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EDITORS

Hollis L. Hyans
hhyans@mofo.com

Irwin M. Slomka
islomka@mofo.com

NEW YORK STATE + LOCAL TAX GROUP

Craig B. Fields
cfields@mofo.com

Paul H. Frankel
pfrankel@mofo.com

Hollis L. Hyans
hhyans@mofo.com

Mitchell A. Newmark
mnewmark@mofo.com

R. Gregory Roberts
rroberts@mofo.com

Irwin M. Slomka
islomka@mofo.com

Open Weaver Banks
obanks@mofo.com

Amy F. Nogid
anogid@mofo.com

Michael A. Pearl
mpearl@mofo.com

Richard C. Call
rcall@mofo.com

Ted W. Friedman
tfriedman@mofo.com

Nicole L. Johnson
njohnson@mofo.com

Kara M. Kraman
kkraman@mofo.com

William T. Pardue
wpardue@mofo.com

Rebecca M. Ulich
rulich@mofo.com

TAXPAYER WINS AND LOSES IN STATUTORY RESIDENCY CASE

By Kara M. Kraman

In Matter of *David J. and Laurie Knoebel*, DTA No. 824117 (N.Y.S. Div. of Tax App., Sept. 19, 2013), a New York State Administrative Law Judge held that the taxpayers successfully proved they were not present in New York City for more than 183 days during 2006, but failed to prove they were not present in New York *State* for more than 183 days during the same year.

The Knoebels lived in Elysburg, Pennsylvania, where they owned a home. In 2006, they filed a Pennsylvania income tax return, voted in Pennsylvania, had their automobile registered in Pennsylvania, purchased insurance in Pennsylvania and received medical care in Pennsylvania. However, during that time, the Knoebels also maintained and periodically used an apartment located on West 17th Street in Manhattan. The Knoebels also allowed their two daughters, both of whom lived in Brooklyn, to use the West 17th Street apartment without restriction. In addition to spending time in their New York City apartment, the Knoebels visited Utica, New York eight times in 2006 in order to provide assistance to Ms. Knoebel's ailing mother.

New York State and New York City income tax is imposed on "resident individuals." A resident individual refers to someone who is either domiciled in New York, or who falls within the definition of a "statutory resident." Both the Tax Law (State) and the Administrative Code (City) define a "statutory resident" as someone who, while not domiciled in New York, maintains a "permanent place of abode" in the State (or City) and spends in the aggregate more than 183 days a year in the State (or City). The Department did not assert that the Knoebels were New York domiciliaries, and the Knoebels did not dispute that the West 17th Street apartment constituted a "permanent place of abode." The only issue in the case was whether the Knoebels spent enough days in New York City and New York State to be considered statutory residents.

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After hearing the evidence, the ALJ determined that the Knoebels had established by clear and convincing evidence that they were not in New York City on 16 of the 199 days asserted by the Department, putting them below the 184 day threshold. The ALJ relied on the testimony of Mr. Knoebel and one of his daughters, as well as contemporaneous records of telephone calls and credit card charges. Although the ALJ relied on both testimony and documentary evidence in reaching his conclusion, he noted that "credible testimony alone is sufficient to establish whether a day was spent in New York City."

However, for purposes of the New York State day-count, the ALJ refused to exclude the eight days the Knoebels spent in Utica, New York caring for Ms. Knoebel's mother, as urged by the Knoebels. The Knoebels claimed that the decision in *Stranahan v. New York State Tax Commission*, 68 A.D.2d 250 (3d Dep't 1979), which held that days spent in New York for the treatment of a taxpayer's serious illness should be excluded from the day count for statutory residency purposes, permitted them to exclude the days they spent in Utica caring for Ms. Knoebel's mother. The ALJ rejected this approach and declined to expand the holding in *Stranahan* to cover days spent caring for someone in New York who is ill, on the grounds that such an expansion would make practical administration of the rules "impossibly cumbersome."

The ALJ...declined to expand the holding in *Stranahan* to cover days spent caring for someone in New York who is ill, on the grounds that such an expansion would make practical administration of the rules "impossibly cumbersome."

The ALJ also rejected the Knoebels' argument that the days they spent in Utica should be excluded because there was no nexus between Utica and their "permanent place of abode" in New York City, noting that there is no authority for the proposition that there must be a connection between the presence in New York and the permanent place of abode. Accordingly the ALJ found that the Knoebels were properly regarded as statutory residents of New York State, although not of New York City.

