 North Eastern States Tax Officials Association cooperative agreement regarding domicile, statutory residence, and allocation, in which 13 states pledged to focus on the same primary factors for considering a person’s domicile status. So to the extent you have to deal with residency audits in other states, the analysis in this article will likely be helpful as well.

I. What Is a Residency Audit?

A residency audit is designed to determine whether the taxpayer correctly filed his New York state personal income tax return as a nonresident, part-year resident, or even as a resident. Because New York residents are subject to tax on their worldwide income, while nonresidents are subject to tax only on that portion of their income attributable to (sourced to) New York, the difference in tax liability can be significant, particularly if the taxpayer has substantial investment income. Both New York state and New York City residency are on the line. The stakes are greater with New York City residency, because city residents pay tax on their worldwide income, while city nonresidents pay no tax to the city, even if they work there.

In a residency audit, the auditor will first attempt to establish whether the taxpayer is domiciled in New York. That is the first step in any audit. The New York tax department follows the rules, and generally all residency audits focus on questions of statutory residency too.

II. The Domicile Test in General

A domicile audit usually is concerned with change: Did the taxpayer move into or out of New York during the audit period? Practitioners are often looking to tie that to a change in lifestyle or a life-changing event, such as a marriage,
requirement or to his consideration. Thus, Noonan’s Notes 208
Matter 208
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1976) (quoting Matter of Bourne, 181 Misc. 238, 246, aff’d, 267 App. Div. 876, aff’d, 293 N.Y. 785 (1943)).
52014 nonresident audit guidelines, supra note 2, at 12; see also, e.g., Matter of Jeter, DTA No. 821646 (AlJ 2007).
6Matter of Knight, DTA No. 819485 (Tax Appeals Tribunal 2006).

retirement, or a new job. And despite what many taxpayers and practitioners believe, the inquiry is not really focused on where the taxpayer is registered to vote, maintains a driver’s license, or registers his cars. It is a much more subjective inquiry, based on long-standing common law principles that are often difficult to apply. The general standard is that “the test of intent with respect to a purported new domicile [depends on] whether the place of habitation is the permanent home of a person, with the range of sentiment, feeling and permanent association with it.”4

Critically, the party asserting a change of domicile has the burden of proof, by clear and convincing evidence, to show that the taxpayer abandoned his historic domicile and moved to the new location with the intent to remain there permanently. Don’t take the burden of proof concept lightly. Clear and convincing evidence is not defined, but we’re sure it means better than 51 percent for, 49 percent against. If a taxpayer has the burden of proof in a domicile audit and the case is a close one, a tie will go to the New York tax department. Of course, if the department is asserting a change of domicile into New York, the burden goes the other way, and the department must prove that the taxpayer intended to change his domicile to New York.5

An often overlooked aspect of domicile cases involves the “leave and land” concept. To change his domicile, a person not only has to leave his old home, but also has to land in a new one. Leaving without landing, and vice versa, won’t get the job done. As stated by the tax appeals tribunal in Knight:

If a domiciliary of New York terminated his residence in New York with the intention of never returning and spent the following several years traveling among the capitals of Europe, residing for a few months in each, and finally returned to the United States to make a home in Florida, he would remain a domiciliary of New York until his new home in Florida was established.6

That example illustrates the leave and land principle quite well. Even though the taxpayer was physically absent from New York for several years, he never landed in another place with the intention of remaining there permanently. Thus, under New York’s tax law, his domicile reverted to New York. And although a taxpayer’s existing domicile continues until a new one is acquired, the law does not require ownership of a home at the new location. A taxpayer can move, live with family or friends, or rent a new home in the new location and still be considered to have changed domicile.7

Overall, of course, the domicile inquiry has to do with a taxpayer’s feelings and intentions, which can be difficult to quantify. The nonresident audit guidelines that the tax department has put together are of great value in assisting auditors (and practitioners) in working through the issues that come up during a residency audit. Under the guidelines, the auditor is instructed to analyze the taxpayer’s lifestyle, using five primary factors to determine where the taxpayer’s domicile — his one, true home — is actually located. The tax department uses a comparison of those five factors, and a series of less significant other factors if necessary as an objective means to a subjective end: On balance, the place the factors most heavily favor is likely the taxpayer’s domicile.

