

# 2022-2023 NY Tax Update

## NYS Budget, Other Legislation, and New Enforcement Strategies

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## Topics Discussed

1. 2022-2023 Budget and Other Legislation
2. New Resident and Nonresident Allocation  
Audits/Telecommuting
3. Sales Tax Hot Topics
4. NYS Abandoned Property

## Section 1: New Legislation

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## What's In

- Expanded Appeal Rights
- Business Income Tax Rate Extensions
- Enhanced False Claim Options
- PTET Updates
- MCTMT Updates
- Modified Tax Credits

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## What's Out

- PIT Tax Rate Increases
- Mandatory NYS S Elections
- New Taxes on Digital Products

## Tax Appeals Tribunal Appeal Rights

- Taxpayers have always had the right to appeal adverse Tribunal decisions; but until now, the Tax Department was not permitted appeal rights.
- The Budget allows the Tax Department to appeal Tax Appeals Tribunal decisions to the Appellate Division of the Supreme Court, Third Department.
- For the Department to appeal a decision, the review must be “premised on interpretation of the state or federal constitution, international law, federal law, the law of other states, or other legal matters that are beyond the purview of the state legislature.” What does this mean?
- Pause on accrual of interest and penalty.
- What is the standard of review?

## Business Income Tax Rate Extension

- The Budget extends through tax year 2026 the temporary 7.25% business income tax rate, for corporate taxpayers with business income bases in excess of \$5 million, and the temporary 0.1875% capital base tax rate.
- The income tax rate increase and the capital base tax were scheduled to sunset at the end of 2023.

## False Claims Act

- The Budget amends the New York False Claims Act (the “NYFCA”) to permit actions in cases where the taxpayer is alleged to have “knowingly concealed or knowingly and improperly avoided an obligation to pay taxes to the state or local government.”
- The expansion of the NYFCA takes effect immediately and in “any pending case” applies to any tax obligations knowingly concealed or knowingly avoided on or after the effective date.
- For actions filed after the effective date, this act only applies to such tax obligations knowingly concealed or avoided on or after May 1, 2020.
- Intended to close a perceived loophole that arguably avoided whistleblower complaints when no tax return was filed by the taxpayer and there was thus no “false statement” by the taxpayer upon which a whistleblower complaint might be premised.
- Big, new universe of potential non-filers!

## Pass-Through Entity Tax

- The Budget amends the State Pass-Through Entity Tax (PTET) and the City PTET. The definitions of “pass-through entity taxable income” and “city pass-through entity taxable income” in Tax Law §§ 860(h) and 867(b) are amended to require entities to exclude deductions for PTET taxes paid when computing their state and city pass-through entity taxable incomes.
- This change corrects an unintended “circular” mathematical computation requiring entities to deduct PTET taxes from their pass-through entity taxable income that forms the basis for the PTET tax being deducted.
- In addition, the Budget amends the definition of “city taxpayer” to correct the unintentional omission of city resident trusts and estates from participating in the NYC PTET.
- The Budget also clarifies when an entity must elect into/revoke their election into the PTET and NYC PTET. Participation elections must be made “on or before” the due date of the first estimated payment and “after” such due date elections are irrevocable.

## MTA Mobility Tax Applicability

- The MCTMT has been a tax imposed on certain employers and self-employed individuals engaging in business within the MCTD.
- Prior to the Budget, the MCTMT applied to employers paying wages to employees working in the MCTD and to self-employed individuals (including non-limited partners) with net earnings from self-employment within the MCTD that exceed \$50,000.
- The Budget amends the definition of “net earnings from self-employment” in the Tax Law so that **limited partners who are actively engaged in the operations of their partnerships** are now deemed to have net earnings from self-employment subject to the MCTMT.
- Decouples from the Internal Revenue Code (“IRC”) definition, which excludes amounts earned by limited partners.
- This change takes effect immediately.
- See new MCTMT Publication 420 recently issued by the Tax Department.
- Retroactive application?

## MTA Mobility Tax Rate

- A Budget-related enactment (2023 NY Laws Ch. 58, Part Q) increased the top MCTMT rate from 0.34% to 0.60% for employers with quarterly payrolls over \$437,500 in the counties of Bronx, Kings, New York, Queens, and Richmond (effective July 1, 2023).
- For taxpayers with MCTD-source earnings from self-employment, the MCTMT rate increased from 0.34% to 0.47% in the 2023 tax year (effective July 1), and to 0.60% for the 2024 tax year, for MCTD income attributable to the counties of Bronx, Kings, New York, Queens, and Richmond.
- So, now there are different rates of tax depending on where in the MCTD your business is located.
- For self-employed individuals that have multiple offices with one in, for example, Manhattan and another within White Plains, the calculation may be complicated.

## MTA Corporate Tax Surcharge

- The Budget establishes the rate of the Metropolitan Transportation Authority (“MTA”) surcharge on corporate franchise tax liability at 30% of the state tax paid on income corporations earn within the metropolitan commuter transportation district (the “MCTD”).

## Credits

- The Budget offers substantial modifications to various New York tax credits:
  - Extends the New York City Musical and Theatrical Production Tax Credit, allowing it to be claimed through tax year 2025, and establishes a \$350,000 maximum credit amount for each “qualified New York city musical and theatrical production in a level two qualified New York city production facility.”
  - Amends the Film Production Tax Credit, primarily by increasing the credit rate to 30 percent, increasing the annual credit cap to \$700 million, extending the program’s duration to 2034, and allowing an additional credit for non-wage production costs.
  - Amends the Investment Tax Credit to make it refundable for eligible farmers, through tax year 2027.
  - Expands the period in which the Brownfield Tax Credit can be claimed for certain projects, based on the location of the project and when the taxpayer purchased the project site.

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## Credits (continued)

- The Budget offers substantial modifications to various New York tax credits:
  - Creates the Child Care Creation and Expansion Tax Credit Program Act for businesses creating or expanding their childcare capacity for the children of their employees, whether directly or via a third party. Businesses may claim a credit equal to 20 percent of the costs of creating or expanding their program’s available infant and toddler seats, capped at 25 seats. The aggregate amount of credit available is \$25 million each year, from 2023 through 2025, which will be allocated on a pro rata basis.
  - Allows New York City to adopt a biotechnology credit, beginning in tax year 2023. Governor Hochul’s original budget proposal allowed the credit to be claimed under the New York City general corporation tax, unincorporated business tax, and banking corporation tax. The Budget, however, limits the credit to the New York City general corporation tax and the unincorporated business tax.
  - Repeals a provision of the Corporate Franchise Tax that previously allowed for the transfer of unused investment tax credits in “qualified transactions” (i.e. IRC §§ 351/355 reorganizations).
- Additionally, the Budget extends or slightly modifies the following credits: the COVID-19 Capital Costs Tax Credit Program (Part F); the Rehabilitation of Historic Properties Tax Credit (Part I); the Empire State Commercial Production Tax Credit (Part I); and the No. 6 Heating Oil Conversion Tax Credit (Part I).

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## Disaster Relief

- The Budget gives the Commissioner of the Tax Department the discretion to award new disaster relief to taxpayers on multiple fronts.
- New interest abatement options for taxpayers affected by a presidentially-declared disaster or by a disaster emergency declared by the Governor.
- The Budget allows the Commissioner to abate the penalty for a corporation's underpayment of estimated tax, where the corporation was impacted by casualty, disaster, or other unusual circumstances and "the imposition of such addition to tax would be against equity and good conscience." Notably, the Commissioner already had this power with respect to personal income tax filers.

## Motor Fuel Tax Reporting

- The Budget requires distributors of motor fuel and diesel motor fuel to collect, report, and remit taxes to the Tax Department on the sale of any gallon of fuel, including additional gallons resulting from temperature fluctuations that cause the product to expand in volume.
- Fun fact: X gallons of fuel purchased by a distributor during cold weather turns in to X + Y gallons as the weather gets warmer. So, distributors can end up purchasing less fuel than they sell!
- In the past, distributors could collect additional tax on the sold fuel due to such temperature fluctuations and subsequent expansions, but were arguably not required to remit additional tax on the expansion gallons.



## REITs

- The Budget extends reduced rates for conveyances to real estate investment trusts under the New York State real estate transfer tax and the New York City real property transfer tax until September 1, 2026.

## What's Out

## No Personal Income Tax Rate Changes

- The Senate and Assembly's respective Budget proposals included increased New York personal income tax rates, including a 10.8% tax rate for income levels between \$5 million and \$25 million and an 11.4% tax rate for income levels over \$25 million.
- Governor Hochul was vocally opposed to these increased rates.
- Tax flight?

## S-Corp Elections

- Governor Hochul's original budget proposal included an amendment so that all federal S corporations would be automatically treated as S corporations for New York tax purposes, unless the corporation was a qualified New York manufacturer under Tax Law § 210(1)(a)(vi) and elected New York C corporation status on its tax return. This provision was omitted from the Budget.
- In January, we saw a similar bill passed in New Jersey (P.L. 2022, c. 133), which eliminated the requirement for federal S corporations to affirmatively elect New Jersey S corporation status and included an opt-out provision.
- As of January 1, 2023, unless an S corporation in New Jersey takes affirmative steps to opt out (which requires the consent of 100% of the shareholders), the corporation is automatically treated as a New Jersey S corporation.

## Sales Tax on Digital Products

- The Assembly's budget proposal (A.3009-B, Part EE) included a new sales tax on streaming entertainment and digital products, to fund MTA transportation systems.
- The proposal, if included in the Budget, would have imposed a 4% sales tax on digital products, including certain popular streaming services, apps, games, music, podcasts, and audiobooks. The Assembly's proposal, however, was omitted from the final Budget. Concerns were raised over the proposal's constitutionality and its conformity with the Internet Tax Freedom Act.
- A court challenge of Maryland's version of the digital products tax is ongoing.

