The Goods on *Gaied*: What It Means, From the Front Lines

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For more than 25 years, New York's residency audit program has been in high gear, and residency issues have been a major part of many tax practices. Recently, New York's highest court issued an important residency decision — the first time in decades it has weighed in on the question.

In this article, the authors, who represented the taxpayer, discuss what the decision means for future residency cases.

As most readers know, New York's highest court recently issued a groundbreaking decision on the state's residency rules — one of the first times that court has addressed this important New York tax issue. *Gaied v. New York State Tax Appeals Tribunal*, No. 26 (N.Y. 2014), has left practitioners and commentators buzzing over the ramifications for New York residency audits.[1] Many think it is a big deal and that it will have a huge effect on future cases. Others have had more tempered reactions, viewing the case as a great win for John Gaied, but not one that will affect many others, given the unique facts in the case.

As the lawyers who litigated *Gaied*, we thought it was time to weigh in. And as one might expect, we're in the "big deal" camp. When New York's highest court makes a new pronouncement on income tax residency — an issue typically confined to administrative appeals — practitioners, taxpayers, and the New York State Department of Taxation and Finance have to take notice.

Gaied is a major development in New York's tax law, and it should shift the way statutory residency cases are analyzed in the state. It also raises many questions for current and future cases. One thing is certain: Even with the court's decision in *Gaied*, we're not yet able to put the residency issue to bed (or to couch, as the case may be).[2]

I. The Roots of the Statutory Residency Test

To appreciate the ramifications of the decision, it's important to understand the context and history of New York's statutory residence provision. The adoption of the statutory residence test dates back to 1922. That year, the New York State Legislature enacted a statutory definition of a resident for income tax purposes to include a person "who maintains a permanent place of abode within the state, and spends in the aggregate more than seven months of the taxable year within the state."[3]

The tax department made clear in its memorandum in support of the new law why the measure was necessary: It was an alternative to the highly subjective common law test of domicile, which had governed residency determinations until that point.[4] As the department said, "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."[5] The addition of the abode-plus-seven months test "would do

[1] *See, e.g.,* 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 Villmer, "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] If you don't get this joke, read on.

[3] *See* former N.Y. Tax Law section 350(7). The definition of a resident individual under Tax Law section 605(b)(1)(B) requires maintenance of a permanent place of abode and presence in the state for more than 183 days.

[4] 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).

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

away with a lot of this faking and probably result in a man's conceiving his domicile to be at the place where he really resides," according to the department.[6]

That point was further highlighted in 1954, when the Legislature amended the seven-month test for presence in New York and replaced it with the 183-day rule. In explaining the justification for the proposed change, the department's memorandum in support noted that there had been many cases of tax avoidance, even evasion, and that "persons who really are residents nevertheless manage to comply with the present seven-month rule by spending long weekends, holidays and vacations outside the state."[7]

In 1998 New York's court of appeals referenced that legislative history in *Tamagni v. New York State Tax Appeals Tribunal*, 91 N.Y.2d 530, 535 (1998), *cert. denied*, 525 U.S. 931 (1998), which involved the constitutionality of two states taxing someone as a resident. The court said New York's statutory residence test was enacted to discourage tax evasion by New York residents, adding that the provision "serves the important function of taxing those 'who, while really and [for] all intents and purposes [are] residents of the state, have maintained a voting residence elsewhere and insist on paying taxes to us as nonresidents.'"[8]

Thus, from legislative history, we see that the intent underlying the statutory residency test was to ensure that people who actually resided in New York couldn't escape tax simply by declaring their legal residence and domicile to be elsewhere.

Keep that legislative history in mind. We'll come back to it often, not only because it guided the court of appeals' analysis in *Gaied*, but also because it's the key to understanding the concept of statutory residence.