III. The 5 Domicile Factors

A. Home

The home factor reviews the use and maintenance of the taxpayer’s New York residence as compared with the nature and use patterns of the non-New York residence. In other words, does the taxpayer behave as though the non-New York residence is her home? That is particularly crucial when a taxpayer, whose domicile is in another state, acquires a New York residence, or when a residence in New York is retained after a move to another state. So questions about timing, and which residence was owned or occupied first, are often important. But other questions often arise. Is one residence owned but the other a rental? What is the value and size of each residence? What actions did the taxpayer take to remove herself from the old community? Has she established roots in the new community? Where does the family spend holidays and special occasions? Those are the questions practitioners have to ask, because the auditor will.

B. Active Business Involvement

This factor considers the pattern of employment and the compensation derived from that employment. It also examines the taxpayer’s active business involvement other than employment. Ongoing participation in decision-making

7There’s an older case that we usually cite for this principle. In Aetna National Bank v. Kramer, 126 N.Y.S. 970 (1st Dep’t 1911), a move into temporary quarters in the new state of domicile was sufficient because the taxpayer otherwise had the intent to remain permanently.
and frequent communication with a business, even after
official retirement, can be viewed as the most significant
evidence of one’s domicile.8

For this factor, we would want to determine where the
taxpayer actually worked on a daily basis as well as the
location of his primary office. If the taxpayer is a partner or
shareholder in a New York business, the level of participa-
tion in the day-to-day management of the business can also
be considered.

Often, the taxpayer is retired, so that can be a non-factor.
Sometimes a taxpayer moves from New York to Westchester
County, Long Island, or another city suburb. She continues
to work in New York after the move, but only as a com-
muter, not a resident. Auditors are instructed to be reason-
able in that situation and not conflate the value of that factor
vis-à-vis a taxpayer’s otherwise strong non-New York City
connections.

C. Time

Time is often the most important factor in a domicile
case. Generally, an individual is going to spend the majority
of time at his home, so the residency audit is naturally
focused on the time factor, which has a few important
aspects.

First, often we see taxpayers focus on the statutory resi-
dency test detailed below and do everything they can to
ensure they spend less than six months in New York. That’s
great, and it’s obviously important, but a taxpayer who
spends 182 days in New York might still have a residency
problem under the domicile test.

Second, as indicated, with the time factor, auditors are
trying to determine where the taxpayer spends most of her
time. If the taxpayer does not spend more time in her
claimed home than in any other location, the auditor will
have questions. A look at the raw number of days spent in
any given place, however, is not always determinative. In-
deed, the domicile test focuses on a change in patterns more
than a simple quantification of days in and out of New York.
For instance, as clearly stated in the audit guidelines, the
auditor “should focus on the overall living pattern of the
taxpayer, asking whether the patterns present strong evi-
dence that the new location has become the taxpayer’s domicile.”9 Thus, for example, a taxpayer who goes from
spending 300 days in New York to 150, and from 10 days in
Florida to 145, certainly may be able to establish a change in
domicile given the change in pattern.

Moreover, this factor sometimes takes on less importance
for those who commute into New York. As the New York
Tax Appeals Tribunal has said, regular presence and signifi-
cant time in New York City, without further proof of a New
York domicile, is not inconsistent with a suburban com-

92014 nonresident audit guidelines, supra note 2, at 27.

mutter who comes into New York just for work or play.10
Along the same lines, while statutory residency is concerned
with a day-count test that focuses on whether the taxpayer
spent any part of a day in New York — that is, “a minute is
a day” in New York — practitioners can advocate for a
different application of the time factor analysis when the
facts warrant it. For example, if the taxpayer spent 250 days
in New York City, but didn’t spend a single night in New
York City during a particular tax year, the 250 days in the
city will rightfully carry less significance.

Finally, to state it bluntly, the time factor can be a real
pain. Proof of day-to-day location in some form or another
is generally required for every single day in the audit period.
Maintaining that evidence, and then producing it on de-
mand, is obviously a time-consuming process, and — such
as the statutory residency test described below — one that
requires an examination of diaries or appointment books,
expense reports, credit cards, phone bills, frequent flier
statements, passports, and similar documents.

