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Home Is . . . Where the Domicile Is?

Part I of a two-part series • By Jeffrey Greener, Esq.

While “home is where the heart is”, “domicile” is where the tax savings reside. Determining one’s domicile becomes very important when a person has connections with New York and another state, and they want to avoid being subject to New York State tax.

New York State Tax Law Section 605(b) says simply that if you’re in New York for more than 183 days a year and you have a permanent place of abode here, you are a “statutory resident” of New York for income tax purposes. However, under some circumstances, even if you pass the 605(b) test (i.e. you spend less than 183 days in New York), you can still be declared to be a New York resident for income tax purposes if you are domiciled in New York.

The general rule is that residency, or more specifically, domicile is defined in terms of one’s intent. Domicile is a term of art that defines one’s legal residence; the place where you wish to make your home. You can have several residences or places of abode, but you can have only one domicile. Proving domicile, however, is more difficult than just stating your preference of living arrangements particularly here in New York State where the Department of Taxation and Finance (the Department) is keen on classifying New Yorkers as New York residents even after they’ve moved.

Determining intent isn’t always easy, but the Department has an aggressive Audit Program directed at “former” residents to determine this issue. The audits generally affect both income taxes while you are living, and estate taxes after your death. These audits result in more than $100 million of additional tax revenue to New York each year.

The Department’s guidelines instruct its auditors to look for four (4) major factors to determine intent:

(1) New York Business;

(2) Home;

(3) Time; and

(4) Items Near and Dear.

In assessing the New York Business factor auditors will ask for phone, email and fax records, as well as other evidence of active participation in the business to conclude that a retiree,

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for example, hasn’t really left his or her New York job. If a retiring entrepreneur retains a significant management or supervisory presence, or a policy-making role in the business, it won’t matter that it’s from long distance. In regards to the second factor, Home, auditors will visit homes in both locations to compare size, value, nature of use and other factors including where key possessions are located.

For the third factor, auditors look very closely at the “quality time” issue. Is the social life centered in New York or the new state? Is your social life still primarily revolving around the children and grandchildren in New York? Did you resign or downgrade to out of state memberships at their New York clubs and other social organizations? Do the taxpayers have new friends, clubs, etc. in the new state? Auditors will ask for diaries, appointment logs, calendars, credit card receipts, ATM records, telephone records and any other evidence of “overall living patterns” that will provide clues to the intent of the taxpayer.

Finally, with the Items Near and Dear, auditors will ask for bills of lading and other shipping records, copies of homeowners insurance policies and the like, to establish where the items “really” are, when they were shipped, etc. In addition to the above four factors, the final item that is sometimes considered by auditors is the Family Connection. However, auditors are instructed that because of the “intrusive nature” of this factor, they are not to consider it unless no domicile determination can be made after a careful analysis of the first four factors. This inquiry basically involves a much more intrusive examination of Item #3 – what is the “commitment” for “quality time” back in New York?

The audit guidelines also list “Other” factors to be considered if a determination can’t be reached after analysis of the “major” factors. Some of the Other factors could obviously be considered as part of one or more of the major factors, but the Department doesn’t place much emphasis on them as independent factors because many, in themselves, constitute symbolic actions totally within the control of the taxpayer. A sampling of the Other factors listed in the audit guidelines are: address to which bank statements, bills, correspondence, etc. are sent; location of safe deposit boxes; state of driver’s license, car or boat registration, etc.; where Federal Income tax returns are filed; Voter Registration location, but more importantly, whether the voting right is actually exercised – not just in November, but local municipal and School Board elections, etc.; type of telephone, computer and cable services at each location; listing of taxpayer’s domicile in Wills and other legal documents.

When evaluating one’s intent, the guidelines make it clear that auditors are not permitted to consider charitable contributions and membership in religious organizations. In other words, if, for example, the newly minted Florida residents want to maintain their old New York charitable involvements and religious congregation affiliations, it can’t be used against them. Despite these admonitions to the auditors in the guidelines, common sense would dictate that, if possible, checks should be sent to Florida chapters of charities, and new affiliations be forged with Florida religious congregations similar to the ones enjoyed by the taxpayers in New York. Alternatively, at least make the new connections while retaining the old ones (e.g. split a $500.00 annual contribution to the American Cancer Society or Red Cross evenly between the Chapters in New York and Florida).

As with any audit, record keeping and accuracy will assist you in successfully establishing your intended domicile. We recommend you keep a diary so that you can show when you were in your new domicile each year and prove your time outside your former domicile. Telephone bills, utility bills and credit card bills all may be indicative of where you were living, so make sure your calendar is accurate. In addition, it is recommended that individuals seeking to avoid running afoul of residency audits purchase or rent a residence in the new state, execute a new Will or codicil and change your residence on all legal documents which recite residency such as drivers licenses, insurance, and voter registration.

In the Winter 2012 edition of our newsletter, Part II of this article will set forth different methods to successfully avoid running afoul of residency audits. The complete article is currently available now on our firm website. ■

Same-Sex Marriages and the Defense of Marriage Act ("DOMA")

By: Sarah B. Rebosa, Esq.

The constitutionality of the Defense of Marriage Act ("DOMA") is being questioned. A New York court in Windsor v. United States, 833 F. Supp. 2d 394 (S.D.N.Y. 2012), is one of several federal courts that recently declared Section 3 of DOMA unconstitutional because it violates the equal protection clause of the Fifth Amendment to the United States Constitution. Section 3 of DOMA states that for purposes of federal law, "marriage" is between "one man and one woman as husband and wife". Section 3 further defines "spouse" as "a person of the opposite sex who is a husband or wife".