II. *Matter of Evans* and the Permanence Test

Amazingly, it took almost 70 years after the enactment of the 1922 legislation before any substantive case law emerged construing the meaning of the term "permanent place of abode" (PPA) in the statute. The department had adopted regulations defining an abode as "a dwelling place permanently maintained by the taxpayer,"[9] and the regulations offered some examples of dwellings that would not qualify.[10] But it was not until the New York State Tax Appeals Tribunal's decision in *Matter of Evans v. Tax Appeals Tribunal*, DTA No. 806515 (N.Y. Tax App. Trib. 1992), *confirmed*, 199 A.D.2d 840 (N.Y. App. Div. 3d Dept. 1993), that the term "permanent place of abode" finally received a comprehensive analysis. At that time, the new residency audit program kicked off by the department in the late 1980s was in high gear.

In *Evans*, the tribunal found that a room at a church rectory in New York City where the taxpayer resided for five days each week constituted his PPA in the city, even though he did not own or lease the quarters or make direct monetary contributions to its maintenance. In reaching that determination, the tribunal held that the PPA inquiry involved two questions: (1) whether the taxpayer indeed maintained the abode, and (2) whether the taxpayer's "living arrangements were within the statute's meaning of 'permanent.'"

On the maintenance inquiry, the *Evans* tribunal found that "one maintains an abode by doing whatever is necessary to continue one's living arrangements in a particular dwelling place," including making "contributions to the household, in money or otherwise." On the permanence question, the tribunal framed its analysis as follows:

> In our view, the permanence of a dwelling place for purposes of the personal income tax can depend on a variety of factors and cannot be limited to circumstances which establish a property right in the dwelling place. Permanence in this context must encompass the physical aspects of a dwelling place as well as the individual's relationship to the place.

That "relationship to the place" element seems consistent with the legislative history discussed above, doesn't it? And in *Evans*, the result was that the taxpayer, who spent five days a week residing at a dwelling, keeping clothes there, and using it as a base for his workweek — that is, a person who for all intents and purposes resided in the city during the week — could not escape the tax merely by claiming he didn't really maintain a dwelling or that it wasn't permanent for him.

III. The Next 20 Years: A Retreat From *Evans*?

New York's appellate division affirmed the *Evans* determination, and over the next 20 years, its two-prong test would be cited in virtually every statutory residence case involving the PPA question.

But as the department continued to grow its residency audit program, subjecting thousands of nonresident returns to audit, a trend began to emerge. The wide net cast by the department began entangling not just people who really did

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[6] *Id.*

[7] Mem. of Dept. of Taxation & Finance, 1954 N.Y. Legis. Ann., at 296.

[8] *Id.* (quoting Mem. of Income Tax Bureau, *supra* note 5).

[9] Former 20 NYCRR section 105.20(e). That version of the regulations reference a dwelling "of *a* permanent nature maintained by the taxpayer" rather than a dwelling "permanently maintained" by the taxpayer. 20 NYCRR section 105.20(e). The Tax Appeals Tribunal in *Matter of Knight*, DTA No. 819485 (N.Y. Tax App. Trib. 2006) pointed out that the word "permanent" in the statute modified the term "abode," yet the regulations referred to an abode that is permanently maintained.

[10] Those include "a mere camp or cottage, which is suitable and used only for vacations"; a "barracks or any construction which does

(Footnote continued in next column.)

not contain facilities ordinarily found in a dwelling, such as facilities for cooking, bathing"; and a dwelling maintained by a full-time undergraduate student. *See* 20 NYCRR section 105.20(e).

reside in New York but also those with merely transient, non-abiding connections to a dwelling in New York. That included persons who had a dwelling available but never slept there or used the place during the years in question,[11] maintained a dwelling but did so for someone else's use,[12] occasionally used an apartment maintained by someone else,[13] and rarely used their rural vacation homes.[14] Sometimes the department won those cases; sometimes it lost. More often than not, the cases never saw any administrative or judicial courtroom, instead being settled in difficult audits.

But in many of those cases, it would be difficult to argue that the taxpayers were really residents of New York. Often, the taxpayer's relationship with the purported New York abode was impermanent or transitory in nature. And in many cases, it would be difficult to argue that the taxpayers actually lived in New York. But none of those issues really mattered. Despite the guidance from the legislative history, from the court of appeals in *Tamagni*, and from the tribunal in *Evans*, the tax department took a more mechanical view of the PPA test. And although dozens of rulings and cases emerged over 20 years, they offered no definitive direction on how to interpret when an abode was permanent for purposes of the statutory residency test.