## Something Else to Consider

- The NYS Tax Department has officially proposed (on July 25, 2023) its corporate tax reform regulations.....FINALLY!
- The new regulations propose a look-through rule for passive investment customers.
  - The passive investment customer sourcing rule has been changed to investor location (not where the contract is managed) unless location of the investor cannot be determined.
- The new regulations adjust goodwill apportionment and officially include a three-year lookback period.

## Something Else to Consider

- Remember, these regulations also make changes to New York's treatment of Public Law 86-272.
- Public Law 86-272 prevents states from imposing income taxes on businesses whose only activities in the state are restricted to the "mere solicitation" of sales of tangible personal property.
- The draft corporate regulations limit Public Law 86-272's protections for online activities.
- NY released guidance on 4/29/22 that would disqualify many internet activities from the protections of P.L. 86-272, conforming with a previous Multistate Tax Commission statement.

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## Something Else to Consider

- NY proposes that any activities, including those conducted over the internet, would escape the P.L. 86-272 shield, unless they consist only of solicitation of orders for TPP, or are de minimis.
- For example, "interacting with customers or potential customers through the corporation's website or computer application" would not be shielded by P.L. 86-272.
- Additionally, any business that uses internet "cookies" will not be shielded from taxation in NY. According to NY, the cookies generally gather information that the business will use in ways that are not entirely ancillary to solicitation or orders for TPP.
- But in conformity with MTC, just placing static text or images on a website does not trigger taxation.
- If enacted, the regulations will effectively create a path for NY to tax certain companies, with no in-state activity, simply because NY residents are engaging with the corporation's website.

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## Section 2: New Resident and Nonresident Allocation Audits/Telecommuting



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## Americans Moved to Low-Tax States in 2022

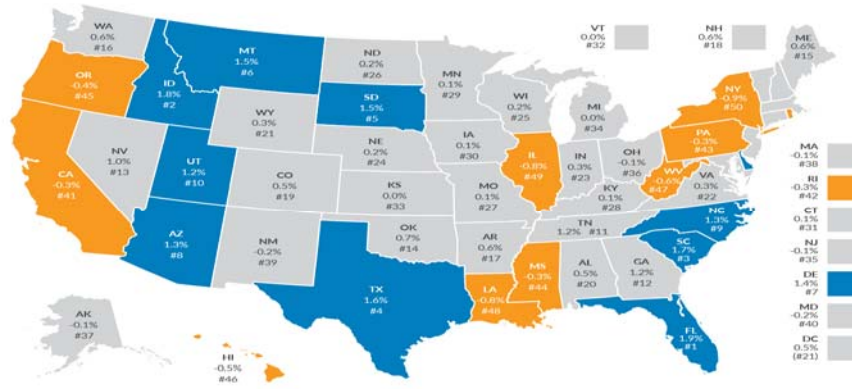
- The U.S. population grew 0.4 percent between July 2021 and July 2022, an increase from the previous year's historically low rate of 0.1 percent.
- New York's population shrunk by 0.9 percent between July 2021 and July 2022.
- According to the Tax Foundation's multistate analysis, "This population shift paints a clear picture: people left high-tax, high-cost states for lower-tax, lower-cost alternatives."
- "Moving data from U-Haul and United Van Lines...speaks more directly to cross-border migration and is confirmatory. Both companies see states like California, Illinois, Massachusetts, and New York as the biggest losers, while states like Texas, Florida, and Tennessee are among the largest net gainers."
- <https://taxfoundation.org/state-population-change-2022/>

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# Americans Moved to Low-Tax States in 2022

## State Population Change in 2022

State Migration Patterns, from Most Inbound to Most Outbound, 2022



Note: D.C.'s rank does not affect states' ranks, but the figure in parentheses indicates where it would have ranked if included.  
Source: U.S. Census Bureau.

■ Top 10 States for Inbound Migration  
■ Top 10 States for Outbound Migration

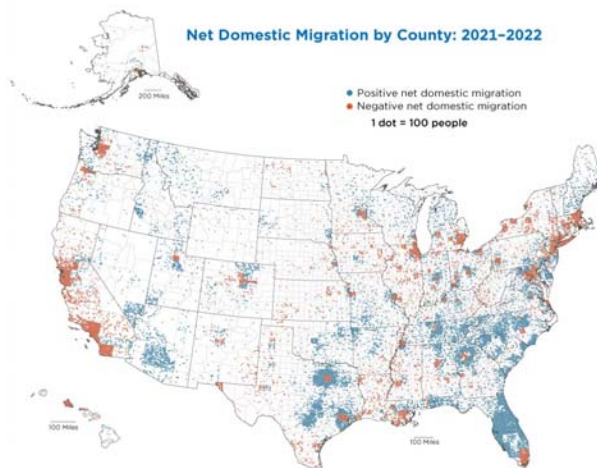
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# Americans Moved to Low-Tax States in 2022

## Net Domestic Migration by County: 2021-2022



Source: U.S. Census Bureau, Vintage 2022 Population Estimates.

■ [www.census.gov/content/dam/Census/library/stories/2023/03/domestic-migration-trends-shifted-map-1.jpg](https://www.census.gov/content/dam/Census/library/stories/2023/03/domestic-migration-trends-shifted-map-1.jpg)

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## Background

- While New York saw an exodus of residents who reported \$21 billion in total income on their 2019 federal returns, according to the IRS, Florida saw an influx of residents who reported \$41 billion in income, the most any state received. And that was before COVID!! [https://www.wsj.com/articles/miamis-gold-rush-finance-firms-and-crypto-suarez-rents-development-boom-11657317076?reflink=share\\_mobilewebshare](https://www.wsj.com/articles/miamis-gold-rush-finance-firms-and-crypto-suarez-rents-development-boom-11657317076?reflink=share_mobilewebshare).
- The COVID-driven rush of New Yorkers into Florida has turned into a stampede — with no end in sight. A record-breaking number of Empire State residents switched their driver's licenses to the Sunshine State version in August according to a NY Post analysis of Florida Department of Highway Safety and Motor Vehicles data. A total of 5,838 New Yorkers made the switch — the highest recorded number for a single month in history, the numbers show. Year to date, 41,885 New Yorkers have handed over their licenses after moving south, a torrid pace that's pointing to a new annual record. <https://nypost.com/2022/09/20/record-number-of-new-yorkers-swap-to-florida-licenses/>.
- “More New Yorkers moved to Florida in 2022 than any year in history in staggering exodus.” <https://nypost.com/2023/01/19/more-new-yorkers-moved-to-florida-in-2022-than-any-year-in-history/>.

## Background

- The State Wealth-Tax Alliance: “The ...tax alliance emerged late last week when lawmakers from eight states unveiled plans to target wealthy residents. California, New York, Illinois, Maryland, Hawaii, Minnesota, Connecticut and Washington state are all represented, and several of the sponsors have already released bills.” Jan. 24, 2023.
- <https://www.wsj.com/articles/the-state-wealth-tax-alliance-progressive-states-coordinate-illinois-new-york-washington-11674600250>

## More Interesting Numbers

- The NYC Independent Budget Office (IBO) released some startling figures in early December 2022. See: <https://www.thecity.nyc/economy/2022/12/6/23497265/nyc-tax-data-high-earners-drop-2020>.
- The analysis revealed:
  - the number of New Yorkers making between \$150,000 and \$750,000 declined by almost 6% between 2019 and 2020
  - and the number of those making more than \$750,000 dropped by almost 10%.
- The 41,000 filers in the top 1% pay just over 40% of all income taxes.
- The 450,000 in the top 10% contribute almost exactly two-thirds of the city's income tax revenue.
- The remaining 3.3 million taxpayers pay the final third.

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## New York Audit Initiatives

### Tax Audit Report - Personal Income Tax (Article 22 and 23) Desk Audits

Fiscal Year	Number of FTE Auditors	Number of Audits
2018	203	647,566
2019	217	616,572
2020	220	548,183
2021	216	494,341
2022	201	771,104

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# Residency Basics

## ▪ The Two Residency Tests (in most states)

### 1. Domicile

- One permanent, primary home
- The “Leave and Land” Rule
- Burden of proof on you (clear and convincing)
- People generally don’t change their permanent home lightly/often
- Looking for a “Lifestyle Change” (e.g. retirement, huge change in time patterns, upsizing/downsizing, health issues)
- The 5 Factors



### 2. “Statutory” Residency

- Previously 183 days + a Permanent Place of Abode
- A minute in the state counts as a day in state
- Few exceptions to day count rules



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# New York Residency Update

- In *Matter of Nelson Obus et al., v New York State Tax Appeals Tribunal*, the court ruled that a seldom-used vacation home in New York cannot be considered a “permanent place of abode” for statutory residency purposes.
- Mr. Obus lived in New Jersey but worked in New York City and maintained a vacation home upstate. And while he spent more than 183 days in New York City for work, he only used his vacation home for 3 weeks a year, it was four hours from where he worked, and he and his wife didn’t keep things there.
- And even though the place was large and definitely suitable for year-round use, the court discarded any sort of objective test to determine whether the place was a permanent place of abode for the taxpayer.
- Instead, since the case involved something so fact-specific as residency, an inquiry into the subjective aspects of the taxpayer’s use of the abode was required: “[t]he taxpayer must have utilized the dwelling as his or her residence; maintaining a dwelling that could be a permanent place of abode is not enough to establish status as a statutory resident.”

