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GOVERNOR CUOMO RELEASES 2015-16 EXECUTIVE BUDGET, INCLUDING NEW YORK CITY CORPORATE TAX REFORM

As we went to press, New York State Governor Andrew M. Cuomo released the 2015-2016 Executive Budget. The proposed budget includes a variety of tax proposals, including: (i) expanding sales tax collection for "marketplace providers" (Part X); (ii) closing certain "sales and use tax avoidance strategies" (Part Y); (iii) requiring transportation, utility, and telecommunications companies subject to Article 9 to first refund overpaid taxes to customers in order to obtain a refund or credit of overpaid taxes (Part Q); (iv) technical changes to the 2014 New York State corporate tax reform legislation (Part T); and (v) creating a professional and business license tax clearance procedure requiring that past-due tax liabilities be satisfied in order to receive or renew professional or business licenses (Part JJ).

The Executive Budget also includes a New York City corporate tax reform proposal, retroactive to tax years beginning on or after January 1, 2015, which would generally (but not entirely) conform to last year's New York State corporate tax reform legislation (Part QQ).

More details on the Executive Budget will follow in future issues of *New York Tax Insights*. The deadline for enactment of the budget is April 1, 2015.

NEW COMMISSIONER OF TAXATION AND FINANCE

On January 12, 2015, Governor Cuomo announced the appointment of Kenneth Adams as the new Commissioner of the New York State Department of Taxation and Finance. Mr. Adams has been the Commissioner of the New York State Department of Economic Development since 2011, and before that was the President and CEO of The Business Council of New York State from 2006 to 2011. Prior to that, Mr. Adams was President of the Brooklyn Chamber of Commerce and Director of the MetroTech Business Improvement District, and was the founding Executive Director of New York Cares.

Outgoing Commissioner Thomas Mattox, who was appointed in January 2011, served throughout Governor Cuomo's entire first term in office,

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and had recently overseen the enactment of legislation completely reforming New York's corporate tax system for years beginning on or after January 1, 2015.

ALJ HOLDS THAT HUSBAND CHANGED HIS DOMICILE TO LONDON

By Irwin M. Slomka

In a potentially significant decision involving changes of domicile for personal income tax purposes, a New York State Administrative Law Judge has concluded that a husband successfully established that he changed his domicile from New York to London even though his family never permanently relocated with him. *Matter of Irenee D. May*, DTA No. 825173 (N.Y.S. Div. of Tax App., Jan. 8, 2015). In reaching his decision, the ALJ rejected the Department's claim that proving a change to a foreign domicile requires a greater showing than proving a change of domicile to anther state.

Facts. As in most domicile cases, the decision contains a very detailed recitation of the facts, which will only be summarized here. In 1992, Mr. May and his wife moved to New York, purchasing a home in Harrison, New York, where they raised their son and daughter. The following year, he began working for JP Morgan in New York City, managing and developing its hedge fund business.

In late 2004, Mr. May was terminated by JP Morgan (by then known as JPMorgan Chase), effective January 2005.

The ALJ rejected the Department's assertion that establishing a change to a foreign domicile requires a greater showing than establishing a change of domicile to another state.

Within a few months, he obtained a position as Managing Director at the Royal Bank of Scotland in London, England. Mr. May and his wife made plans to find a home in London and to find a suitable school for their school-age children. He (and his wife and their nanny) obtained five-year work permit visas, after which he could apply for permanent residency in the UK.

In September 2005, Mr. May moved to London and began work at Royal Bank of Scotland under an "at will" employment contract. He and his wife found a large rental home in London, initially for a one-year term but with the goal of eventually purchasing a home there. Due to problems in finding a suitable school in London for their son, his wife and children soon returned to their Harrison, New York home. Their daughter did live with Mr. May in London for several months and attended school there, but by the Spring of 2006, she returned to Harrison to live with her mother and brother.

Mr. May did not list their Harrison home for sale due to the uncertainties of the timing of his family's move to London. By late 2006, the delay in his family's move caused him to move to a smaller rental home in London, again without his family. During the years 2006 and 2007, Mr. May's professional life flourished in London, as did his social life, which was tied to his work.

At the same time, Mr. May's marriage was deteriorating, with Mrs. May remaining in Harrison with their two children. In October 2007, Mrs. May served her husband with divorce papers. Claiming abandonment, the divorce papers recited that Mr. May "repeatedly stated his intention not to return to New York and reside with [his family there]." The following month, Mrs. May obtained sole and exclusive use of their Harrison home by stipulation and eventual court decree. Mr. May remained in London throughout the years 2006 through 2008. Their divorce was finalized in 2011.

