



ULLMAN

Update

## New York State Tax Residency:

## AN OUNCE OF PLANNING IS WORTH A POUND OF AUDIT

E. Parker Brown, II &amp; Edward Schusler, Senior Vice President

When snow drifts up to the windowsills many a New Yorker of a certain age looks longingly toward retirement in balmy Florida – or at least they did before Florida turned into hurricane alley. Many contemplating a change of domicile to Florida (or elsewhere) assume that the tax consequences are automatic: move to Florida and establish residence there, cease to be a resident of New York for personal income tax purposes. Unfortunately, it's not so simple.

To explore this thorny topic, Edward Schusler, JGUA Sr. Vice President, has interviewed E. Parker Brown, II, an attorney in Syracuse who concentrates his practice in the area of New York State taxation. Parker has handled residency cases for twenty-five years from the planning stage to audit to appeals to litigation.<sup>1</sup> Ed has assisted numerous clients of John G. Ullman & Associates over many years with financial planning for retirement, including advice on the tax ramifications of retirement in other states.

**Ed Schusler:** Let me thank you for agreeing to answer questions on New York residency. To lay the groundwork for our discussion, will you please explain what can occur when a person in good faith changes his or her residence from New York to another state such as Florida.

**Parker Brown:** I will be delighted. The short answer is that the New York Tax Department may not recognize the change. The Department may deem the person to remain a New York resident and subject to New York tax on both earned and investment income. Often such a determination is made on audit of a taxpayer



E. Parker Brown, II

several years after the individual's intended establishment of Florida residency. The result can be a New York tax bill, including interest and penalties, of substantial proportions.

**Ed Schusler:** What test does New York apply when it makes a residency determination?

**Parker Brown:** New York has a two-part test. The first prong of the test concerns domicile, while the second prong deals with what New York calls "statutory residency." If a person, despite his or her efforts, remains a domiciliary of New York, then the person is a tax resident of the state. There is no reason to go on to the second prong of the test. But, if a person is not a domiciliary of New York, then the second prong comes into play. The person may be held a statutory resident of New York and subject to New York's personal income tax as a resident individual.

**Ed Schusler:** But on audit a person may be held to be both a domiciliary and a statutory resident.

**Parker Brown:** That's right. Auditors may see it that way. They may think the taxpayer failed to prove a change of domicile and that the taxpayer, in any event, failed to prove that he or she didn't fall in the statutory resident category.

**Ed Schusler:** Speaking of proof, what is required of the taxpayer?

**Parker Brown:** The burden of proof under both tests is on the taxpayer. It is imperative that the taxpayer undertaking a change of tax residency maintain good records documenting both the change of domicile and the factors relevant to the statutory residency test. I will come back to record keeping later.

"The burden of proof under both tests is on the taxpayer."

<sup>1</sup>Parker emphasizes that his comments here are for informational purposes only and are not intended as legal advice. He also notes that space limitations prevent discussion of persons present in a foreign country, military personnel, and other aspects of the residency topic, including New York City ramifications.

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# AN OUNCE OF PLANNING IS WORTH A POUND OF AUDIT

*E. Parker Brown, II & Edward Schusler, Senior Vice President*

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## The Domicile Test

**Ed Schusler:** Would you explain how the domicile test works?

**Parker Brown:** As I have said, a domiciliary of New York is a tax resident of New York.<sup>2</sup> A person's domicile is the place which an individual intends to be his or her permanent home; the place to which an individual intends to return whenever he or she may be absent. In an old, but influential, decision, New York's Court of Appeals wrote that "in order to acquire a new domicile there must be a union of residence and intention. Residence without intention, or intention without residence is of no avail." The Court continued that "there must be a present, definite and honest purpose to give up the old and take up the new place as the domicile..." "Every human being may select and make his own domicile, but the selection must be followed by proper action."

**Ed Schusler:** So a domicile change is a matter of intent, but the intent must be proved by deeds?

**Parker Brown:** Exactly. The taxpayer must come forward with clear and convincing evidence to carry his or her burden of proof, and this evidence necessarily will focus on actions consistent with the mental intent.

"The taxpayer must come forward..."

**Ed Schusler:** What kind of actions are we talking about?

**Parker Brown:** I will go over these in detail. But let me generalize for a minute based on my practical experience: The actions of a taxpayer seeking to change domicile need to reflect a real, as distinguished from a merely formal, change of lifestyle. To use

military parlance, something must happen "on the ground," not simply in the paperwork.

**Ed Schusler:** But the paperwork – such as shifting drivers' licenses from New York to Florida – may assume importance if it is not done.

**Parker Brown:** A good point. Cumulatively, registration changes, formal declarations and the like could be quite important if neglected. But the fact remains that these things are seldom determinative.

**Ed Schusler:** How do taxpayers generally go about changing domicile?

**Parker Brown:** There are two basic patterns, I would say. Changes of domicile tend to be either a matter of crystallization of intent at a certain moment, typically at retirement, or a matter of evolution over time. The former are easier to prove. When there is a clean break from New York as of a date certain, it is usually easier to document markedly different "before" and "after" lifestyles. (And, to avoid part-year complications, the clean break might be made as of January 1<sup>st</sup>, unless there are reasons to do otherwise.)