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## New York Residency Update

- The Obus court's focus on the subjective aspects of a taxpayer's abode and the purpose of the statutory residence test in the first place — to tax people who really are residents — is a major development, and will definitely have an impact not only on how vacation-home cases are handled, but on any statutory residency case where the subjective facts may suggest the taxpayer really isn't living their life as New York resident.
- Now the question will have to be, as the Obus court directed, whether a taxpayer falls within “the purview of the target class of taxpayers who were intended to qualify as statutory residents.” And who is that? In Gaied court told us that the test is designed to capture people who are, for all intents and purposes, residents of the state, i.e., people who really live in New York.
- Several questions now arise. The statutory residency test was a more mechanical test, but the new ruling injects a level of subjectivity. For example:
  - The apartment is not regularly used as a residence, but it happens to be close to the taxpayer's office?
  - How much use transforms an apartment into a PPA?

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## New York Residency Update

- The New York State Department of Taxation and Finance released a new version of its audit guidelines for nonresidents.
- Given that the last update was in 2014, we were interested to see what had changed.
- But when we dug into the new guidelines, we really only found one significant substantive change:
- The “11-Month Rule” is now the “10-Month Rule”!!!

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# Statutory Residency/Presumptions

State	Presumption/Rule
Alabama	Either maintain a place of abode in-state or spend more than a total of seven months in the year within Alabama - presumed to be residents.
Arkansas	Maintains a permanent place of abode within Arkansas and spends in the aggregate more than six months of the year
Arizona	Spends in the aggregate more than 9 months of the taxable year in Arizona is presumed to be a resident
California	Spends in the aggregate more than 9 months of the taxable year in California is presumed to be a resident
Colorado	Maintains a permanent place of abode within Colorado and who spends in the aggregate more than six months of the taxable year in Colorado
Connecticut	Maintains a permanent place of abode in the state and is in the state for an aggregate of more than 183 days during the taxable year.
D.C.	Maintains a place of abode within the District for an aggregate of 183 days or more during the taxable year
Delaware	Maintains a place of abode in Delaware and spends in the aggregate more than 183 days of the tax year in Delaware
Georgia	Residing within Georgia for 183 days or part-days, in the aggregate, of the immediately preceding 365 day period.
Hawaii	Persons who spend more than 200 days of the tax year in Hawaii are presumed to be residents
Iowa	Presumption applies if an individual maintains a place of abode in Iowa and spends more than 183 days of the tax year in Iowa
Idaho	Maintain a place of abode in Idaho for the entire tax year and spend more than 270 days of the tax year in Idaho – some safe harbors available
Illinois	Prior year resident presumed to be a resident if present in Illinois more days than in any other state during year
Indiana	Maintains a permanent place of residence in Indiana and spends more than 183 days of the taxable year within Indiana
Kansas	Spends an aggregate amount of more than six months of a taxable year within Kansas in the absence of proof to the contrary.
Kentucky	Spends, in the aggregate, more than 183 days of the tax year in the state and who maintains a place of abode in the state during that period
Louisiana	Maintains a permanent place of abode within the state or who spends in the aggregate more than six months of the taxable year within the state
Massachusetts	Maintains a permanent place of abode in Massachusetts and spends more than 183 days of the taxable year in Massachusetts
Maryland	For more than six months of the taxable year, maintained a place of abode in Maryland.
Maine	Maintains a permanent place of abode in Maine and spends in the aggregate more than 183 days of the taxable year in Maine
Michigan	Deemed a resident if lives in the state at least 183 days during the tax year or more than half the days during a tax year of less than 12 months.

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# Statutory Residency/Presumptions

State	Presumption/Rule
Minnesota	Spends at least 183 days in Minnesota and the taxpayer or spouse own, rent, maintain, or occupy a residence in Minnesota
Missouri	Maintain a permanent place of abode in-state and spend more than 183 days of the taxable period in Missouri.
Mississippi	Individuals who maintain homes, apartments, or other places of abodes in Mississippi or who meet the requirements of a Mississippi voter or enjoy a Mississippi homestead exemption are legal Mississippi residents
Montana	Maintaining a "permanent place of abode," in Montana and not establishing residency elsewhere.
North Carolina	In the absence of convincing proof to the contrary, being present within the state for more than 183 days of an income year constitutes residence.
North Dakota	Maintains a permanent place of abode within the state and spends more than seven months (210 days) of the year within the state
Nebraska	For an aggregate of more than 6 months, both maintains a permanent place of abode within Nebraska and is present in Nebraska
New Jersey	Maintains a permanent place of abode in the state and spends in the aggregate more than 183 days of the taxable year in this State
New Mexico	Physically present in New Mexico for 185 days or more during the taxable year regardless of domicile
New York	More than 183 days in New York combined with a permanent place of abode.
Ohio	An individual who has at least 213 "contact periods" with the state is presumed to be domiciled for the entire taxable year.
Oklahoma	Spends more than seven months of the taxable year in Oklahoma is presumed to be a resident in absence of proof to the contrary.
Oregon	Maintains a permanent place of abode in Oregon and spends more than 200 days, in the aggregate, of the taxable year.
Pennsylvania	Maintains a permanent place of abode in Pennsylvania and spends, in the aggregate, more than 183 days there.
Rhode Island	Maintains a permanent place of abode in Rhode Island and is present in the state for an aggregate of more than 183 days during the tax year
Tennessee	Maintaining a place of residence for more than six months will cause a person to be liable for tax
Utah	Has an abode in the state and spends at least 183 days in the state during the tax year (recently changed to be a factor for domicile)
Virginia	Maintains a place of abode in Virginia for more than 183 days during the tax year.
Vermont	Those who maintain a Vermont permanent residence and are in Vermont for over 183 days of the tax year are considered residents.
West Virginia	Maintains a permanent place of abode in-state and spends in the aggregate more than 183 days of the taxable year in-state

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## Nonresident Comp. Allocation

- If employee is a resident of the state where they work, then 100% of their compensation income is subject to that state's tax, and employer must withhold 100% state tax.
- If employee is a nonresident of the state where they work, then state tax still due to the extent of the taxpayer's workdays in the state.
- Formula:  $[\text{In-State Workdays}] \div [\text{Total Workdays}] = [\text{Workday Percentage}]$ 
  - Employer must withhold state tax based on that workday percentage
  - Employee reports allocable income based on that workday percentage

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## The Basics of Allocating Compensation

- What counts as a workday?
  - Typical workdays (Monday-Friday)
  - Weekends? Holidays? Travel days?
- Where is the workday spent?
  - Pre-Covid: Most states using "physical presence" to determine location
  - Easy: Days spent in the state by the nonresident employee on company business
  - Not so easy: Telecommuting and remote work

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## Allocating “Regular” Wages/Salary

- Allocation is required when a nonresident’s in-state workdays/compensation exceeds the applicable threshold (if any)

- Allocation formula:

$$\frac{\text{In-State Workdays}}{\text{Total Workdays}} \times \text{Total Wages}$$

- “Workday” typically **includes** travel days, days worked from home, days worked on weekends
- “Workday” typically **excludes** holidays, vacations, sick days, weekends

## Counting Workdays

Total Days in Year		365
Nonworking days:		
Saturdays/Sundays	104	
Holidays	10	
Vacation Days	14	
Sick Days	5	
Other Nonworking Days	2	
Total Nonworking Days		135
Total Days Worked in Year		230
Total Days Worked Out-of-State		55
Total Days Worked In-State		175

## State Responses to Telecommuting and COVID-19

State	Sourced to Employer's Home State	Sourced to Employee's Work Location
Alabama	X	
Arkansas	X (until 12/1/20)	X (as of 1/1/21)
California		X
Colorado		X
Connecticut		X (2020 only)
Delaware		X
Georgia	X	
Illinois*		X
Iowa		X
Kansas	X (both until 12/31/20)	X (only as of 1/1/21)
Kentucky		X
Maine	X (until 6/30/21)	
Maryland		X
Massachusetts	X (until 9/13/21)	
Minnesota		X
Mississippi	X	

\*Withholding required if employee is telecommuting from IL for more than 30 days

State	Sourced to Employer's Home State	Sourced to Employee's Work Location
Missouri	X (for some employers if elected until 7/19/21)	X
Montana		X
Nebraska	X (until 7/30/21)	
New Jersey**	X	X
New York	X	
North Carolina		X
Ohio (municipal income tax)	X (until 12/31/21)	
Oregon		X
Pennsylvania		X (until 6/20/21)
Rhode Island	X	
South Carolina	X (until 9/30/21)	
Vermont		X
Wisconsin		X

\*\*Rules of Employer's home state dictate which state gets the tax

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## Telecommuting Post-COVID

### So Now What?

- Telecommuting is not going away.
- And while states were willing to change rules during the emergency of COVID, now what happens?
- Enter the Convenience Rule and NY's new enforcement initiatives.

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## 2021/2022 Requests for Information – Excerpts

**We need more information by June 15, 2021 about your 2020 New York State income tax return.**

**Why did you get this letter?**

We need to verify the amount of income you allocated to New York State, as reported in the *New York State amount* column of your return.

If you are a nonresident or part-year resident whose assigned primary work location is in New York State, days you worked at a location outside New York State may be considered New York State work days. In particular, days you telecommuted from a location outside New York State are considered New York State work days unless your employer has established a bona fide employer office at your telecommuting location.

Additional information about residency and telecommuting can be found on our website at [www.tax.ny.gov](http://www.tax.ny.gov) (search: telecommuting).

**What must you do?**

1. You must verify your income allocation by providing the following (for each taxpayer if a joint return):
  - A copy of your federal W-2, *Wage and Tax Statement*, for each employer;
  - A completed *Income Allocation Questionnaire* (Form AU-262.55, enclosed) for each employer; and
  - A full description of the composition of your wages (base compensation, bonuses, stock options, sick pay, vacation pay, severance pay, gambling income, unemployment compensation, etc.).