D. Near and Dear

This factor is often the most unusual. The auditor will
investigate the location of items that are of value to the
taxpayer, whether the value is monetary or sentimental.
Auditors often use insurance riders to attempt to verify the
location of treasured items, defined as “those personal items
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This factor used to be considered only if the auditor
could not reach a conclusion using the other four primary
factors, but in today’s residency audit, this factor is analyzed
along with the other primary factors in the ordinary course
of the audit. However, its scope is limited. Auditors are
supposed to consider only where a taxpayer’s spouse and
minor children live. Indeed, as acknowledged in the tax
department’s audit guidelines, the location where minor
children attend school can be one of the most important
factors in a domicile audit. Occasionally, however, the loca-
tion of other family members (siblings, parents, and so
forth) may be determinative in a person’s choice to change
domiciles. When we find that to be the case, we bring it to
the auditor’s attention.

Notice that so far, none of the five primary domicile fac-
tors look to things such as voter registration or driver’s
license. Those are the so-called other factors (so-called in the
tax department’s audit guidelines), and they include:
• the address at which bank statements, bills, and other
family and business correspondence are received;
• the physical location of safe deposit boxes;

10Knight, DTA No. 819485.
112014 nonresident audit guidelines, supra note 2, at 29.
the location of auto, boat, and airplane registrations and of the taxpayer’s driver’s or operator’s license;
• voter registration, and where and when the taxpayer voted;
• possession of a New York City parking tax exemption;
• telephone services and activity at each residence; and
• a taxpayer’s domicile declaration in legal documents such as a will and through property tax exemptions.12

Although it is important that taxpayers who change their residence have those things, generally the items aren’t the types of things that are determinative in a residency audit. In fact, they can’t by themselves be determinative of a taxpayer’s domicile.13 We like to think of the other factors as defensive in nature and have them to back up our residency position — but they won’t be enough to carry the day.

So how do you present all that in the context of an audit? While every case is different, there usually is no substitute for a well-written “domicile letter” clearly explaining your position on each factor and backing it up with proof and documentation. Sometimes, it helps to present the information in a live meeting, too, but having it all down on paper is usually a good thing. And it might help to bring the taxpayer along to talk about the domicile issues. Usually, we don’t find that is needed, and it’s often an unnecessary stress on the taxpayer. But in the right case, with the right set of auditors who have an open mind, it can make all the difference, so don’t rule it out.

IV. The Statutory Residency Test

A taxpayer can also be a resident if he qualifies as a statutory resident of New York state or New York City under section 605(b)(1)(B) of the New York Tax Law. A statutory resident is one who “is not domiciled in this state but maintains a permanent place of abode in New York state and spends in the aggregate more than one hundred and eighty-three days of the taxable year in this state.”14 Those are two separate requirements: A statutory resident must both maintain a permanent place of abode (PPA) in New York and spend more than 183 days in New York.

The first requirement, maintenance of a PPA, has different parts. First, the place of abode must be a dwelling place, meaning it must be suitable for human habitation throughout the year. A rustic hunting camp lacking running water and heat, for example, would not qualify as a taxpayer’s PPA. Nor would a dwelling that is suitable for living but used only for vacation purposes, perhaps because it doesn’t have heat in the winter or year-round road access.15 And significant construction on an abode can also undermine the notion that it is a PPA. Photos, utility bills, construction documentation, and other materials could be used to prove all that.

Also, the taxpayer must maintain the place of abode as a residence for himself. Ownership or a property interest in the dwelling is irrelevant. For many years, taxpayers and the New York tax department have disagreed over what is required for a taxpayer to be considered maintaining a PPA in New York. New York’s highest appellate court recently addressed that issue in Matter of Gaied, 22 N.Y.3d 592 (2014).16

Other unique situations can lead to a taxpayer being considered to maintain a PPA in New York. Corporate apartments maintained for use by an executive or employee are one example. If a company maintains a corporate apartment that is used by many people, or if an apartment is maintained as something other than a residence for the taxpayer or his family, the apartment would not be considered the PPA of any one person. However, under audit, the taxpayer would have to show that the apartment was regularly used by more than one person (and that the taxpayer didn’t have a dedicated space or bedroom within the apartment), usually by providing records or other proof that arrangements must be made in advance for the apartment’s use.