Additional Insights

Since *Stranahan* was decided in 1979, taxpayers have frequently sought to extend the holding that "when a non-domiciliary seeks treatment in New York for a serious illness, the time spent in a medical facility for the treatment of that illness should not be counted [for statutory residency purposes]." In *Kern v. Tax Appeals Tribunal*, 240 A.D.2d 969 (3d Dep't 1997), the Appellate Division sustained the Tribunal's rejection of a taxpayer's attempt to exclude days during which the taxpayer was an outpatient visiting doctors in New York, and in *Matter of Dr. Charles F. Brush III & The Estate of Ellen S. Brush*, DTA No. 817204 (N.Y.S. Div. Tax App., April 12, 2001), an ALJ rejected a taxpayer's attempt to exclude days he spent visiting his wife at a New York hospital. Taken together with this case, these rulings demonstrate the hurdles in applying *Stranahan* to exclude any days other than days spent in New York for the taxpayer's own medical confinement due to a serious illness.

GUIDANCE ISSUED ON RECIPROCAL CREDIT FOR SALES OR USE TAX

By Hollis L. Hyans

The New York State Department of Taxation and Finance has issued guidance explaining the reciprocal state and local use tax credit that may be allowed when sales or use tax has been paid to another state or locality. *Tax Bulletin*, TB-ST-765 (N.Y.S. Dep't of Taxation & Fin. Oct. 9, 2013). Such a credit may be available if taxable items or services are purchased outside of New York and then brought into the state, or if taxable items or services are purchased in one local taxing jurisdiction within New York and then brought into another local taxing jurisdiction where the purchaser is a resident.

Sales and Use Tax Credits

New York residents are liable for the New York State use tax on all items for which New York tax was not paid at the time of purchase, if they were residents at the time of purchase. The term "resident" is defined differently for sales tax purposes than it is for personal income tax, and includes, for example, an individual with a permanent place of abode, even if not in the state more than 183 days; a student attending college in New York; and a member of the military stationed in New York. The term "resident" also includes a person carrying on any employment, trade, business or profession in New York.

A resident purchaser is required to pay New York State's 4% sales tax plus an additional 3/8% tax imposed in the Metropolitan Commuter Transportation District, if applicable, plus any local tax. This tax can be paid on a personal income tax return using a sales and use tax chart based on the resident's income. For purchases of taxable property or services costing $1,000 or more, a resident must use the "exact calculation method," which requires payment of the actual tax that would be due on the purchase.

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Available credits

When a resident purchaser has paid a sales or use tax at the place of purchase, a credit may be available, but only if certain requirements are met: the other state must allow a corresponding credit; the purchaser had to have been legally liable for a sales or use tax in the other state; there must be no right to a refund in the other state; and the purchaser must have proof of payment. Federal excise taxes, customs duties and taxes or fees paid in foreign countries are not allowed as credits.

While many New York residents are aware that they may owe sales tax on items purchased from remote vendors who do not collect sales tax at the time of purchase, not many residents may have focused on the duty to pay use tax on items purchased outside the state or outside their localities.

Where the other state allows a reciprocal credit for both New York State tax and local tax, the reciprocal credit is the sum of the other state's state and local taxes. If the amount of tax paid to the other state exceeds the amount due in New York, no New York tax is due. If the amount of New York State and local tax exceeds the amount paid in the other state, the excess must be paid. If the other state allows a reciprocal credit for only New York State sales tax, or only for local tax, then credits are allowed only for those amounts.

Alternative basis for computing tax on certain property

If the item purchased outside New York, or outside the locality of residence, was used for more than six months prior to the item being brought into New York, the amount subject to tax is the lesser of the purchase price or the fair market value at the time brought into New York. If the item is tangible personal property to be used in the performance of a contract for a period of less than six months, the amount subject to tax may, at the election of the user, be based on the fair rental value of the property for the period of use, but only if the property is not completely consumed or incorporated into real property in New York.

Additional Insights

While many New York residents are aware that they may owe sales tax on items purchased from remote vendors who do not collect sales tax at the time of purchase, not many residents may have focused on the duty to pay use tax on items purchased outside the state or outside their localities. The safest way for individuals to protect themselves against potential problems, if they purchase items outside the state or locality of residence, is to pay sales tax in conjunction with filing their personal income tax returns and to use the standard chart to estimate the tax due, as long as items purchased outside the state do not cost $1,000 or more, in which case the exact tax due has to be reported.

STATE TAX DEPARTMENT ISSUES GUIDANCE ON START-UP NY PROGRAM

By Irwin M. Slomka

Earlier this year, legislation was signed into law creating the "SUNY Tax-Free Areas to Revitalize and Transform Upstate New York" program (the "START-UP NY Program"). Ch. 68, Laws of 2013 (Part A). Its purpose is to provide broad-based New York State and local tax benefits to approved businesses that locate in vacant space or land of approved New York State and City public and private colleges and universities, and to employees of those businesses. The New York State Department of Taxation and Finance has now released a technical memorandum to provide guidance regarding the tax benefits under that program. "SUNY Tax-Free Areas to Revitalize and Transform New York Program," TSB-M-13(7)C, *et al.* (N.Y.S. Dep't of Taxation & Fin., Oct. 22, 2013).