**How do you send this back to us?**

The best way is online. It is easy to start an account at [www.tax.ny.gov/online](http://www.tax.ny.gov/online). From there, you can attach images and files of supporting documentation. Please include an image of this letter in your response. Responding online is also:

- Safe, secure, and confidential. Your information and privacy are protected.
- Quick. Your information will be instantly delivered to us.
- User-friendly. It is easy to navigate.
- Economical. It is the least expensive way to respond.

## 2021/2022 Requests for Information – Excerpts

X- [REDACTED]

**What if you cannot get online?**

You can also send us the information by fax, U.S. Mail, or by a private delivery service (see Publication 55, *Designated Private Delivery Services*). Please include a copy of this letter in your response.

- Fax: 518-435-8518
- U.S. Mail: NYS Tax Department, Audit Division-Income/Franchise Desk, P.O. Box 15270, Albany, NY 12212-5270
- Private delivery service: NYS Tax Department, RPC-PIT, 90 Cohoes Avenue, Green Island, NY 12183.

**What happens after you send in the required information?**

We will attach the information you provide to the return you already submitted, then we will continue processing your return. There may still be other changes to your return. If we need additional information to continue processing your return, would you like us to contact you by phone? If so, please include a daytime phone number:

Daytime phone number \_\_\_\_\_ Taxpayer name \_\_\_\_\_

**What happens if you do not send all the information we need by [REDACTED] 2021?**

We will process your return without this information. That may reduce your refund or increase the amount of tax you owe.

**Who do you contact if you have questions?**

You may call us at 518-457-2255.

**Your rights as a taxpayer**

See Publication 130-D, *The New York State Tax Audit - Your Rights and Responsibilities*, available on our website.

## 2021/2022 Requests for Information – Excerpts


**Department of  
Taxation and Finance**  
 Audit Division-Income/Franchise Desk  
 W A Harriman Campus, Albany NY 12227-9995

X-999999999

### Income Allocation Questionnaire

Tax year	Taxpayer name	Audit case ID
----------	---------------	---------------

You must verify the amount of income you allocated to New York State as reported in the *New York State* amount column of your income tax return. If you are a nonresident or part-year resident whose assigned primary work location is in New York State, days you worked at a location outside New York State may be considered New York workdays. In particular, days you telecommuted from a location outside New York State are considered days worked in the state, unless your employer has established a bona fide employer office at your telecommuting location.

Complete this questionnaire for **each** employer (for each taxpayer if a joint return). Attach additional sheets if necessary.

Employer name and address: \_\_\_\_\_

Job title: \_\_\_\_\_

Period of employment (full year or specific dates): \_\_\_\_\_

Assigned primary work location: \_\_\_\_\_

If your assigned primary work location changed during the tax year, provide proof of this change.

Total compensation for the period of employment (from federal Forms W-2): \_\_\_\_\_

Provide a full description of the composition of your wages (base compensation, bonuses, stock options, sick pay, vacation pay, severance pay, gambling income, unemployment compensation, etc.): \_\_\_\_\_

Total number of days in the employment period: \_\_\_\_\_

Total number of non-working days (weekends, holidays, vacation, sick leave, etc.): \_\_\_\_\_

Total number of working days: \_\_\_\_\_

Total days worked at home: \_\_\_\_\_

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## 2021/2022 Requests for Information – Excerpts

### Location of working days:

Address	Type of work location (office, home, client site, etc.)	Number of days worked at location	Nature of duties performed (in-person business meetings, telecommuting, client visit, etc.)

You must be prepared to provide documentation substantiating the above day counts upon request.

If you telecommuted from a location or locations outside New York State, please specify whether any such location constituted a bona fide employer office, and provide proof of actions taken by the employer, if any, to establish a bona fide employer office at that location. For more information on the factors used to determine whether a telecommuting location is a bona fide employer office, see [www.tax.ny.gov](http://www.tax.ny.gov) (search: *telecommuting*).

I certify that the information given herein is true and correct.

Date	Taxpayer's signature	Taxpayer's Social Security number
Date	Spouse's signature (if joint return)	Spouse's Social Security number (if joint return)




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# Pre-Pandemic Desk Audit Notices

 **Department of  
Taxation and Finance**  
Audit Division-Income/Franchise Desk-AGS  
W A Harriman Campus, Albany NY 12227-9996

August 14, 2019

Case ID: [REDACTED]  
DLN: [REDACTED]  
Tax year: 2016

190300234700-AD00

[REDACTED]

**We need more information about your New York State income tax return.**

We need additional information about the capital gains reported on your return for the tax year above.

If you do not respond to this letter within **30 days**, we will consider all your capital gains to be New York source income, which may result in a bill.

**Send us:**

- The date you moved out of New York State: \_\_\_\_\_
- A copy of the federal Schedule D, *Capital Gains and Losses*, and Form(s) 8949, *Sales and Other Dispositions of Capital Assets*.
- For each capital gain or loss, provide the date of sale.
- If any of the gains or losses were from a partnership, S corporation, trust, or estate, provide an explanation of how you allocated the gains or losses to your New York State residency period.
- If you sold property, provide the address of the property and the date it was sold: \_\_\_\_\_
- If the capital gain is the result of an installment sale, provide a copy of federal Form 6252, *Installment Sale Income*, with Part 1 completed from the year of the sale.
- A daytime phone number so we may contact you if we need more information: \_\_\_\_\_

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# The “Convenience of the Employer” Rule

## The Basic Rule

- In general, if the employee works from home for their own convenience, broadly defined, the workdays at home will be treated as days worked at their assigned work location.
- Applications:
  - Nonresident income allocation
  - Withholding
  - Resident credits

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# The “Convenience of the Employer” Rule

- 7 states (AR, CT, DE, NE, NJ, NY, PA) have some form of a “Convenience Rule.”
- Nuances:
  - CT’s and NJ’s rule only applies if the other state is a “Convenience State.”
  - NJ’s rule is brand new (July 1, 2023) and only applies to AR, DE, NE, and NY. It does not apply to PA due to a reciprocity agreement, and it does not apply to CT because that state’s rule only applies if the other state imposes a general convenience rule. See: <https://www.state.nj.us/treasury/taxation/newlegislation2023.shtml>.
  - Several states (GA, MA, ME, MS, NE, NY, PA, RI, SC) issued guidance or temporary legislation during pandemic requiring that days worked at home continue to be treated as if worked the employee’s regular place of work.

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## Convenience Rule States

<b>Connecticut</b> Conn. Gen. Stat. § 12-711(b)(2)(C)	“For purposes of determining the compensation derived from or connected with sources within this state, a nonresident . . . shall include income from days worked outside this state for such person’s convenience <u>if such person’s state of domicile uses a similar test.</u> ”
<b>Delaware</b> 2020 Schedule W 30 Del. C. § 1124(b).	For nonresidents, non-Delaware workdays “must be based on necessity of work outside . . . Delaware in performance of duties for the employer, as opposed to solely for the convenience of the employee. Working from [a home office] does not satisfy the requirements of ‘necessity’ of duties for your employer and is considered for the convenience of the employee <u>unless working from home is a requirement of employment with your employer.</u> ”
<b>New Jersey</b> P.L.2023, c.125 was enacted on July 21, 2023, effective Jan. 1, 2023	<p>Under the convenience rule, a nonresident taxpayer’s employee compensation from a New Jersey employer for the performance of personal services is sourced to the employer’s location (New Jersey) if the employee is working from an out-of-state location (e.g. at home in their resident state) for their own convenience rather than for the necessity of their employer.</p> <p>In determining whether compensation earned by a nonresident telecommuting for a New Jersey employer will be deemed New Jersey sourced income, New Jersey will apply a similar rule which would be the same as the triggering state’s rule. For example, compensation earned by a New York resident telecommuting for a New Jersey employer will be deemed New Jersey sourced income by applying the New York “convenience of the employer” test.</p>

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## Convenience Rule States - *continued*

<b>Nebraska</b> 316 Neb. Admin. Code 22-003.01C(1)	<p>"If the nonresident's service is performed without Nebraska for his or her convenience, but the service is directly related to a business, trade, or profession carried on within Nebraska and except for the nonresident's convenience, the service could have been performed within Nebraska, the compensation for such services shall be Nebraska source income."</p>
<b>New York</b> 20 NYCRR 132.18(a) TSB-M-06(5)I	<p>"Any allowance claimed for days worked outside New York State must be based upon the performance of services which of necessity, as distinguished from convenience, obligate the employee to out-of-state duties in the service of his employer."</p>
<b>Pennsylvania</b> 61 Pa. Code § 109.8	<p>If a nonresident employee (including corporate officers but generally excluding salesmen) performs services both within and without PA, their PA-sourced income includes the ratio of PA workdays over total workdays. For this ratio, Non-PA workdays include days worked out-of-state performing services "which, of necessity, obligate the [employee] to perform out-of-State duties in the service of his employer."</p>

## NY's "Convenience of the Employer" Rule

- New York continues to send desk audit notices to taxpayers who previously allocated all of their W-2 income to New York or whose allocation percentage decreased from 2019-2020 or from 2020-2021.

- Some of the 2020/2021 notices stated:

*"We have determined that you were unable to access your office located in New York due to a temporary office closure resulting from Covid-19. If an employee's assigned or primary work location was New York prior to Covid-19 temporary office closure, and the employer continues to maintain the New York office for the employee, the employer's assigned and primary work location is still New York. The fact that the New York office is not used during the Covid-19 office closure does not affect the conclusion."*

## NY Example: July 2020 NYS FAQ on COVID Telecommuting

**My primary office is inside New York State, but I am telecommuting from outside of the state due to the COVID-19 pandemic. Do I owe New York taxes on the income I earn while telecommuting?**

*If you are a nonresident whose primary office is in New York State, your days telecommuting during the pandemic are considered days worked in the state unless your employer has established a bona fide employer office at your telecommuting location.*

*There are a number of factors that determine whether your employer has established a bona fide employer office at your telecommuting location. In general, unless your employer specifically acted to establish a bona fide employer office at your telecommuting location, you will continue to owe New York State income tax on income earned while telecommuting.*

<https://www.tax.ny.gov/pit/file/nonresident-faqs.htm#telecommuting>

## The “Convenience of the Employer” Rule After COVID-19

- Employers are going to increasingly have to deal with these convenience issues and some interesting questions are arising.
- What happens if an employer no longer has a physical office?
- Are there any nexus or tax calculation issues for allowing employees to telecommute?