Finally, the PPA must be maintained for substantially all of the year, which the tax department has historically interpreted as a period exceeding 11 months.17 That issue often arises when an executive is transferred to New York on a part-time basis. Provided the executive maintains his domicile elsewhere, he won’t be a resident of New York for the part-year periods at the front or back end of his stay in New York. Alternatively, some taxpayers rent out their place for a short time during a tax year, or their apartment is unavailable because of construction or other issues. Under the so-called 11-month rule, those taxpayers probably would not meet the statutory residency test, although the department has recently called that into question as well.18

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12Id. at 38.
13Id. at 37.
14Id.
1520 NYCRR section 105.20(c).
18TSB-A-04(4)I, 2014 nonresident audit guidelines, supra note 2, at 63-64. The guidelines state that the 11-month rule is general and not absolute. Thus, with short-term vacancies and leases, the department can take the position that the 11-month rule is still met. The guidelines note that to prevent abuse, the 11-month rule will generally be applied in years when a taxpayer acquires or disposes of a residence. If an apartment is under substantial construction, rendering it uninhabitable for several months during a tax year, for example, the department (Footnote continued on next page.)
The second requirement for statutory residence, spending more than 183 days of the tax year in the state (and in New York City, if city residence is an issue), is often the most difficult and frustrating aspect of a residency audit. To begin with, the 183-day test does not apply only to full days. Days for that purpose are parts of days — and any part of a day is equal to a full day in New York.\textsuperscript{19} So, for example, if the taxpayer wakes up in his New York apartment on Saturday morning, drives to Atlantic City for the weekend and returns to New York after dinner Sunday evening, he still has two days in New York. Also, the burden of proof is on the taxpayer, and unidentified or undocumented days are counted as New York days. Thus, if there’s no proof of where the taxpayer was on a particular day, can you guess how the auditor will treat it?

The guidelines instruct auditors to be reasonable, but taxpayers shouldn’t bank on auditor reasonableness in lieu of keeping excellent records. If the taxpayer has established that he was in Florida on Tuesday and Thursday, for example, the auditor should concede that the taxpayer was in Florida on Wednesday, absent any evidence to the contrary. Similarly, the auditor is instructed to think about the kinds of documents the taxpayer would be generating when she is at home on weekends and holidays. Most people don’t generate much documentation when they are at home working in the garden or spending time with their families. Thus, as stated in the recent revision to the guidelines, undocumented weekend days and holidays are usually assumed to be at home — that is, at the non-New York or non-New York City domicile.\textsuperscript{20} However, if the auditor sees lots of evidence that a taxpayer is in New York on weekends, the taxpayer may lose the benefit of the assumption of weekends at home.

In terms of the documentation needed during the audit, there’s a laundry list of items to consider, including:

- **Credit card or ATM statements.** Taxpayers tracking their time in New York should maintain a separate credit card for use there. Their spouses and children also should have separate credit cards. American Express separates purchase detail for each separate cardholder on monthly statements, but other companies that aggregate purchases made by various cardholders on a single statement pose difficulties for taxpayers on audit. Keep an eye out for entities that generate “false positive” New York activity, which can occur because a credit card is on file at a dry cleaner or a grocery store, or because of online or remote purchases. Be sure to keep a receipt or invoice for all online purchases, and keep an eye out for a distinction between the date a transaction is posted to a credit card or bank account, and the date the transaction actually occurred. Occasionally, there are discrepancies between these two listings.

  - **Personal diary.** The tax department should accept a personal, contemporaneous diary as proof of a taxpayer’s location, but it often doesn’t. The credibility of a personal diary is considerably bolstered by corroborating third-party documentation.

  - **Electronic calendars.** Taxpayers can retroactively alter electronic calendar appointments and entries, which limits their usefulness on audit. Taxpayers should be careful amending calendar appointments, unless done within a reasonable time following the original appointment.

  - **Flight or travel records.** Taxpayers should keep all travel records, including boarding passes, hotel folios, receipts for fuel and other purchases, and limo and taxi receipts. They should join frequent flyer programs, which can act as a backup record of the customer’s flight history for numerous years.

  - **E-ZPass records.** E-ZPass records are a common source of documentation in residency audits, particularly when a taxpayer lives in the tri-state area and commutes into New York City or state for work. Taxpayers should be careful to avoid commingling E-ZPass tags among several users or vehicles, because it’s often difficult to determine who was in what vehicle at what time when tags are shared. Each family member should have a separate E-ZPass account in her own name. It’s sometimes difficult to obtain E-ZPass records from a non-New York E-ZPass authority, which makes saving E-ZPass statements as they’re generated more important.