A detailed discussion of the 17-page technical memorandum is beyond the scope of this article. However, businesses and practitioners should be aware of the substantial — and in some ways unprecedented — tax benefits that the START-UP NY program provides.

Who is eligible?

Both corporations subject to Article 9-A, and individuals subject to Article 22 (personal income tax) that operate businesses as sole proprietorships, partnerships, LLCs or S corporations, are "eligible taxpayers" if four conditions are met: (i) the business is approved to participate in the START-UP NY Program by Empire State Development; (ii) the business operates in a "tax-free NY area" at an approved location (generally, in vacant space or land of approved New York State and City colleges and universities); (iii) it annually creates "net new jobs" ; and (iv) it meets an annual "employment test."

What is a tax-free NY area?

Generally, a tax-free-NY area is property or land affiliated with public or private colleges and universities, on or near academic campuses throughout New York State. Approved businesses will be issued a certificate of eligibility by the sponsoring campus, university or college.

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What are the tax benefits?

Eligible taxpayers qualify for New York tax benefits available to the business and certain employees of the business for tax periods or transactions after December 31, 2013. The list of potential tax benefits is considerable:

- Tax benefits available for *10 consecutive years* beginning with the year the business locates in the tax-free NY area.
- A tax credit eliminating *corporate entity-level taxes* (Article 9-A) and personal income taxes (Article 22) for income earned in the tax-free NY area.
- Exemption from the State *organization tax* (Tax Law §180) or the State *license or maintenance fee* (Tax Law § 181) for businesses located exclusively in the tax-free area.
- Exemption from State or local *real property transfer taxes* on leases of real property located in the tax-free area.
- Certain exemptions from *real property taxes*.
- A *wages* exclusion *for eligible employees* for New York State, New York City and Yonkers personal income tax purposes, and an available withholding exemption.

Tax benefits available for *40 consecutive calendar quarters* beginning with the quarter the business locates in the tax-free NY area:

- Exemption from the *Metropolitan Commuter Transportation Mobility Tax* on payroll expense and on net earnings from self-employment for approved businesses.

Tax benefits available for *120 consecutive months* beginning with the month the business locates in the tax-free NY area:

- A credit or refund of State and local *sales taxes* imposed on sales of tangible personal property, utility services and certain other services. An approved business that makes sales subject to sales and use tax must still register as a sales tax vendor and collect and remit sales tax on its sales.

The technical memorandum also provides guidance on such things as the calculation of the employment test based on "new net jobs" and the tax-elimination credit under Article 9-A and Article 22, as well as the possible recapture of tax benefits for businesses that fail to meet performance benchmarks.

Additional Insights

Although it is somewhat limited regarding the types of businesses and locations that will qualify under the program, the START-UP NY program is unprecedented as to the scope and duration of the potential tax benefits. The Department's technical memorandum principally addresses the tax benefits under the program. It does not, however, provide detailed guidance regarding the types of businesses that are eligible. Nor does it discuss the statutory requirement that the eligible business "support the academic mission of the college or university." For information regarding eligibility under the program, the State of New York has established a website: http://startup-ny.com.

INSIGHTS IN BRIEF

Roberta Mosely Nero Appointed President of the Tax Appeals Tribunal

Governor Cuomo has designated Roberta Moseley Nero to serve as President of the Tax Appeals Tribunal, effective October 8, 2013. She became a Commissioner of the Tribunal after being confirmed by the New York State Senate this past June. Former President James H. Tully, Jr. will remain as a Tribunal Commissioner, along with Commissioner Charles H. Nesbitt.

Non-Resident's Long-Term Disability Benefits Treated as New York Source Income

The Department has ruled that a New Jersey resident employed in New York City from 2008 through 2010 who, after suffering a stroke, received long-term disability benefits under a noncontributory disability insurance policy, must treat the benefits as New York source income for State personal income tax purposes if the benefits are included in his federal adjusted gross income. *Advisory Opinion*, TSB-A-13(9)I (N.Y.S. Dep't of Taxation & Fin., Sept. 10, 2013). The Department ruled that the individual's disability benefits would be considered New York source income, if includable in federal AGI, because they are considered compensation for services performed in New York in a prior year. The Department noted that such disability benefits paid pursuant to a noncontributory insurance policy are not generally includable in federal AGI, unless attributable to employer contributions that were not includible in the employee's gross income or were paid by the employer.