## Options to Avoid New York's Convenience Rule

- **Option #1: Assign to Non-NY Office**
  - But be careful that this assignment is real! (see next slides)
  - Should be used regularly, paid for by employer, etc.
- **Option #2: Bona-Fide Home Office**
  - TSB-M Factors
- **Option #3: No NY Workdays**
  - Year-by-year test - *Hayes v. State Tax Comm.*, 401 N.Y.S.2d 876 (N.Y. App. Div. 1978): Nonresident, who under his agreement to provide consultant services could have been required to work in New York **but who did not work in New York at all**, was not subject to New York state personal income tax liability no matter for whose convenience or necessity he performed the work.
  - Even a few New York workdays, probably too many (See *Matter of Huckaby*)
  - Should be in writing (employee told that they are not required to come to the NY office and employee indicates that they are not planning to come to NY during the calendar year)
  - Should be documented (for withholding purposes, T&E should reflect that no travel to NY)
- **Watch out for changes**
  - More states may adopt convenience rules
  - Congress could step-in

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## Reassignment to a Non-New York Office

- No written guidance as to what constitutes an individual's primary office.
- On Audit, NY has looked at facts, such as:
  - Office that individual visits more than any other
  - Where is employee's administrative support?
  - Where does the employee's supervisor, managers, or "team" sit?
  - Does the employee still have designated office space in NY?
  - What do employer HR records designate as primary office?
- There must be evidence other than geographical proximity to reassign an employee to another office.

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# The TSB-M Factors

**Step 1: Primary Factor:** Employee's duties require the use of special facilities that cannot be made available at the employer's place of business, but those facilities are available at or near the employee's home

If the home office does NOT satisfy the primary factor, proceed to Step 2

**Step 2: The Secondary and "Other" Factors:** The home office may still qualify as a "bona fide employer office" if it meets four out of the six Secondary Factors **PLUS** three out of the ten "Other" Factors

## Secondary Factors (4 out of 6)

1. Home office is a requirement or condition of employment
2. Employer has a bona fide business purpose for the employee's home office location.
3. Employee performs some core duties at the home office.
4. Employee meets with clients, patients, or customers at the home office.
5. Employer does not provide the employee with office space or regular work accommodations.
6. Employer reimburses expenses for the home office.

## "Other" Factors (3 out of 10)

1. Employer maintains a separate telephone line and listing for the home office.
2. Employee's home office address and phone number are on the employer's business letterhead and/or cards.
3. Employee uses a specific area of the home exclusively for the employer's business.
4. Employee keeps inventory of products or samples in the home office.
5. Employer's business records are stored at the home office.
6. Employer signage at the home office.
7. Home office is advertised as employer's place of business.
8. Home office covered by a business-related insurance policy.
9. Employee properly claims a deduction for home office expenses for federal income tax purposes.
10. Employee is not an officer of the company.

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# Tricky Problems and Practical Solutions

- How do you count a "day"?
- What is the proper denominator?
- Bonuses
- Severance (for past or future services?)
- Stock options
  - New York: Grant to vest
  - California: Grant to exercise
  - Connecticut: Grant to exercise
  - Credits for taxes paid to other states may not sync
- Retirement income – Public Law 104-95
- Special rules for professional athletes, entertainers, public figures & employers involved in the business of interstate transportation
- Rewards for whistleblowers
- IRS information sharing

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## Section 3: Sales Tax Hot Topics

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## Sales and Use Tax: A High-Stakes Gamble

### Sales and Use Tax Characteristics:

1. Ubiquity
2. Onerous Record Keeping
3. Aggressive Audit Methodologies
4. Pyramiding of Tax Liabilities
5. Burdensome Penalties and Interest
6. Personal Liability
7. Advanced Audit Targeting
8. Confusion!



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## Four Examples of Sales Tax Fun

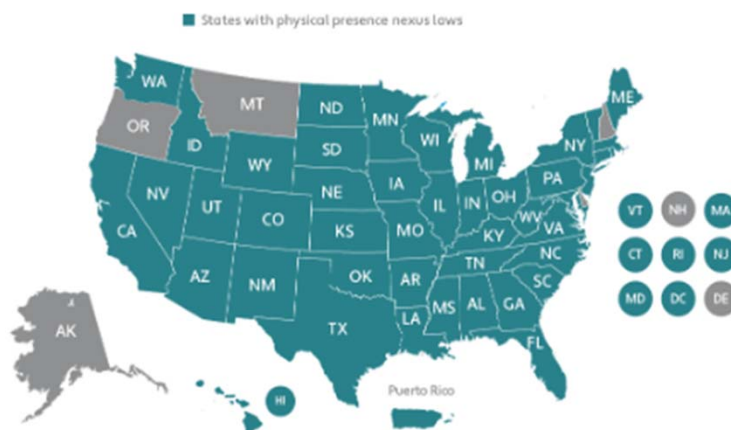
- Don't cut that bagel!
- Is that a headband or a sweatband?
- Home inspections
- Pumpkins



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## On Top of That, Nexus Broadens

- We went from this:

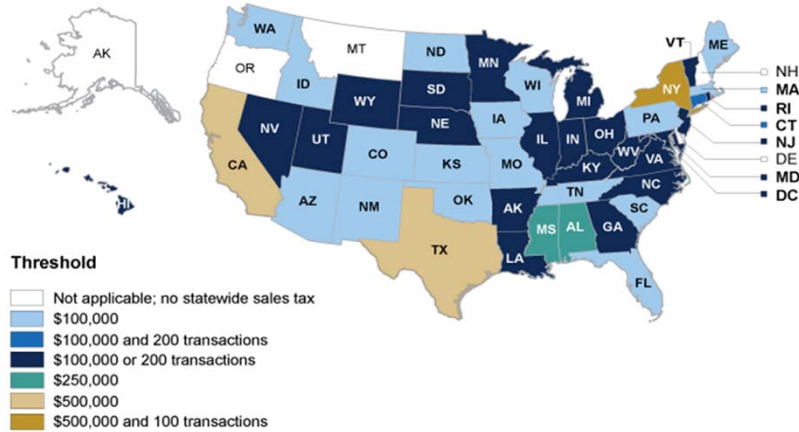


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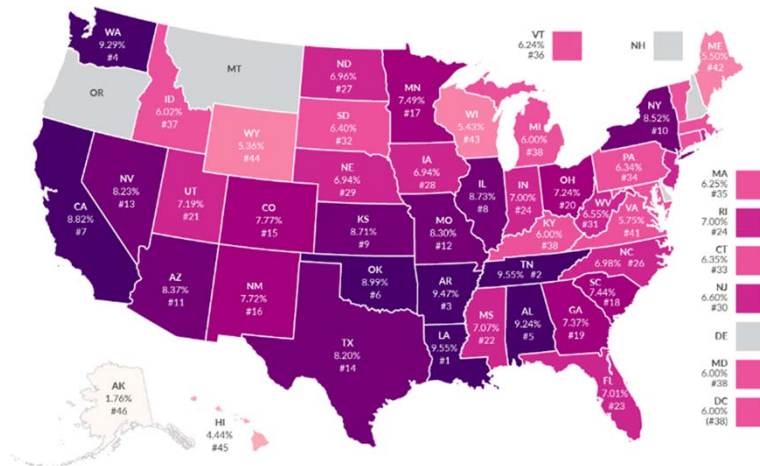
# On Top of That, Nexus Broadens

- And moved to this:



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# Sales and Use Tax Rates



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## Sales Tax Hot Topics

1. Software-as-a-Service and Digital / Technology Transactions
2. Protective / Detective Services
3. Use Tax for Professional Services Businesses
4. Information / Advertising Services
5. Artwork / Collectibles

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## First Things First.....

What digital products are subject to tax in NYS?

1. Canned Software – whether physically or electronically transferred or accessed (e.g., electronic download, SaaS, etc.). Tax Law § 1105(a) – really?
2. Canned Information Services – any information that comes from a common database (i.e., is not personal or individual to the purchaser and can be sold to other purchasers). Tax Law § 1105(c)(1), see also TSB-M-10(7)S.
3. IT Security Services – can be taxable as either remote use of software (firewalls, anti-spamware, anti-malware, etc.) or as a protective service. N.Y. Tax Law § 1105(c)(8); TSB-A-20(49)S; TSB-A-16(20)S; TSB-A-10(14)S.

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## First Things First.....

What digital products are NOT subject to tax in NYS?

1. eBooks, Digital Movies/Songs – provided they do not contain functionality that could allow them to be characterized as software or qualify as an information service. TSB-M-11(5)S; TSB-A-11(20)S.
2. Infrastructure as a Service – remote access of hardware (servers, CPUs, etc.) is not taxable. See TSB-A-15(2)S; TSB-A-17(21)S.
3. Data Hosting Services – generally not taxable, but be careful. Can it be taxable as access to software? TSB-A-16(19)S.
4. Software Maintenance – See Tax Law § 1115(o). But be careful: TSB-A-07(28)S.
5. Non-Fungible Tokens (NFTs) – not yet, but that's the next frontier....