  - **Driver logs.** If a taxpayer has a personal driver or limousine service, it’s important for the driver to keep a detailed and contemporaneous log indicating who was in the car, the origination location and destination of each trip, and date and time of each trip.

  - **Landline phone.** It’s often difficult for taxpayers to obtain detailed reports of their landline telephone use. That information is sometimes of limited value anyway, because multiple users could be making or receiving phone calls (including staff and visitors). That doesn’t stop the New York tax authority from issuing subpoenas to obtain landline call detail, however.

  - **Cellphone use.** Cellphone statements and use reports can be useful in a residency audit, but they are getting more difficult to obtain from various service providers. For a fee, Verizon Wireless will provide historic monthly billing statements to customers listing call origination detail, but obtaining similar records from other companies is difficult or impossible, unless the New York tax department issues a subpoena for the information.

\(19\) 20 NYCRR section 105.20(e); Matter of Zanetti, DTA No. 824337 (Tax App. Trib. 2014).
\(20\) 2014 nonresident audit guidelines, supra note 2, at 66.
• **Swipe card records.** Many companies and buildings maintain records and logs of an occupant or employee’s entrances and exits through electronic entry systems. When these records are available, auditors request them. However, the records are often destroyed on a revolving basis and thus may be available for only a limited period.

• **Monaeo.** Our firm worked with the founders of Monaeo in the development of an accurate mobile platform that taxpayers can use to track their day-by-day location throughout the year. Monaeo was rolled out in 2012, and we’re starting to see the location records it generates implemented in New York residency audits with positive results.

V. Other Nuts-and-Bolts Issues

A. **Timing**

Residency audits tend to be slow. The accumulation and analysis of the documents can take months, if not years, and discussion and negotiation also can drag on. So sit tight. Of course, many audits are resolved for less than 100 percent of the tax that might otherwise be due. But a practitioner’s ability to negotiate a resolution will depend in large part on the quality of the documentation available.

B. **Interest and Penalty**

In most circumstances, statutory interest will be added to any tax liability determined as a result of the audit. It cannot be reduced or negotiated. Interest rates change quarterly but have recently been steady at 7.5 percent for personal income tax deficiencies. As for penalties, New York law provides for the imposition of penalties for failure to file, failure to pay, substantial understatement of income, and negligence. During the negotiation process, practitioners should attempt to abate those penalties as a condition of settlement.

C. **Federal Tax Issues**

A New York residency audit generally does not affect the federal return for the year under audit. However, any New York tax paid as a result of an audit may be deductible on the taxpayer’s federal return for the current year if the taxpayer itemizes deductions and is not subject to alternative minimum tax. To alleviate potential AMT issues, practitioners often can structure an agreement under which the taxpayer pays part of the tax in the current year and part of the tax in the next year. That often makes more of the New York tax usable as an itemized deduction.

D. **Home State Issues**

In many cases, taxpayers are advised to file protective refund claims with their home state to keep its statute of limitations open until the New York audit is concluded. Why? In some cases, the additional New York tax paid may be used to claim a credit from the taxpayer’s home state for the taxes paid to New York. That is not a dollar-for-dollar calculation and will be limited to the amount of tax actually paid to that state on the New York income as well as that state’s rules regarding allocation of income and other items. But it often softens the blow.

E. **What About Next Year?**

Domicile, once determined, remains the same until the taxpayer acts to change it. So if domicile is the only issue in an audit, and the auditor agrees that the taxpayer is not domiciled in New York, there should be no later audit unless the taxpayer relocates to New York or takes some other action that might be construed as relocating.

But statutory residency stands alone. It can be examined every year. As a practical matter, though, our experience has been that a taxpayer who has proven she did not spend 183 days in New York during the audit period can potentially avoid being re-audited for several years. However, a taxpayer who was unable to prove that she did not spend 183 days in New York during the current audit period, or who spent close to 183 days in New York, probably won’t have the same luck.

VI. **Conclusion**

Is that everything you need to know about residency audits? Of course not. We’d need a whole book for that.21 But this article should give you a flavor of the types of issues that will come up in every residency audit. The tax department’s efforts in this area continue to expand, so it’s important for you and your clients to be aware of them.

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