Online-Only Financial Publication Exempt from Sales Tax

An online-only financial publication published 20 times each year and containing articles regarding investing strategies is exempt from sales and use tax as an "electronic periodical" under Tax Law § 1115(gg)(2). *Advisory Opinion*, TSB-A-13(33)S (N.Y.S. Dep't of Taxation & Fin., Sept. 10, 2013). The Department concluded that the publication met the statutory criteria for exemption, finding that its predominant purpose was the delivery of news content, and it was not a listing, catalog, database or compilation. Therefore, sales tax was not required to be collected from subscribers.

Bone Graft Products Ruled Exempt from Sales Tax as Products Consumed for the "Preservation of Health."

Newly developed drug-device bone graft products are not exempt from sales and use tax as "prosthetic aids," but do

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qualify for the "preservation of health" exemption under Tax Law § 1115(a)(3). *Advisory Opinion*, TSB-A-13(26)S (N.Y.S. Dep't of Taxation & Fin., Sept. 9, 2013). The products are not prosthetic aids because they speed bone regeneration after surgery, rather than replace a permanently malfunctioning body part. However, they qualify for the "preservation of health exemption" because they are used in connection with orthopedic surgery to promote bone regeneration and healing after surgery. Several identified Advisory Opinions to the contrary were expressly overruled.

Guidance Provided on Sales Tax "Co-Vendor" Agreements

The Department of Taxation and Finance has issued guidance on "co-vendor" agreements for the collection and reporting of New York State sales tax, where a manufacturer or wholesaler uses an independent distributor to sell its products in the State. *Tax Bulletin*, TB-ST-142 (N.Y.S. Dep't of Taxation & Fin., Oct. 9, 2013). Suppliers that make sales of products through independent distributors sometimes want to register as a sales tax "vendor" to insure that the State sales tax is paid, even though the supplier does not actually make the retail sales. The supplier then collects the sales tax from the distributor. The *Tax Bulletin* describes the procedure for entering into the co-vendor agreement with the Department, and the necessary recordkeeping requirements. The *Tax Bulletin* makes clear that the supplier and the independent distributor remain jointly liable for the sales tax.

New York State "Tax Relief Commission" Formed

On October 2, 2013, Governor Cuomo announced the formation of an eight-member Tax Relief Commission, led by former Governor George Pataki and former State Comptroller Carl McCall, to find ways to reduce New York's property and business taxes. The Commission's recommendations are due by December 6th, so that they can be included in the Governor's 2014 State of the State address. The Tax Relief Commission is to collaborate with the Tax Reform and Fairness Commission, formed in December 2012 to conduct a comprehensive review of corporate, sales and personal income taxation, and to make recommendations to improve and simplify the current tax system. *Governor Cuomo Launches Tax Relief Commission to Identify Ways to Reduce Tax Burdens on New York's Families and Businesses* (Press Release from the office of Governor Cuomo, Oct. 2, 2013).

Supreme Court Review Denied in Strip Club Sales Tax Case

On October 15, 2013 the United States Supreme Court denied review of the decision by New York's highest court in *Matter of 677 New Loudon Corp. v. State of New York Tax Appeals Tribunal*, 19 N.Y.3d 1058 (2012), *cert. denied*, No. 13-38 (Oct. 15, 2013). The Court of Appeals had held that general admission charges and charges for admission to private performance rooms at a strip club were subject to sales tax as admission charges to places of amusement, and affirmed the decisions below that the taxpayer had not established the charges were nontaxable as charges for musical arts performances or choreographed performances. Three judges, including the chief judge, had dissented, concluding that there was "not the slightest doubt" that the charges in question were for dance performances, and that the majority's decision simply found the performances not sufficiently "'cultural and artistic,'" thereby engaging in discrimination based on content, unconstitutional under the First Amendment.

Certain Sales Made by an Elementary School PTA Are Tax Exempt

In an Advisory Opinion, the Department of Taxation and Finance has determined that an elementary school PTA, granted exempt organization status by both the Internal Revenue Service and the Department as a not-for-profit organization, is required to collect sales tax on retail sales of tangible personal property from a "shop or store" it operates. *Advisory Opinion* TSB-A-13(29)S (N.Y.S. Dep't of Taxation & Fin., Sept. 9, 2013). Most of the PTA's sales would be subject to sales tax, including sales of school supplies, sales made at or below cost, and sales on which the PTA paid sales tax on its own purchase of the items. However, if the PTA sold items only four or five times during the school year on no particular schedule, its sales would not be considered to have been made from a shop or store, since they would be "sporadic and infrequent" and thus exempt, but only due to the PTA's exempt status, since New York State does not have a general exclusion from sales tax for occasional sales.

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