## The Primary Function Test

- But what if an otherwise nontaxable service has potentially taxable components?
- Enter the Primary Function Test.
- “...we cannot accept the Division's argument that the means by which a service is provided is the controlling factor in determining whether the subject service is taxable. To neglect the primary function of petitioners' business in order to dissect the service it provides into what appear to be taxable events stretches the application of Article 28 far beyond that contemplated by the Legislature.” *Matter of SSOV '81 Ltd. d/b/a People Resources, et al*, DTA Nos. 810966, 810967, (TAT, Jan. 19, 1995).

## *Matter of Beeline.com, Inc.*

▪ ***In the Matter of Beeline.com, Inc., Division of Tax Appeals, DTA Nos. 829516, February 9, 2023:***

- The question was whether the taxpayer sold a taxable license to use software, or a nontaxable service of “matching” suppliers of temporary labor and customers needing such labor.
- The taxpayer’s website highlighted how important the software was to the final product. According to the ALJ, “it is the software that streamlines, automates and integrates the entire bundle of services petitioner is selling.”
- “...the ultimate goal was to provide customers a seamless, automated and efficient system of fulfilling and monitoring their temporary employment needs, and that required, as the contract reflects, utilization of the software technology license.”

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## *Matter of Yesware, Inc.*

▪ ***In the Matter of Yesware, Inc., Division of Tax Appeals, DTA Nos. 829638, 829639 and 829640, September 29, 2022:***

- The ALJ held Yesware was selling an exempt information service and not licensing taxable software.
- Yesware’s service was storage of client data and provision of access to it through Yesware’s website and browser extensions. The company tracks, processes, and analyzes data it receives from recipients of its clients’ emails and generates individualized reports to assist clients with their email prospecting and customer engagement efforts.
- Critically, the license agreement was for the license to use the *service*, and not a license of *software*.
- The ALJ applied the “primary function” test to determine that Yesware’s bundled product was more service than software. What Yesware’s clients really wanted were the reports Yesware generated.
- <https://www.dta.ny.gov/pdf/determinations/829638.det.pdf>

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## Matter of Employment Screening Services, Inc.

### ▪ ***In the Matter of Employment Screening Services, Inc., Division of Tax Appeals, DTA No. 829702, October 6, 2022:***

- The ALJ held that the Petitioner's employee pre-screening services were not taxable as "protective or detective services". Petitioner provided screening services to employers, including verifying a prospective employee's federal and state criminal record, drug screenings, education, bankruptcies, etc.
- The Judge reasoned the services could not be "detective" services, as Petitioner did not hold itself out as a detective service; nor was it licensed as a detective or private investigator. Nor did the services constitute "protective" service, since the services did not consist of watching, guarding and patrolling or similar functions:
- *"While it is acknowledged that petitioner's screening services provide some degree of assurance to its clients that they are screening out 'bad actors,' these services can hardly be considered the type of protective services that come within the purview of the statute."*
- The ALJ instead held the services constituted a form of "information service," but one that met the exclusion for information that is "personal and individual in nature".
- <https://www.dta.ny.gov/pdf/determinations/829702.det.pdf>
- PS – this taxpayer also sought to have the Tax Department to pay its legal fees, but its application was denied.

## Matter of Secureworks, Inc.

### ▪ ***In the Matter of SecureWorks, Inc., Tax Appeals Tribunal, DTA Nos. 828328 and 828329, February, 17 2022:***

- The Tribunal upheld the ALJ decisions which concluded that New York sales tax applies to certain online security services when such services are provided with respect to devices located in New York. The Tribunal found that most of the IT security services provided by the taxpayer were subject to New York sales tax as "protective and detective services" under N.Y. Tax Law § 1105(c)(8).
- The taxable IT services generally included SecureWorks' performance security "management" services and security "monitoring" services.
- The Tribunal also concluded that certain ancillary SecureWorks offerings were not "protective and detective services," but were taxable as "information services" under N.Y. Tax Law § 1105(c)(1). The Tribunal explained these information services did not qualify for New York's "personal or individual in nature" exception because "[c]ustomization of publicly available information into a report does not render it personal or individual in nature."
- Lastly, the Tribunal concluded that only the "log retention service" was not a taxable "protective and detective service" because the taxpayer merely "ensur[es] the proper operation of a device so that it retains all of the events created on a network."
- <https://www.dta.ny.gov/pdf/decisions/828328and828329.dec.pdf>

## *Matter of Breakdown Services, Ltd.*

▪ **In the *Matter of Breakdown Services, Ltd.*, Division of Tax Appeals, DTA No. 829396, January 27, 2022:**

- The ALJ held that the taxpayer's online casting facilitation service—helping casting agents find roles for film/television roles—was similar to the dating service in *SSOV'81*. The taxpayer provided a forum through which casting directors and talent representatives could list and view roles and connect regarding those roles.
- The record showed that the taxpayer was involved in the entire casting process, not just posting and providing access to information on roles, but assisting in facilitating connections and scheduling of auditions, etc.
- The service included various software and information components, so SaaS was at issue, too.
- BUT - **"Clearly, the primary function of petitioner's service is the facilitating of casting actors in acting roles, which is an unenumerated, nontaxable service."**
- <https://www.dta.ny.gov/pdf/determinations/829396.det.pdf>

## *Matter of Lender Consulting Services, Inc.*

▪ **In the *Matter of Lender Consulting Services, Inc.*, Division of Tax Appeals, DTA No. 829198 December 2, 2021**

- ALJ determined the primary function/object of the Petitioner's environmental risk reports sold to commercial lenders was a professional opinion regarding risk of environmental contamination not merely a sale of the underlying information on which the opinion was based.
- This was the case even though the "reports" often contained hundreds of pages of common database information on a parcel and only several pages explaining the resulting risk opinion.

## Primary Function Takeaways

- Define the product appropriately – be specific and technical.
  - Emphasize the aspects of the service/product that are not automated or that require employee interaction. Too often these are left out of or not adequately described in contracts and invoicing.
  - Avoid problematic buzzwords like software, technology, platform, SaaS, licenses, etc.
  - Focus on nontaxable services where appropriate: data processing, logistics management, computing power, data storage, advertising services.
  - This is about who “uses” the software; the service provider or the customer?
  - But ultimately, the facts of the situation will govern. If it quacks like a duck.....

## Primary Function Takeaways

- Speak with one voice
  - Make sure the following items all define the product consistently:
    - Books & records
    - Tax returns
    - Contracts
    - Invoices
    - Marketing brochures
    - Website material
    - Regulatory filings
    - Client deliverables

# Enforcement/Audit Issues

## ■ How does a business get chosen for audit?

1. Audits of other taxpayers
2. Whistleblower Issues
3. NY's CISS program
  - Corporate tax return sales v. sales tax return sales
  - Consistent taxable percentage
  - Drastic changes in filing pattern
  - New "self-audit" letters based on ratios and "typical" use tax liabilities.
  - Information from more sources (franchisers, insurance companies, liquor distributors, and financial institutions)
  - Compare returns of similar businesses operating within the same geographic areas
  - Lottery traffic vs. low sales
  - Cash/credit card ratio out of sync with similar businesses
  - Speeding and parking tickets
  - The pre-audit analysis (auditors have info before taxpayer knows an audit is underway)



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# Initial Audit Letter

**Department of Taxation and Finance**  
Transaction Field Audit Bureau - Buffalo District Office  
77 Broadway, Suite 300, Buffalo, NY 14203-1842

March 17, 2023

**Initial Here**

Taxpayer ID: [REDACTED]  
Audit Period: 12/01/2016 - 11/09/2022  
Tax Article(s): 28 & 29  
Case ID(s): [REDACTED]

**We've scheduled an audit of your New York State Sales and Use Tax records.**

A Tax Department auditor, Mrs. Lisa Massey, will be at your place of business on **May 2, 2023** at **9:00 AM** to begin the audit.

Please call your auditor, Mrs. Lisa Massey, at (716) 855-6335 to confirm this initial conference.

Please confirm receipt of this Information Document Request (IDR) by either contacting your auditor by phone at the number listed above or returning an inked copy of this letter. If not using U.S. Mail, see Publication 55, Designated Private Delivery Services.

**What to expect**  
In a sales and use tax audit, Tax Department auditors will review your books and records to confirm that you've complied with all applicable tax laws. At the initial conference, the auditor can answer any questions you may have about the audit process.

To learn more, see the enclosed Publication 130F, The New York State Tax Audit—Your Rights and Responsibilities and Publication 900, Important Information for Business Owners.

**Who should attend**  
Any of your business's officers or employees who are familiar with your business operations should attend the initial conference. If you've authorized someone to appear on your behalf during the audit, make sure that they bring a completed Power of Attorney (Form POA-1, available on our website, [www.tax.ny.gov](http://www.tax.ny.gov)) to the meeting.

**What books and records you must provide**  
You must show any and all documentation in auditable form and electronic form (if available) which supports the returns as filed. The enclosed IDR describes the books and records that you must have available at the initial conference. Please record the date each item is provided to the auditor in the "Date(s) Provided" column. Please also note what items are unavailable.

If records are voluminous, please discuss the IDR with the auditor. Audit techniques, as described in Pub. 130F, can also be discussed at that time. The auditor may ask you to provide only a few items at the initial conference, or they may ask for specific records and information in addition to the items on the IDR.

DD-1631 (5/15) [www.tax.ny.gov](http://www.tax.ny.gov)

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Be sure to have all **exemption certificates** available at the initial conference. The auditor may **disallow** any certificates that:

- you do not provide; or
- are not properly completed.

**Other taxes**  
This audit will focus on **sales and use tax**. In the course of the audit, we may learn of issues regarding other kinds of taxes, such as personal income tax or corporation tax. If so, the Tax Department may expand the scope of the audit and conduct a multi-tax audit or a separate tax audit. If so, you must provide the auditors with records pertaining to these other taxes.