IV. Intersection of *Barker* and *Gaied* in 2010 and 2011

It was the vacation home scenario that finally brought the issue to a head and put the public spotlight on the PPA concept and statutory residence in general. In *Matter of Barker*, DTA No. 822324 (ALJ 2009),[15] a Connecticut resident who commuted to New York City daily for work was found to be a statutory resident of New York because he also owned a cottage on Long Island, where he and his family spent minimal time (11 nights per year on average). In bringing *Barker* to the division of tax appeals, our focus in part was on the legislative history of the statutory residency provisions, asking whether John Barker was really, for all intents and purposes, a resident of New York.

But the legislative history argument never gained much traction in *Barker*. The administrative law judge ruled that the combination of the taxpayer's New York days (almost all of which were connected to his job in New York City) plus the ownership of the vacation home on Long Island was sufficient to hold that he was a resident. Notably, the ALJ held that *Evans* and its "relationship to the place" inquiry were irrelevant to Barker's situation because he and his wife owned the abode and paid its monetary expenses. Hence, the ALJ said that "there is no reason to examine their relationship to the property as there was in *Evans*." The clear import was that once a person had a legal property right in a dwelling, the permanence test was met, regardless of how (or even whether) the taxpayer used the property.

Our firm believed that *Barker* was a significant departure not only from *Evans*, but also from the legislative history. It turns out that *Barker* was just the beginning of the fun.

> ***Barker* was a significant departure from the legislative history and turned out to be just the beginning of the fun.**

Enter *Gaied*. The tax appeals tribunal issued its first decision in *Gaied* in July 2010,[16] while the appeal in *Barker* was before the tribunal. In its initial decision, the tribunal held that Gaied, a New Jersey domiciliary with a business in Staten Island, could not be considered a resident of New York because his sole abode was a three-unit apartment building that he owned and maintained only as a rental property and home for his elderly parents who depended on him for support.

Significantly, the tribunal reached its decision by turning to *Evans* and its test for permanence, even though Gaied indisputably owned and maintained the dwelling. It noted that the department's own regulations "make it clear that the physical attributes of an abode, as well as its use by a taxpayer, are determining factors in defining whether it is considered permanent." It identified the factors that weighed against the property being considered a PPA for Gaied, including that he didn't have a bed or room in the place, he didn't keep any personal effects there, and he stayed overnight (on his parents' couch) only when required because of his parents' needs. As a result of those factors, the tribunal concluded that Gaied "did not have a place to stay in a residence that he maintained for his parents."

That ruling was consistent with the original intent of statutory residency and seemed to be a repudiation of the basis for the ALJ's rationale in *Barker*. But the result was short-lived.

Unhappy with the result and unable to appeal (because Tax Law section 2016 prevents the department from appealing a decision of the tax appeals tribunal), the department took the rare step in late 2010 of filing a motion for reargument. Similar to the arguments it advanced in *Barker*, the department's motion for reargument was based on the notion that once ownership or a property right is established, there is no need to look at any subjective factors regarding the taxpayer's use of or relationship to the abode — not even whether he actually lived in it.

[11] *See Matter of Calvano*, DTA No. 807096 (ALJ 1995).

[12] *See Matter of Boyd*, DTA No. 808599 (N.Y. Tax App. Trib. 1994); and *Matter of Panico*, DTA No. 805810 (ALJ 1990).

[13] *See Matter of Moed*, DTA No. 810997 (N.Y. Tax App. Trib. 1995); and *Knight*, DTA No. 819485.

[14] *See Matter of Barker*, DTA No. 822324 (N.Y. Tax App. Trib. 2011), *aff'd*, DTA No. 822324 (N.Y. Tax App. Trib. 2012); and *Matter of Slavin*, DTA No. 820744 (ALJ 2007).