For the years 2006, 2007, and 2008, Mr. May filed New York State income tax returns separate from his wife as a nonresident. He maintained that he had changed his domicile to London. The Department claimed that Mr. May remained a New York domiciliary, assessing income tax against him as a resident, plus interest and penalties.

Decision. The ALJ held that Mr. May had established a change in domicile to London, considering the criteria previously employed by the Tribunal, which involved: (i) retention of the place of abode in the former domicile; (ii) location of business activity; (iii) family ties; (iv) social and community ties; and (v) formal declarations of domicile. The ALJ noted that both Mr. May and his now-former wife testified credibly and unequivocally at the hearing regarding his intention to make London his and his family's new and permanent home, testimony that the ALJ considered "extremely potent evidence" of Mr. May's change in domicile.

Under the income tax regulations and New York case law, an individual's domicile continues until a new one is established, and the party alleging the change — whether the taxpayer or the Department — bears the burden of proving a change of domicile by clear and convincing evidence. 20 NYCRR 105.20(b); *Matter of Bodfish v. Gallman*, 50 A.D. 2d 457 (1976).

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The ALJ distinguished decisions involving taxpayers who accepted temporary work assignments outside the country, where claimed changes in domicile were rejected. The ALJ also emphasized that Mr. May spent far more time in London than in New York: between 236 and 280 days in London each year, but only between 25 and 40 days in New York.

The Department claimed that 20 NYCRR 105.20(d)(3), which provides that "a United States citizen will not ordinarily be deemed to have changed such citizen's domicile by going to a foreign country unless it is clearly shown that such citizen intends to remain there permanently," creates a "stronger than general" regulatory presumption against a change in domicile. The ALJ rejected the Department's assertion that establishing a change to a foreign domicile requires a greater showing than establishing a change of domicile to another state. According to the ALJ, the regulation cited by the Department "simply provides the same standard as required for those claiming interstate, and not international changes of domicile."

Additional Insights

The decision, although not binding precedent and subject to appeal, is noteworthy in its rejection of the Department's frequently advanced position that establishing a change of domicile to a foreign country is more difficult than to another state. The Department's position may stem from a misinterpretation of case law involving individuals on temporary work assignments outside the United States who unsuccessfully claimed to have changed their domiciles from New York. The decisions rejecting domicile changes under those circumstances were based on the temporary nature of the individual's presence outside the country, however, not merely because the individual was claiming a foreign domicile.

REIMBURSEMENTS RECEIVED FOR "LOYALTY CARD" PROGRAM ARE INCLUDABLE IN RECEIPTS FOR SALES TAX PURPOSES

By Kara M. Kraman

A New York State Administrative Law Judge has held that a gas station operator that provided discounts to customers pursuant to its participation in a fuel discount program was required to include the amounts it received as reimbursement for its participation in that program in its taxable receipts for sales tax purposes. *Matter of GRJH, Inc.*, DTA No. 825192 (N.Y.S. Div. of Tax App., Jan. 15, 2015).

Facts. GRJH, Inc. (the "gas station operator") operated several Sunoco gasoline stations in New York State. All of its gas stations participated in the Price Chopper Fuel Advantage Program ("Program"). Under that fuel discount program, a customer earned points by purchasing items at a Price Chopper grocery store. The customer could then use those points to receive a 10-cents-per-gallon discount on the price of gasoline at Sunoco stations.

Within two days of making a discounted sale to a customer, the gas station operator was reimbursed by its Sunoco gasoline distributor for the discounts it gave to program participants. The reimbursement was in the form of a credit against the gas station operator's purchase of gasoline from the distributor.

The gas station operator reported and paid sales tax on its sales of gasoline based on the actual selling price of gasoline at the pumps. In cases where the customer received a discounted price through the fuel discount program, the gas station operator only reported and paid sales tax on the discounted price. The gas station operator did not report or pay sales tax on the reimbursement credits it received from the Sunoco distributor.

The Department audited the gas station operator's sales and use tax returns for the period June 1, 2005 through February 28, 2010. The Department determined that the operator should have included the undiscounted prices for gasoline in its taxable receipts, and assessed additional sales tax. At issue was whether taxable receipts included the distributor credits reimbursing the operator for the customer discounts.