**Communication by secure e-mail**  
The Tax Department's secure e-mail program allows taxpayers and their representatives to communicate electronically with auditors and to transfer data files quickly and securely. Please let your auditor know if you're interested in registering for the program.

**Auditor name:** Mrs. Lisa Massey  
**Auditor title:** Field Audit Specialist  
**Auditor email:** [lisa.massey@tax.ny.gov](mailto:lisa.massey@tax.ny.gov)  
**Supervisor name:** Mr. Joseph H. Edwards  
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**Supervisor email:** [joseph.edwards@tax.ny.gov](mailto:joseph.edwards@tax.ny.gov)



**Enclosures:** Assistance Information Flyer  
Information Document Request #01  
Publication 130F  
Publication 900  
Sales Tax Questionnaire  
Responsible Person Questionnaire  
Computer Audit Feasibility Questionnaire

DD-1631 (5/15) Page 2 of 2 [www.tax.ny.gov](http://www.tax.ny.gov)

**Hodgson RUSSELL**  
ATTORNEYS




# Initial Audit Letter

<p> <b>Department of Taxation and Finance</b> Transaction Field Audit Bureau - Long Island Regional Office 1170 Office Building, 285 Veterans Memorial Highway, Hauppauge, NY 11788-5559</p> <p>March 22, 2023 Audit case ID: [REDACTED] Tax type: Sales and Use Tax Tax period: 03/01/2020 - 02/28/2023 Audit period: 03/01/2020 - 02/28/2023 Taxpayer ID: [REDACTED]</p> <p><b>We selected your New York State sales and use tax records for an audit.</b> This letter is to inform you that we will examine your records. Review the attached Information Document Request (IDR).</p> <p><b>What to expect</b> A Tax Department auditor, Mrs. Kanichia Osbourne, will review your books and records to confirm you complied with all applicable tax laws. The auditor can answer any questions you may have about the audit process at any time. To learn more, see the enclosed Publication 130-F, The New York State Tax Audit—Your Rights and Responsibilities, and Publication 900, Important Information for Business Owners. <b>What books and records you must provide</b> You must provide all documentation in auditable form and electronic form (if available) to support the returns as filed. The enclosed IDR describes the books and records that you must provide. If your records are voluminous, discuss the IDR with the auditor. You can also discuss audit techniques, as described in Publication 130-F, at that time. As the audit progresses, the auditor may ask you to provide records and information in addition to the items on the IDR. We may schedule a field visit to review the information requested.</p> <p>AU-1631.2 (5/02) <i>Continued on page 2</i> <a href="http://www.tax.ny.gov">www.tax.ny.gov</a></p>	<p><b>Other taxes</b> During the audit, we may learn of issues regarding other kinds of taxes. If so, we may expand the scope of the audit and conduct a multi-tax audit or a separate tax audit and you must provide the auditors with records pertaining to these other taxes.</p> <p><b>Secure communication and data transfer</b> The Tax Department's secure e-mail program allows taxpayers and their representatives to communicate electronically with auditors and to transfer data files quickly and securely. We also offer a secure data transfer tool for taxpayers and their representatives to share electronic files with their auditor. Let your auditor know if you are interested in using either program.</p> <p><b>Questionnaires</b> We enclosed one or more questionnaires requesting information about your business. The information that you provide on the questionnaires will help the audit process. Please fill them out and return them by 04/05/2023: • by mail to the address above; • by secure email; or • by FAX at (516) 435-8554.</p> <p><b>What to do next</b> 1. Call your auditor by 04/05/2023, at the number below to confirm receipt of the IDR. 2. Complete all items on the IDR and send them to your auditor by the date shown on the IDR.</p> <p><b>Questions?</b> • Visit our website • Contact your auditor at the phone number below</p> <p>Auditor name: Mrs. Kanichia Osbourne Auditor phone: (831) 595-4233 Auditor email: <a href="mailto:kanichia.osbourne@tax.ny.gov">kanichia.osbourne@tax.ny.gov</a> Supervisor name: Mrs. Mary Ohara Supervisor phone: (831) 595-4342 Supervisor email: <a href="mailto:Mary.Ohara@tax.ny.gov">Mary.Ohara@tax.ny.gov</a> Enclosures: Assistance Information Flysheet Information Document Request #01 Publication 130-F Publication 900 Responsible Person Questionnaire Sales Tax Questionnaire Computer Audit Feasibility Questionnaire</p> <p>AU-1631.2 (5/02) Page 2 <a href="http://www.tax.ny.gov">www.tax.ny.gov</a></p>	<p></p>
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# Information and Document Request #1

<p>New York State Department of Taxation and Finance Transaction Field Audit Bureau 1170 Office Building, 285 Veterans Memorial Highway, Hauppauge, NY 11788-5559 Phone: (516) 595-4233 Fax: (516) 435-8554</p> <p><b>Information Document Request</b></p> <p>Taxpayer name: [REDACTED] Audit years: 03/01/2020 - 02/28/2023 Identification number: [REDACTED] Case ID: [REDACTED] Auditor: Mrs. Kanichia Osbourne Articles: 28 &amp; 29 Requested on: [REDACTED] Date requested: March 22, 2023 Date(s) provided/copies completed by: [REDACTED]</p> <p><b>Your response is due by: 04/05/2023</b></p> <table border="1"><thead><tr><th>Description of documents and information requested</th><th>Name</th><th>Federal/Proprietor</th></tr></thead><tbody><tr><td>1. Sales tax returns, worksheets, and canceled checks showing taxes paid</td><td></td><td></td></tr><tr><td>2. Federal income tax returns (Forms 1120, 1065, or 1040)</td><td></td><td></td></tr><tr><td>3. New York State corporation tax returns</td><td></td><td></td></tr><tr><td>4. General ledger</td><td></td><td></td></tr><tr><td>5. Year-end trial balance</td><td></td><td></td></tr><tr><td>6. Year-end financial statements</td><td></td><td></td></tr><tr><td>7. General journal and closing entries</td><td></td><td></td></tr><tr><td>8. Sales invoices</td><td></td><td></td></tr><tr><td>9. All exemption documents supporting non-taxable sales, including: • resale, exempt use, exempt organization, and capital improvement certificates • any other documentation necessary to prove non-taxable sales</td><td></td><td></td></tr><tr><td>10. Chart of accounts</td><td></td><td></td></tr><tr><td>11. Fixed asset purchase/sales invoices</td><td></td><td></td></tr><tr><td>12. Expense purchase invoices</td><td></td><td></td></tr><tr><td>13. Merchandise purchase invoices</td><td></td><td></td></tr></tbody></table> <p><small>Taxpayers are required to make all books and records available to the auditor, and they must remain available until the audit is complete, unless the auditor indicates that the records are no longer needed. An entry in the right column does not necessarily indicate that this portion of the request has been fully satisfied.</small></p>	Description of documents and information requested	Name	Federal/Proprietor	1. Sales tax returns, worksheets, and canceled checks showing taxes paid			2. Federal income tax returns (Forms 1120, 1065, or 1040)			3. New York State corporation tax returns			4. General ledger			5. Year-end trial balance			6. Year-end financial statements			7. General journal and closing entries			8. Sales invoices			9. All exemption documents supporting non-taxable sales, including: • resale, exempt use, exempt organization, and capital improvement certificates • any other documentation necessary to prove non-taxable sales			10. Chart of accounts			11. Fixed asset purchase/sales invoices			12. Expense purchase invoices			13. Merchandise purchase invoices			<p>Audit Period 03/01/2020 - 02/28/2023</p> <table border="1"><tbody><tr><td>14. Bank statements, canceled checks, and deposit slips for all accounts</td><td></td></tr><tr><td>15. Cash receipts journal -- including sales journal, if applicable</td><td></td></tr><tr><td>16. Cash disbursement journal -- including purchase journal, if applicable</td><td></td></tr><tr><td>17. The corporate book, including minutes, board of directors, and articles of incorporation</td><td></td></tr><tr><td>18. Depreciation schedules</td><td></td></tr><tr><td>19. Lease/Rental Agreements</td><td></td></tr></tbody></table> <p>AU-800 Page 2 of 2 3/22/2023 </p>	14. Bank statements, canceled checks, and deposit slips for all accounts		15. Cash receipts journal -- including sales journal, if applicable		16. Cash disbursement journal -- including purchase journal, if applicable		17. The corporate book, including minutes, board of directors, and articles of incorporation		18. Depreciation schedules		19. Lease/Rental Agreements	
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# Questionnaires

**New York State Department of Taxation and Finance**  
**Sales Tax Examination Questionnaire** DO-1632

Business name and address:  
City: \_\_\_\_\_ State: \_\_\_\_\_ Zip: \_\_\_\_\_

If you have any of the following identification (ID) numbers, enter them in the spaces below:  
 Sales Tax ID number: \_\_\_\_\_  
 Federal Tax ID number: \_\_\_\_\_  
 Corporation Tax ID number: \_\_\_\_\_

Print or type your answers to the following questions. Attach additional sheets if necessary.