[15] We also represented Barker in this case.

[16] DTA No. 821727 (N.Y. Tax App. Trib. 2010).

In January 2011, a month before it ruled on the reargument motion, the tribunal issued its decision in the *Barker* appeal — one seemingly at odds with its decision in *Gaied*. The tribunal held in *Barker* that "a dwelling is a permanent place of abode where, as it is here, the residence is objectively suitable for year-round living and the taxpayer maintains dominion and control over the dwelling." It also held that there "is no requirement that the petitioner actually dwell in the abode, but simply that he maintain it."[17]

That mechanical reasoning from *Barker* ultimately carried over into the tribunal's decision on the department's motion for reargument in *Gaied*. First, in February 2011 the tribunal granted the department's motion for reargument to consider the main question whether "the proper legal standards regarding 'maintenance' and 'permanent place of abode' were applied to the facts of that case." And unsurprisingly, with the rationale from its January 2011 decision in *Barker* now out there, the tribunal reversed itself in a 2-1 decision in June 2011.[18] The majority determined that its original decision in *Gaied* had misconstrued the applicable standard and relevance of *Evans*:

> A review of decisions from both prior to and subsequent to our July 8, 2010 decision indicates that when a taxpayer has a property right to the subject premises, it is neither necessary nor appropriate to look beyond the physical aspects of the dwelling place to inquire into the taxpayer's subjective use of the premises.

That statement was consistent with the department's theory in *Barker* and *Gaied* that there "is no requirement that the petitioner actually dwell in the abode [in order for it to be a PPA], but simply that he maintain it."[19] The tribunal even said in a note that a dwelling could be considered a taxpayer's PPA even if it had no bed.

When viewed through the lens of the legislative history, the notion that a mere property right in a habitable dwelling suffices to create a PPA for residency purposes shows just how far things had strayed from the original intent of the 1922 statute. But as the dust settled after the 2011 tribunal rulings in *Gaied* and *Barker*, the connection between the legislative history underlying the statutory residency test and the application of that history in the construction of the law was never more far apart.

V. The Court of Appeals: A Return to the Statute's Intent

Gaied appealed to New York's appellate division, as required for taxpayers unhappy with an adverse tribunal decision. And although the appellate division upheld the tribunal's ruling, it did so in another split decision, which set the stage for an appeal to the court of appeals.[20] The majority's opinion hinted at a somewhat more flexible standard for finding a PPA, but the decision more or less punted on the analysis, noting that the court "was constrained to confirm" the tribunal's second decision in *Gaied* because the finding was supported by substantial facts in the record.[21]

More importantly, however, the dissenting judges acknowledged the application of the legislative history to the proper analysis of the law. That was the first time in a recent statutory residency case that a judge or court acknowledged the argument that the intent of the law should play a role. The dissent recognized that the intent of the law was to "tax those who really and [for] all intents and purposes [were] residents of the state."[22] And using language that would later be adopted by the court of appeals, the dissent asserted that the inquiry should focus on the person's own living arrangements in the purported PPA and on whether the taxpayer himself had a residential interest in the place.

In reversing the appellate division's decision, New York's court of appeals started where the dissent left off. Indeed, one of the focal points during oral argument was on legislative intent, highlighted by an exchange between Judge Eugene F. Pigott Jr. and New York State Assistant Attorney Solicitor Robert M. Goldfarb:

> **Judge Pigott**: Do you agree with Mr. Noonan's statements about what the purpose of this statute is when it was first enacted, and as outlined in *Tamagni*?
>
> **Assistant Attorney Solicitor Robert M. Goldfarb**: Yes, I do, and that's what the court said in *Tamagni*. You're really trying to get people who are residents . . .
>
> **Pigott**: That are living outside the state and you want to make sure that they're paying their New York taxes.
>
> **Goldfarb**: That's right, but the . . .
>
> **Pigott**: Does this appear to you to be the reverse now? Where there are people who are actually living in another state, you know, who are doing things like this, and that's kind of the — it seems to me it's kind of the inverse of what the original intent was.
>
> **Goldfarb**: Well, that's an argument that can be made to the Legislature. This . . .
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> **Pigott**: Why? If that's the intent of the statute and we agree that that's the intent of the statute, why do we