The Windsor court stated that defining "marriage" and "spouses" as only between persons of the opposite sex has no "rational basis" to a legitimate government objective. In other words, there is no "logical relationship" between DOMA and the following objectives, or in the alternative, the following objectives are not legitimate enough to justify DOMA: preserving the traditional institution of marriage, promoting an ideal family structure for procreation, ensuring that federal benefits are uniformly and consistently applied, or conserving government resources.

In recent years, several states including New York have enacted laws allowing same-sex couples to legally marry. However, under DOMA same-sex marriages are not recognized for purposes of federal law. For estate tax purposes, Section 3 of DOMA creates a disparity in how estate tax is imposed upon same-sex versus opposite-sex married couples. Generally, spouses are entitled to an unlimited estate tax marital deduction for property passing to a surviving spouse. This means that, if properly structured, there is no estate tax due until both spouses have died. This helps to ensure that surviving spouses are not required to divest their savings in order to pay taxes. Therefore, despite being legally married in one's state, a surviving same-sex spouse is not entitled to the federal estate tax marital deduction. This can result in a significant amount of estate tax due upon the death of the first spouse.

DOMA not only affects estate taxes but it also affects same-sex married couples in many other capacities, such as but not limited to access to federal health insurance plans, income tax, bankruptcy, and immigration. Several other jurisdictions have also addressed challenges to DOMA, resulting in a split of opinions as to whether Section 3 of DOMA is constitutional. Three recent cases that also found Section 3 unconstitutional are: *Pederson v. OPM*, 2012 U.S. Dist. LEXIS 106713 (D. Conn., July 31, 2012); *Gill v. OPM*, 699 F. Supp. 2d 374 (D. Mass. 2010), aff'd, 682 F.3d 1 (1st Cir. 2012); and *Golinski v. OPM*, 824 F. Supp. 2d 968 (N.D. Calif. 2012).

These three cases involve plaintiffs who were married same-sex couples (or a surviving same-sex spouse) under their respective state's law. Each of the plaintiffs were either denied a lump sum death benefit payable to spouses under Social Security, denied access to a spouse's federal employee health insurance plan, denied access to theirs spouse's federal flexible spending plan, denied leave under the Family Medical Leave Act to care for a spouse, denied certain benefits as a spouse under Medicare Part B, or denied the right to file joint federal income tax returns.

It is anticipated that the United States Supreme Court will soon address the constitutionality of DOMA. As of August 2012, the parties in *Golinski* and *Windsor* had filed for a Writ of Certiorari Before Judgment with the U.S. Supreme Court, which is a request for expedited review. If granted, these cases would skip intermediate appellate review and move directly to the highest court of the nation. *Gill* is already pending in the U.S. Supreme Court. If Section 3 of DOMA is ultimately determined to be unconstitutional, then same-sex married couples will be entitled to the same benefits under federal law that opposite-sex married couples are already entitled to, including the unlimited estate tax marital deduction. ■

Technical Section

By Moira A. Jabir, Esq.

President Obama's Budget Impacts Intentionally Defective Trusts

If President Obama's 2013 budget proposal passes then a grantor trust would be included in the grantor's estate or used to pay gift taxes if trust assets are distributed before the grantor's death or the grantor ceases to be treated as the owner. This attempt to deter the use of the Intentionally Defective Grantor Trusts is the first time the government has taken notice of this popular estate planning tool.

New Net Investment Tax to Impact all Non-Grantor Trusts

With the passage of the new health care plan, it is anticipated that beginning in 2013, all non-grantor trusts and estates with income over $11,200 (indexed for inflation) will be subject to a new net investment tax of 3.8%, although the Internal Revenue Service has not yet issued guidance.

Representatives Personally Liable for Estate Tax Despite Indemnity Agreement

In *U.S. v. Johnson*, Case No. 2:11-CV-00087, the decedent was survived by four children of whom two were her fiduciaries. The fiduciaries deferred a portion of the estate tax under IRC Section 6166 and later distributed the decedent's assets to her beneficiaries who had agreed in writing to each pay their proportionate share of the unpaid estate tax. A few years later the decedent's corporation went bankrupt, the estate defaulted on the unpaid taxes and the IRS sought payment from the fiduciaries as well as the beneficiaries. The Court concluded that Section 6324(a)(2) which imputes personal liability to a decedent's transferees, was not applicable to the beneficiaries despite the indemnity agreement because they were only entitled to receive the assets after certain gifts were made and all taxes were paid. Instead, the Court concluded that the Trustees of the family trust which received all the assets under the decedent's Will were the transferees under IRC Section 6324(a)(2).

Gifts of Limited Partnership Interests Qualified as Present Interests for Annual Exclusion

In *Wimmer v. Commissioner*, T.C. Memo 2012-157 (June 4, 2012), the court found that the gifts of limited partnership interests qualified for the annual exclusion because the donees received income distributions. This case is significant because three cases prior to Wimmer had denied the annual exclusions for gifts of limited partnership interests. In order for gifts to convey a present interest, they must convey a substantial economic benefit by allowing use, possession or enjoyment of (1) property or (2) income. In *Wimmer*, since the partnership agreement contained so many restrictions on transferability, the Court determined that the beneficiaries did not have a present right to use the property. However, using a three-part test which demonstrated that the partnership was expected to generate income, the income would flow steadily to the beneficiaries and the income was ascertainable based on the stock history, the Court determined that the beneficiaries had a right to the income and thus that the gift qualified for the annual exclusion. ■

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