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Practice Update

Heading South: Understanding the Rules of Changing Residency

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It's Trickier Than You Think, Even for the President

In a tweet on October 31, 2019, the President announced that New York "will always have a special place in my heart!" While there may be political reasons for relocating to Florida, he is taking a path that many other northerners have taken before him to save big on taxes.

President Trump's "Declaration of Domicile" statement filed in Palm Beach County Circuit Court in September is a necessary step toward eliminating his state and city income tax of 13 percent, and just as important, if not more important, avoiding an estate tax of 16 percent. However it will take more than filing a form to convince auditors that one's legal residence has changed. The migration of taxpayers from high tax states like California, Illinois, New Jersey, and New York accelerated starting in tax year 2018, after Congress adopted legislation capping an annual deduction for state and local taxes paid at $10,000 for individuals.

High-net-worth individuals leaving New York[1] are permitted to say that they are headed to Florida for tax reasons. However, understanding the rules of residency and planning for the necessary steps to take (and for the audit that will probably come) are imperative. The hardest situation to remedy is when

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someone waits until he or she sells a business and then says, “Now, how can I become a Floridian?”

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State residency auditors will not bless a change of residency without a fight because a substantial amount of tax is usually at stake. To convince an auditor, the standard of proof in New York is high, requiring clear and convincing evidence. The burden of proving a change is upon the party asserting the change.

Tax law generally defines a resident as one who:

1. Is domiciled in New York or another taxing state (explained below), or
2. Is not domiciled in New York, but who maintains a permanent place of abode in New York and spends more than 183 days in the state (statutory residency).

Thus, the state gets two chances to make you a resident. Even if you are in New York for less than 100 days, the auditor can still assert that you never changed your domicile. If you are domiciled in New Jersey but commute daily to New York City and maintain a *pied-à-terre*, you could be treated as a resident of both states. While New Jersey would provide a tax credit for the earned income, and personal service income initially taxed in New York, your investments would be exposed to double taxation.

In general, your domicile is:

- The place you intend to have as your permanent home.
- Where your permanent home is located.
- The place you intend to return to after being away (as on vacation, business assignments, educational leave, or military assignments).

You can have only one domicile. A New York domicile does not change until you can demonstrate that you have abandoned your New York domicile and established a new domicile outside New York State. Occasionally, the occurrence of a life event makes the domicile inquiry easier because it supports a typical pattern. Retirement, loss of employment, the death of a spouse, a divorce and re-marriage, or even the growing up of one's children often triggers a desire to change a lifestyle and domicile which can buttress a taxpayer's position.

What is The Domicile Test?

Because one's domicile can be subjective, the auditors in New York and elsewhere look at five primary factors that would allow them to make an objective determination. From these objective factors they draw an inference as to what your intent was.

The primary factors are:

1. ***Home:*** That is, the individual's use and maintenance of a New York residence, compared to the nature and use patterns of a non-New York residence. Also considered is the extent the taxpayer is involved with local community activities.
2. ***Active Business Involvement:*** The active participation in a local business would infer that your domicile is the home that is nearby.
3. ***Time:*** Another one of the primary factors is a quantitative and qualitative analysis of where the

individual spends his or her time during the tax year. The days spent in New York, in relation to the time spent at other locations, should not be the plurality.

4. ***Near and Dear:*** The location of pets, personal items or other sentimental possessions such as fine art and collectibles which the taxpayer holds dear. Also, the location of medical records and financial records are a good indicator as to which residence is one's domicile.
5. ***Family Connections:*** The location where minors attend school can be one of the most important factors in determining where someone is domiciled. The proximity to close relatives may be relevant but without minor children the factor carries less importance.

183

Number of days out of the year an individual must maintain a "permanent place of abode" to be considered a statutory resident.

Where analysis of the primary factors does not present clear and convincing evidence as to an individual's domicile, the auditors should examine the "other" factors in an attempt to clarify the individual's domicile. Taking care of these activities will generally not improve your chances but the failure to do them will be used against you. The type of other factors we are referring to include:

- The address at which bank statements, bills, financial data, and correspondence concerning other family business is primarily received.
- The physical location of the safe deposit boxes uses for family records and valuables.

- The address shown on auto, boat, and airplane registrations as well as the individual's personal driver's or operator's license.
- The state where the individual voted.
- The address listed in testamentary documents.

If you are successful and the auditor agrees with you on the issue of domicile, you still must show that you are not a statutory resident. An individual is a statutory resident if he or she maintains a "permanent place of abode" in the state and spends more than 183 whole or part days in a year. If found to be a statutory resident, your compensation income and investment income will be fully taxable for the entire year. Your attorney can assist you in determining whether your living quarters constitute a "permanent place of abode" and how one counts days for purposes of the day count test.

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If found to be a nonresident, New York sourced income will still be subject to income tax. For example, wages for work performed in New York or rents from property in the state would still be subject to New York income tax, but not income from intangible investment income, which would be sourced to your new domicile. Even if President Trump is not domiciled in New York, he may still owe income tax to New York or another state if he receives income from services performed or generated by property he owns in the state.

Moreover, as the President will surely learn, avoiding taxes by leaving New York may not be that simple. States can and do subject taxpayers who say that they have relocated to intrusive audits that drag on for some time.

Takeaways

Since one's intent is a decisive factor regarding domicile (the crucial question in a residency audit), this subjective inquiry should be made in consultation with residency tax lawyers. Individuals who are not sure whether they want to purchase a home in Florida because they will still have contacts with New York or a neighboring state, must consider all of their contacts from visiting grandchildren to business responsibilities. However, the contacts should not hold someone back from purchasing a home in Florida. One can become a Floridian while not abandoning all contacts in New York or a surrounding state. The key is to understand residency rules and how they operate.

Akerman will be co-hosting a series of seminars in our Naples, West Palm Beach, and Miami offices with Withum and National Social Security Partners addressing the best practices and avoiding the pitfalls of claiming new residency in low-tax states. For more information, please click here.

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[1] For purposes of this update, references to New York generally also include New York City and other high tax states.