"...a clean break from New York..."

**Ed Schusler:** How does the "evolution" scenario differ?

**Parker Brown:** To give a common example, the taxpayer begins as a typical snowbird vacationing in Florida in the winter. As the years go by the taxpayer spends increasing amounts of time there, and, at some point, the taxpayer decides to make Florida his or her permanent home. The question often is what point, because "before" and "after" lifestyles are not markedly divergent. This is a prime example where good planning can eliminate problems upon audit.

**Ed Schusler:** Are there any regulations issued by the New York Tax Department on all of this?

## Domicile: Primary Factors

**Parker Brown:** Yes, there are helpful regulations, but these are rather brief. A much more extensive discussion of residency is found in the Tax Department's "Nonresident Audits Outline" in the manual it issues to auditors. For convenience, I'll call this the "Audit Guidelines" or simply "Guidelines." These instructions establish two categories of factors relevant to a domicile determination: "primary" factors and "other" factors. The Audit Guidelines list five primary factors.

**Ed Schusler:** What are these?

**Parker Brown:** 1) Home; 2) active business involvement; 3) time; 4) items "near and dear;" and 5) family connections.

**Ed Schusler:** And these, in the Tax Department's view, are the really important areas of inquiry regarding domicile?

**Parker Brown:** Yes. I will add that, in my experience with audits, home, active business involvement and time are often the heart of the case. They seem to be, as a practical matter, more important than items near and dear and family connections. In the Audit Guidelines the explanation of "home" takes up five closely-spaced pages, whereas the explanation of "family connections" takes up a little over one page.

<sup>2</sup>There is a seldom-encountered exception in the law for a domiciliary who maintains no permanent place of abode in New York; maintains a permanent place of abode elsewhere; and spends not more than 30 days in a given year in New York.

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**Ed Schusler:** Can you give us the flavor of the discussion of the primary factors in the Guidelines?

**Parker Brown:** Space limitations prevent me from summarizing all of this advice to auditors, but I can cite a few of the questions often asked about each factor. Regarding the “home” factor, has the taxpayer sold his or her old primary dwelling in New York? If not, has the taxpayer attempted to sell it? Has the taxpayer traded down to a smaller dwelling in New York? Has the taxpayer bought a new home in Florida? If a dwelling is retained in New York, how does it compare in cost and square footage with the Florida dwelling? Has the pattern of use of the old New York dwelling, if retained, changed (say, from year-round to summer)? Is either the old or new dwelling leased as opposed to owned?

**Ed Schusler:** These questions are relevant to the comment you made earlier – that the New York Tax Department will be looking for a real change of lifestyle. Parting with the old family dwelling or markedly diminishing one’s usage of it point to a bona fide intention to take up residence elsewhere.



Edward Schusler

**Parker Brown:** Exactly. And that is true as well of the remaining primary factors. Regarding the second factor, the Guidelines state that “the degree of active involvement in New York businesses in comparison to involvement in businesses located outside New York is an essential element to be determined during audit.”

The Guidelines continue, “In today’s world of electronic gadgetry and instant communications, involvement with New York businesses can take place from afar or while physically present in New York State. The degree and dimension of a taxpayer’s involvement in the day-to-day operation, or in a policy position, must be analyzed during audit.”

**Ed Schusler:** The most clear-cut scenario is retirement and relinquishment of corporate office and duties in a New York business. A problem can arise when the involvement in a New York business – especially a close corporation – continues without very much diminishment.

**Parker Brown:** Yes. Then the question becomes “Has this person really made a change in his or her business life?” The Guidelines indicate that “passive investment in a New York business is not indicative of domicile whereas a taxpayer actively participating in the management of a business may be.”



Attorney Brown practices law in Syracuse, NY, primarily in the area of state and local taxation. From 1986 to 1995 he was a member of the Executive Committee of the NYS Bar Association’s Tax Section. He is a graduate of the University of Virginia School of Law and is admitted to the Bars of New York, the District of Columbia and Virginia.

## STAY TUNED:

Part II of the Interview with Parker Brown will be published in the Winter 05 issue of the Ullman Update. If you desire a printed copy of the interview in its entirety, please call or email us at [info@jgua.com](mailto:info@jgua.com) and we will send a copy out to you.



# THINKING OUTSIDE THE SHOEBOX

Rebecca Bement-Patros & Jessica Lawrence, CPA



Rebecca Bement-Patros

*S*O receipts from different years added incorrectly. Three handwritten sheets of paper with business income and expenses in no particular order with no supporting documentation. Taxpayer's, spouse's, and children's W-2s, 1099s and medical expenses tossed in a shoebox. If your tax information looks like this, we have some helpful hints.

The following list explains the information a preparer needs to prepare a complete and accurate return.