Tax Law § 1105(a) imposes sales tax on the "receipts" from every retail sale of tangible personal property. "Receipts" are defined as "[t]he amount of the sale price of any property . . . whether received in money or otherwise, including any amount for which credit is allowed by the vendor to the purchaser, without any deduction for expenses . . . ." Tax Law § 1101(b)(3). The New York State sales tax regulations provide that, where a "manufacturer" issues a "coupon" entitling a customer to a discount on the item purchased and later reimburses the seller, sales tax is due on the amount paid plus the amount of the coupon credit. 20 NYCRR § 526.5. The same regulation also states that reimbursement from the manufacturer includes reimbursement in any form, including credits against purchases.

The gas station operator argued that it properly reported and paid the sales tax based on the actual discounted selling price at the pumps, and properly excluded from

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its calculation of receipts the credit reimbursements it received from the Sunoco distributor. The gas station operator pointed out that the credit reimbursement amounts — provided by the gasoline distributor as a credit against gas purchases by the operator — were properly accounted for as a reduction in its cost of goods sold. The Department argued that the fuel discount program was analogous to a manufacturer's coupon and that, therefore, the gas station operator's receipts for sales tax purposes consisted of the actual amounts paid by customers, plus the amounts the gas station operator received in credits for the discounts (i.e., the undiscounted price per gallon).

[T]he method under which the fuel discount program provided a discount, through use of a so-called store "loyalty card," was essentially "an ongoing or reusable coupon," and therefore "fits squarely" within the definition of a taxable "receipt."

Decision. The ALJ upheld the Department's assessment, and found that the Department's analogy of the fuel discount program to a manufacturer's coupon was an apt one. The ALJ explained that the method under which the fuel discount program provided a discount, through use of a so-called store "loyalty card," was essentially "an ongoing or reusable coupon," and therefore "fits squarely" within the definition of a taxable "receipt." The ALJ was not convinced by the gas station operator's argument that it was not a manufacturer's coupon because there was no actual "coupon" or "manufacturer," finding that such an approach elevated form over substance.

Additional Insights

The ALJ's conclusion is consistent with the Department's Tax Bulletin ST-145 (TB-ST-145, Sept. 29, 2011) and with the taxability of manufacturers' discounts in general. When a manufacturer's discount applies, sales tax is due on the full price of the item, not on the discounted price. This is because the seller receives the full price of the item when the seller is reimbursed by the manufacturer, although the customer pays only the discounted price. In this case, although the reimbursement to the gas station operator was in the form of a credit against its gasoline purchases rather than in the form of a direct payment, the ALJ found that the form of reimbursement did not impact the treatment of the reimbursement for sales tax purposes.

ALJ UPHOLDS DENIAL OF BROWNFIELD CREDIT

By Hollis L. Hyans

A New York State Administrative Law Judge has upheld the denial by the Department of Taxation and Finance of the site preparation credit component of a brownfield redevelopment tax credit because the taxpayer expensed the costs for federal income tax purposes. *Matter of Coltec Industries, Inc.*, DTA No. 825211 (N.Y.S. Div. of Tax App., Dec. 31, 2014).

Facts. Coltec was the sole member of an LLC that manufactures industrial seals and sealing components. The LLC had entered into a Brownfield Site Cleanup Agreement for remediation of a brownfield site, known as the Gylon site, located in Palmyra, New York. In December 2008 the LLC received a Certificate of Compliance for completing the remedial program at the Gylon site. Coltec then claimed a brownfield redevelopment tax credit for costs that the LLC incurred as part of its remediation of the Gylon site.

Background. In 2003, the New York State Legislature enacted a Brownfield Cleanup Program ("BCP"), to encourage the cleanup and decontamination of sites known as brownfields, which were defined broadly as properties that were or might be contaminated by hazardous waste, pollutants, or other contaminants. ECL 27-1405(2). The BCP provided a redevelopment tax credit, ranging from 10% to 22% of covered costs, as a financial incentive to clean up the sites. The tax credit has three components: (i) a site preparation credit component, for costs incurred to prepare the site for cleanup and redevelopment, excluding the cost of acquisition of the property; (ii) a tangible property credit component, for the costs of erecting buildings; and (iii) an on-site groundwater remediation credit component. Tax Law §§ 21(a) and (b).

Site preparation costs are defined as "all amounts properly chargeable to a capital account . . . paid or incurred in connection with a site's qualification for a certificate of completion . . . and all other site preparation costs . . . incurred in . . . preparing a site for the erection of a building or a component of a building . . . " Tax Law § 21(b)(2).