1. Where should we contact to reach our examination?  
 Name: \_\_\_\_\_  
 Position: \_\_\_\_\_  
 Title: \_\_\_\_\_ Telephone number: \_\_\_\_\_

2. What type of products or services does your company sell or provide?  
 \_\_\_\_\_

3. Did you acquire this business (or assets of a business) from a registered sales tax vendor?  
 Yes ☐ No ☐  
 If yes, have you filed Form ST-105.10, Notification of Sale, Transfer or Assignment with the Tax Department?  
 Yes ☐ No ☐  
 Please attach sales tax returns: \_\_\_\_\_

4. Does your company have a sales unit?  
 Yes ☐ No ☐  
 If yes, provide sales address: \_\_\_\_\_

5. Does your company make sales through this Web site?  
 Yes ☐ No ☐  
 If yes, complete the following:  
 Name of affiliated company: \_\_\_\_\_ Web address: \_\_\_\_\_ Telephone: \_\_\_\_\_

6. Do you make tax exempt sales?  
 Yes ☐ No ☐  
 If yes, what is the basis for exemption? (over or in what state?)  
 Exemption provided exemption certificate: \_\_\_\_\_ Sales returned out of state: \_\_\_\_\_  
 Sales are not taxable: \_\_\_\_\_ Explain: \_\_\_\_\_  
 Other: \_\_\_\_\_ Explain: \_\_\_\_\_

7. Are there seasonal or other fluctuations in sales?  
 Yes ☐ No ☐  
 If yes, explain: \_\_\_\_\_

**New York State Department of Taxation and Finance**  
**Responsible Person Questionnaire** AU-431

Business name: \_\_\_\_\_  
 Complete a questionnaire for each responsible person of the business.

Sales tax identification number: \_\_\_\_\_ Date: \_\_\_\_\_ Period: \_\_\_\_\_

**Identification section**  
 Name of responsible person: \_\_\_\_\_ Social security number: \_\_\_\_\_  
 Title: \_\_\_\_\_ Physical mailing address: \_\_\_\_\_  
 Period served: \_\_\_\_\_ Percent of time devoted to business: \_\_\_\_\_

For the person named above, mark an X in the appropriate box for each item below.

	Yes	No	Not applicable or unknown
1. Is he or she responsible for preparing or supervising the preparation of sales tax returns and ensuring the remittance of tax?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
2. Does he or she participate in making significant business decisions?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
3. Is he or she responsible for maintaining and managing the business?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
4. Does he or she own: • corporate stock? • voting stock?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
5. Does he or she derive substantial income or have a substantial economic stake in the business?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
6. Does he or she have authority to: • manage the business with knowledge and control over financial affairs? • pay or direct payment of bills or other business liabilities? • sign checks? • act on behalf of the business, with the Tax Department? • sign contracts extending periods of litigation? • sign power of attorney for the business? • sign contracts listing him? • sign treatment agreements? • hire and fire employees? • negotiate loans, borrow money for the business, or guarantee business loans.	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

7. Describe any additional responsibilities not listed above:  
 \_\_\_\_\_  
 \_\_\_\_\_

(Continued on back page)

# Areas to be Reviewed on Audit

- Auditors look at a few key areas:
  1. Tax reconciliation
  2. Expenses - usually recurring - use of test period or statistic sample preferred.
  3. Sales - usually sampled, depends on level of sales activity: guest checks - register tapes - taxable ratio.
  4. Capital acquisitions - full detail usually preferred, items usually reconciled with cash disbursements journal and federal depreciation schedule.

# Audit Methodology

## ▪ Audit Methodology

### 1. Direct Audit

- What qualifies as “adequate records?”
- Typical for non-cash businesses
- Test Period Consent

### 2. Indirect or Estimated Audit Methodologies

- Records must be requested and deemed inadequate
- Observation Test
- Purchase Markup Test
- Cash to Credit Card Test
- Industry Indices Test (e.g., rent to sales ratio)
- Beware income tax issues!



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# Major Audit Issues

## ▪ Major Audit Issues:

1. Where to hold audit
2. Responsible officer questionnaire
  - LLCs be especially careful
3. Access to information
4. Consent to extend
5. Statute of Limitations

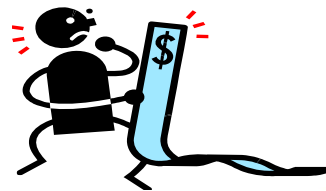


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# Concluding an Audit

- Concluding An Audit

1. Audit Work Papers
2. Presumption of Correctness and Burden of Proof Issues
3. Penalties:
  - i. Failure to file (max 30% of tax due),
  - ii. Substantial Understatement (10% of amount omitted)
  - iii. Fraud (200% of tax due)
  - iv. interest (14.5%) Closing Agreements
4. Follow-Up Audits



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# Mitigation Strategies

- Issues to review to mitigate audit liabilities:

1. Customer paid use tax, direct pay permits, etc.?
2. Customer or transaction exempt?
3. Overlapping audit policy?
4. Chargeback customer? Six year statute of limitations on contract claims. May not be the best business decision.

- Send the customers an XYZ letter inquiring about these issues.

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## Section 4: Abandoned Property: A Possible Budgetary Balm

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## Abandoned Property: General Rules

### ■ General Information

1. All 50 states, the District of Columbia and 3 Canadian provinces (Alberta, British Columbia, and Quebec) have enacted unclaimed property laws. Ontario proposed unclaimed property legislation in its 2012 budget.
2. Unclaimed property laws are intended to safeguard the property of a state's citizens, while utilizing the escheated property for the benefit of all citizens.
3. States have increasingly turned to their unclaimed property laws to increase revenue without raising or extending taxes, which is politically unpopular.
4. States' Unclaimed property laws apply to all entity types, including:
  - Corporations;
  - S Corporations;
  - Partnerships; and
  - Limited Liability Companies



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# Abandoned Property: General Rules (cont.)

## ■ General Information

1. As you might expect, NYS is known as one of the more aggressive states for abandoned property purposes.
2. In fact, the Council on State Taxation ("COST") recently gave NY its lowest grade when comparing the aggressiveness of the abandoned property laws across the 50 states. Only NY, DE and MS received a grade of "D-".
3. Here is a sampling of some of the states in the Northeast:
  - CT : B-
  - MA: A
  - MD: B+
  - NH: D
  - NJ: D
  - PA: D
  - VT: C-

# General Rules: Definitions

## "Unclaimed Property"

- Unclaimed property generally includes property for which there has been no contact between the owner and holder for a statutorily prescribed period of time ("dormancy period").
- Common categories include:
  - Wages, payroll, salaries, commissions, pension payments
  - Uncashed payable/vendor checks
  - Gift certificates/gift cards/stored value cards
  - Customer credits, deposits, refunds or rebates
  - Overpayments/unidentified balances
  - Cash and stock dividends
  - Merger redemption proceeds
  - Underlying and unexchanged shares
  - Bond principal and interest
  - Mutual fund and dividend reinvestment plan book shares, physical shares, and associated distributions

# Compliance: Sourcing Rules

The Supreme Court of the United States in *Texas v. New Jersey*, established the following two-pronged unclaimed property sourcing rule:

- The state in which the owner's last known address is located has the power to escheat the unclaimed property, but;
- If that state does not have a law covering the property or if there is no record of the last known address, then the state in which the holder is incorporated has the power to escheat the unclaimed property.



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# Compliance: Sourcing Rules (cont.)

- Reporting organizations incorporated, chartered, organized, or domiciled (in the case of a federally-chartered bank) in New York are required to report all amounts and securities held for:
  1. New York residents,
  2. foreign owners, and
  3. unknowns.
- New York incorporated life insurance companies are required to report amounts payable to New York residents and unknowns.
- All other reporting organizations are required to report amounts held for New York residents only.



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# Compliance: Reporting

## ▪ Aggregate Reporting

- Many states allow holders to report smaller amounts of unclaimed property in the aggregate in order to ease compliance burdens.
- In NY, all amounts are reportable (there is no minimum threshold). However, holders may report certain property valued at \$20 or less per owner in aggregate. If detailed information is available for aggregate accounts, holders are asked to attach it to the report to better serve claimants with small values.

## ▪ Negative Reporting

- States may require holders of unclaimed property to file a negative report to confirm that they do not have any unclaimed property on their books and records.
- Be cautious of not engaging in negative reporting – it can keep statutes of limitations open. Consequently, some businesses choose to file a zero report.
- The NYS Abandoned Property Law does not require organizations to file negative reports.

# Compliance: NY Due Diligence

- New York requires holders to attempt to contact owners prior to remitting the property to the state.
- This is known as “due diligence.”
- NY due diligence requires:
  1. First mailing for all property regardless of value at least 90 days before reporting.
  2. Second mailing via certified letter for all property of \$1,000 or more at least 60 days prior to reporting.



# Compliance: Reporting

- For Traditional Business Corporations
- Filing Date: 3/10
- Covers Property Abandoned as of: 12/31 of the preceding year
- Due Diligence:
  - First Mailing: 12/10 of the preceding year
  - Second Mailing: 1/10 (for accounts over \$1,000)
- Penalties : Willful failure to report penalty is \$100 a day for every day the report is late
- Interest: 10% simple interest
- No COVID update or change from usual filing extension procedures

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# Voluntary Disclosure

- New York offers a voluntary disclosure program that allows holders to come forward (anonymously at first) and remit unclaimed property. However, participants usually have to satisfy the following requirements:
  - Holder has not been previously contacted by the state regarding unclaimed property audit;
  - The applicant is a first time filer and has not participated in a voluntary disclosure previously (In some cases those who filed in the past may once again apply through this program if they failed to report a particular type of property and want to voluntarily correct the error);
  - Holder comes forward (often times anonymously in the beginning) in good faith to report unclaimed property liabilities.

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## Voluntary Disclosure (cont.)

### ▪ Advantages

- Limited lookback of 10 years of liability;
- Eliminates penalty and interest (10% per annum in NYS);
- The holder gets to take a "first crack" at fixing the liability;
- Indemnification from owners and states; and
- Ability to re-evaluate or even release reserves.

### ▪ Disadvantages

- Though the lookback is limited, it still reaches back a significant number of years.
- Pandora's Box: The state may not agree with the holder's liability calculation.
- Coming forward will likely put the state on notice about other related entities.



## Thank You

Call or email with questions!



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