- **Wages** - The W-2 is imperative for preparation of your 1040 and is a required attachment to your federal and most state returns. Provide all your W-2s to your preparer.
- **Interest, Dividends and Capital Gains & Losses** - To properly report interest and dividends, Forms 1099INT and 1099DIV are needed. These normally come in a package that also includes your Form 1099B, Gross Proceeds, necessary to prepare your Schedule D. The entire package comes from your broker and should be delivered in kind to your preparer.
- **Taxable State Refund** - If you received a state refund last year, send Form 1099G from the state.
- **Self-Employment and Rentals** - If you are a contractor, sole proprietor, or rental property owner, please enclose a summary of your income and expenses for the year. Also provide a detailed list of any equipment, furniture, fixtures and building improvements including the date the asset was placed in service and the original cost.
- **Other Income** - If you received a Form 1099MISC for anything other than your main source of income, please send it with a description of the source.
- **Retirement** - Pension and IRA distributions will be reported on Form 1099R and Social Security received will be on Form 1099SSA. As with the W-2, these forms are imperative for preparation of your return and need to be sent to your preparer.
- **Ownership Interests** - Are you an owner in a partnership or S-Corporation? Are you a beneficiary of a trust or estate? Do you receive royalty income? If you answered yes to any of these questions, you may be receiving a Form K-1 from that entity that needs to be included in your tax information.
- **Retirement Contributions** - Any contributions made to an IRA, SEP, or Keogh should be reported to your preparer. Waiting for your accountant to tell you how much to contribute? Send a reminder note!



Jessica Lawrence

- **Student Loan Interest** - Former students repaying student loans should send in Form 1098E which reports student loan interest paid.

- **Education Expenses** - Current students paying tuition and fees for education should send Form 1098T. Tuition and fees from colleges are reported to you on that form.

- **Itemized Deductions** -

- **Medical** - Send in a summary of medical expenses. Although medical expenses are subject to a 7.5% AGI threshold, they add up quickly, so please keep track of them throughout the year. Some pharmacists and doctors are able to print you a year end list of expenses paid and the insurance reimbursement.

- **Taxes and Interest** - If you have a mortgage or a home equity loan, send in your Form 1098. If your real estate taxes are not included in your Form 1098, please provide tax bills. If your state charges personal property tax based on the value of an asset (your car for example), please provide the tax bill.

- **Charity** - Send a summary of all charitable donations. Maintain receipts either with your preparer or in your files as they may be required in the event of an audit. For any noncash donations, a helpful valuation guide from the Salvation Army is at [www.satruck.com/ValueGuide.asp](http://www.satruck.com/ValueGuide.asp). This provides a general guideline, but the actual deduction depends on the condition of the item. Please include the date of non-cash donations in your information. If you donated a vehicle this year, let your preparer know as soon as you can. It's a good idea to take a picture of the car just prior to donation in case of a future audit. Don't forget, if the fair market value of any single donation is greater than \$5,000, the IRS requires an appraisal (except in the case of publicly traded securities).

- **Dependent Care Expenses** - If you paid child and dependent care expenses, send the cost per child, location, name and employer identification number of the child care provider. You may be eligible for the child and dependent care credit.

- **Estimated Taxes** - Provide dollar amounts and dates paid for all estimated tax payments. We cannot stress enough how important it is to properly report estimated tax payments. A large percentage of our IRS correspondence relates to improper reporting of estimated payments.

The JGUA Tax Department is available year round to help with questions and concerns. If you are having trouble gathering your tax information, call your Account Executive, Tax Preparer or accountant, they can help. Don't fear the shoebox face it head on!



# JGUA NEWS

*John G. Ullman & Associates, Inc. is pleased to announce two staff members assume corporate responsibilities.*



Cathy Crandall

Catherine B. Crandall has been named Chief Compliance Officer for the firm in addition to her ongoing responsibilities as Account Executive. In this role, she is responsible for the ongoing regulatory compliance requirements for the firm and its Broker Dealer subsidiary, USGM Securities, Inc.. Cathy is a graduate of St. Lawrence University and possesses a JD from Albany Law School of Union University, a LLM from Columbia University School of Law and an MBA from the University of Rochester, William E. Simon Graduate School.

James A. Kaffenbarger, Jr. has been named Corporate Secretary. James continues in his role as Account Executive while concurrently performing the legal tasks of the corporation. James is a graduate of Miami University and obtained his JD from Case Western Reserve University School of Law. He joined the firm in 2000.



James A. Kaffenbarger, Jr.



## SEEING DOUBLE!

Another set of twins have joined the “Ullman Family!”

We’ve been seeing double lately! We’ve added another set of twins – making it three sets in three years to Ullman staff families! Molly and Jack Creath arrived on 11/23/04 to JGUA Account Executive Sarah Creath. They join fellow twins Rianne and Nikolus Nickerson, age 3, pictured with dad, and JGUA Account Executive, Jason, and Sarah and Matthew Coon, age 1, with mom, and JGUA Account Coordinator, Jennifer.



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Design:  
Graphic Solutions

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*During this special time of year, the Staff of John G. Ullman & Associates, Inc. wishes you Happy Holidays and all of the best in 2005.*

Please remember – Since the renovations to our offices in 1998, our official address changed to 51 East Market Street. The post office will not deliver any mail addressed to the old address of 94 Cedar Street.

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## COMPREHENSIVE FINANCIAL MANAGEMENT SINCE 1978

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