[17] *Barker*, DTA No. 822324 (2011). The cases the tribunal cited — *Matter of Roth*, DTA No. 802212 (N.Y. Tax App. Trib. 1989), *Stranahan v. New York State Tax Commission*, 68 A.D.2d 250 (N.Y. App. Div. 3d Dept. 1979), and *People ex rel. Mackall v. Bates*, 278 A.D. 724 (N.Y. App. Div. 3d Dept. 1951) — all predated *Evans*.

[18] DTA No. 821727 (Tax App. Trib. 2011).

[19] *Barker*, DTA No. 822324 (2011).

[20] *See Gaied v. New York State Tax Appeals Tribunal*, 101 A.D.3d 1492 (N.Y. App. Div. 3d Dept. 2012).

[21] *Id.* at 1494.

[22] *Id.* at 1494-1495, (Malone, Jr., J., dissenting) (*citing Tamagni*, 91 N.Y.2d at 535).

> have to go to the Legislature? We say they did it right, and you're interpreting the law wrong.[23]

That is exactly what happened. The court of appeals decided that the department was interpreting the law incorrectly. On February 18 the court issued its decision, reversing the appellate division and presenting a new standard for determining whether a dwelling constitutes a PPA. To do so, the court did what is required in any case of statutory construction: It sought out the Legislature's intent. And as we had urged for years, the court started its analysis by referring to its decision in *Tamagni* and to the concern voiced by the Legislature in 1922 that "there had been '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.'"[24] Based on that, the court recognized that the purpose of Tax Law section 605(b)(1)(B) was to discourage tax evasion by individuals who are truly residents — that is, people who really live in New York but still attempt to be taxed as nonresidents.

With that as the backdrop, the court found that the department had no rational basis to tax Gaied as a resident of New York, regardless of the time he spent in the state as a result of his business because he didn't reside in New York.[25] It was insufficient that he had a property interest in a dwelling, or that it was suitable for year-round habitation, or that his parents did not prevent him from accessing it. Rather, as the court held, "For an individual to qualify as a statutory resident, there must be some basis to conclude that the dwelling was utilized as the taxpayer's residence."[26]

The court's decision is significant not just because it was issued from the highest court in the state.

And although not cited by the court, that view is consistent with a more recent decision in a pistol permit case, in which the court also described what it means to be a resident of a jurisdiction.[27] The statute at issue in that case limited the filing of a permit application to the county in which the applicant resides. In interpreting that residency requirement, the court acknowledged the difference between domicile and residence, noting that domicile requires residing in a location with the intent to remain there permanently, but that establishing residence "turns on whether [one] has a significant connection with some locality in the State as the result of living there for some length of time during the course of a year."[28] Again, the idea is that to be a resident of a jurisdiction, a person actually has to live there for some period of time.

Whatever the case, the court's repudiation of the analysis set forth by the department, tribunal, and appellate division was based on three critical points. First, that the statute makes it clear that the PPA must actually relate to the taxpayer. Second, that the legislative history supports the idea that the law was intended to prevent tax evasion by New York residents. And third, that those concepts, as well as the department's regulations, support the notion that the taxpayer himself must have a residential interest in the place for it to constitute his PPA.

VI. Where Do We Go From Here?

Evans was the seminal PPA case for the last 20 years, and *Gaied* will now serve as the new standard. But what does *Gaied* mean? How will the residential interest standard set forth by the court be applied in practice? And is that really a big change in New York's residency rules?

We believe it is. The court's decision is significant not just because it was issued from the highest court in the state. If we take seriously the court's requirement that a dwelling must be used as the taxpayer's residence and consider it in light of the legislative history, as the court did, only those taxpayers who really do live in New York in some capacity can be taxed as statutory residents.