Issue. On its New York State return for 2008, Coltec claimed a total of $2.7 million in brownfield redevelopment tax credits. The dispute concerned only the site preparation credit component, of approximately $800,000. On its federal tax return, Coltec had deducted the site preparation costs on line 26 (other deductions), in accordance with Internal Revenue Code § 198 as then in effect. On audit, the Department denied the site preparation credit, arguing

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that costs expensed under IRC § 198 are, by definition, not chargeable to a capital account as required by Tax Law § 21(b)(2), and arguing that because Coltec had elected to deduct the site preparation costs at the federal level, the expenditures were disqualified from being chargeable to a capital account. Coltec argued that the term "properly chargeable to a capital account" requires only that the costs relate to the acquisition improvement or construction of a capital asset, which are all costs that are capital in nature.

[t]he Department denied the site preparation credit . . . arguing that because Coltec had elected to deduct the site preparation costs at the federal level, the expenditures were disqualified from being chargeable to a capital account.

Decision. The ALJ found that, because a tax credit was involved, the taxpayer has a burden to show that its interpretation of the statute is the only reasonable one, and that Coltec failed to meet this burden. While the brownfield credit was designed to provide an incentive to clean up hazardous sites and to offset a taxpayer's costs relating to that cleanup, the ALJ agreed with the Department that the credit was not intended to provide a double benefit that would result from allowing Coltec to treat the costs as deductible expenses and also claim a credit for the same costs.

The ALJ also looked to the treatment of other credits, such as the investment tax credit and the empire zone investment credit, which require that the qualified property be depreciable under IRC § 167. Tax Law § 210(12)(b)(i). If a taxpayer elects to expense the cost of an asset under IRC § 179, that cost is not eligible for the investment tax credit or the empire zone investment credit. Since the tangible property credit component of the brownfield redevelopment credit contains the same "depreciable" requirement, the ALJ found that the site preparation credit component of the brownfield cleanup credit should be treated the same, and that costs that had been expensed were not "properly chargeable to a capital account" and thus not eligible for the credit.

Additional Insights

Coltec had reduced its federal taxable income by claiming a deduction for the site preparation expenses, and there is no indication in the decision that Coltec had added back or otherwise not claimed that deduction in computing its New York State entire net income. Therefore, the ALJ found that allowing a credit for those same site preparation expenses would amount to a double benefit, and that such a benefit had not been contemplated by the Legislature in granting brownfield credits. However, it is not clear how this situation should best be remedied by a taxpayer, since the decision notes that the federal deduction was claimed in accordance with the IRC, and the brownfield credit legislation does not mandate that a taxpayer add back to income any deductions claimed for federal purposes.

INSIGHTS IN BRIEF

ALJ Grants Innocent Spouse Relief

A New York State Administrative Law Judge has granted innocent spouse relief under Tax Law § 654 to a wife whose husband pled guilty to filing false New York State and City corporation franchise tax returns understating income from restaurants he owned, and also admitted deliberately failing to remit sales taxes collected at those restaurants. *Matter of Vishni Schiro Withanachchi*, DTA No. 825394 (N.Y.S. Div. of Tax App., Dec. 18, 2014). Although Mrs. Withanachchi signed the personal income tax returns in question, the ALJ found that even a careful review of the returns would not have revealed the fraud, that she had no reason to know of the understatement of income from her husband's business, and that there were no unusual or lavish expenditures during the audit years that could have put her on notice of the hidden income. The ALJ also noted that both spouses, although U.S. citizens, were born in Sri Lanka, where the culture defined the male role as handling all financial matters, and that liability for the taxes would create even more difficulties for a family already facing severe economic hardship.

ALJ Denies Tax Department Motion to Dismiss Taxpayer's Petition Challenging Driver's License Revocation

A New York State Administrative Law Judge has issued an Order rejecting the State Tax Department's motion to dismiss a taxpayer's Petition, or alternatively granting summary determination, regarding a notice of proposed driver license suspension due to unpaid tax liabilities of $10,000 or more. *Matter of Miriam Snyder*, DTA No. 826108 (N.Y.S. Div. of Tax App., Jan. 8, 2015). The ALJ concluded that there was no evidence that the required 60-day notice of intent to make a referral to the Department of Motor Vehicles for license suspension could be verified. In addition, the ALJ found that the Department had not yet shown that there existed fixed tax liabilities for which the taxpayer no longer had any right to administrative or judicial review, another predicate for license suspension. The ALJ ordered that the Petition proceed to a hearing in due course.

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