That is a major shift from simply examining whether a dwelling is habitable and whether the taxpayer could have used it. It's a change from the argument advanced by the department in *Gaied* that "One need not dwell in the abode, but only maintain it."

It's also a shift from the department's more recent formulation of the PPA test in its 2012 audit guidelines, issued after the tribunal's second ruling in *Gaied*. There, the department defined permanence based on two factors: physical attributes and relationship. And as relevant here, regarding the "relationship" prong, the department listed factors to be considered: ownership, property rights, maintenance (that is, who pays the bills), relationship to co-inhabitants, registration for government services (voting, etc.), personal items, and access.[29]

But if you apply those tests to Gaied, he would lose; most of the factors in the 2012 guidelines would not weigh in his favor. Of course, the court of appeals saw it differently. It applied a completely different test. And Gaied did not lose. So the idea — which has been expressed by department officials in the wake of *Gaied* — that the 2012 audit guidelines continue to set forth the proper PPA test couldn't be more inaccurate. The court's decision makes clear that the

[23] Transcript of Oral Argument in *Gaied*, at 20-21.

[24] *Gaied*, 2014 Slip Op. 1101 at 4, *citing Tamagni*, 91 N.Y.2d at 535 (*quoting* Mem. of Income Tax Bureau, *supra* note 5).

[25] *See Gaied*, 2014 Slip Op. 1101 at 4-5.

[26] *Id.* at 2.

[27] *See Osterweil v. Bartlett,* 21 N.Y.3d 580 (2013).

[28] *Id.* at 582-583

[29] *See* Nonresident Audit Guidelines (2012), at 95; *see also,* Timothy P. Noonan, "New Nonresident Audit Guidelines," *State Tax Notes*, Oct. 15, 2012, p. 197.

tests and standard applied by the department in *Gaied* had no rational basis. Thus, at a minimum, *Gaied* mandates that the tests and standards in the audit guidelines be changed.

> **The lesson from *Gaied* is that the statutory residency test should be applied only to taxpayers who are actually living or residing in New York.**

Gaied mandates that a more subjective inquiry occur before anyone who spends more than 183 days a year in New York can be taxed as a resident simply by virtue of having a dwelling in New York. And that inquiry needs to focus on whether the dwelling is actually "utilized as the taxpayer's residence." That isn't spin or semantics — those are the words used by New York's high court, and we should listen to them. And when we are applying the law, we should also take into account its purpose, as recognized by the court: That it was designed to tax people who really do live in New York. It is not there to tax commuters who don't live in New York, even if they have some connection to real property there.

How that inquiry plays out in specific factual situations will surely be tackled in future cases (and articles). For example, if Gaied had a spare room (that he never used) in his parents' apartment, would he be deemed to be "residing" in the apartment? We think the answer is no. Does a taxpayer who works in New York City but maintains a vacation home in the Hamptons or the Catskills reside in New York? Does a commuter who is trying to sell an apartment that he no longer lives in still reside in New York? What about the commuter with a rarely used apartment in New York? As far as we are concerned, under the new standard set by the court, all of those cases are in play. And in all of them, a compelling argument can be made that the taxpayers would not be subject to the statutory residency test because they are not residing in New York.

Ultimately, the lesson from *Gaied* is that the statutory residency test should be applied only to taxpayers who are actually living or residing in New York. And if that concept is not incorporated in the application of those rules in future statutory residency cases, expect more litigation on the topic.

VII. Conclusion

Anyone who has ever handled a New York residency audit knows that those cases are difficult. They are fact-intensive, and the rules aren't always clear. For its part, the department has done a good job publicizing its positions, for example, with the audit guidelines.

But subjectivity in residency audit cases is a necessary evil. And quite frankly, it probably should be. The determination as to whether a taxpayer is a resident must vary based on the factual circumstances of each case. It can't be based on cookie-cutter or mechanical tests.

In *Gaied*, New York's highest court highlighted that, with the recognition that a taxpayer has to reside in New York to be taxed as a New York resident. That should jump-start a shift in how statutory residency cases are handled. Time will tell whether that comes to pass. ☆