



JULY 2022

# THE BR STATE + LOCAL TAX SPOTLIGHT **BLANKROME**



CONTENTS

1. Note from the Editors
2. New Jersey's Unconstitutional Penalties for Transfer Prices Should Fail!
3. Appellate Division Holds That Existence of Vacation Home Not Enough to Establish Statutory Residency in New York
4. New York State Tax Department Releases Final Draft Corporate Tax Apportionment Regulations
5. What's Shaking: Blank Rome State + Local Tax Roundup

## STATE + LOCAL TAX TEAM:

Craig B. Fields | [craig.fields@blankrome.com](mailto:craig.fields@blankrome.com)  
Nicole L. Johnson | [nicole.johnson@blankrome.com](mailto:nicole.johnson@blankrome.com)  
Mitchell A. Newmark | [mitchell.newmark@blankrome.com](mailto:mitchell.newmark@blankrome.com)  
Irwin M. Slomka | [irwin.slomka@blankrome.com](mailto:irwin.slomka@blankrome.com)  
Eugene J. Gibilaro | [eugene.gibilaro@blankrome.com](mailto:eugene.gibilaro@blankrome.com)

Kara M. Kraman | [kara.kraman@blankrome.com](mailto:kara.kraman@blankrome.com)  
Philip M. Tatarowicz | [phil.tatarowicz@blankrome.com](mailto:phil.tatarowicz@blankrome.com)  
Madison A. Ball | [madison.ball@blankrome.com](mailto:madison.ball@blankrome.com)  
Anna Uger | [anna.uger@blankrome.com](mailto:anna.uger@blankrome.com)

## Note from the Editors

By Eugene J. Gibilaro and Anna Uger

---

**Welcome to the July 2022 edition of *The BR State + Local Tax Spotlight*.** We understand the unique demands of staying on top of important State + Local Tax developments, which happen frequently and across numerous jurisdictions. Staying updated on significant legislative developments and judicial decisions helps tax departments function more efficiently and improves strategy and planning. That is where *The BR State + Local Tax Spotlight* can help. In each edition, we will highlight for you important State + Local Tax developments that could impact your business. In this issue, we will be covering:

- The New Jersey Division of Taxation Audit Branch's recent initiative to resolve state transfer pricing issues;
- A New York Appellate Division decision that a New Jersey resident's vacation home in upstate New York was not sufficient to establish statutory residency in New York; and
- The New York State Department of Taxation and Finance's final draft of corporate tax apportionment regulations that updates guidance on the state's Corporation Franchise Tax.

**We invite you to share *The BR State + Local Tax Spotlight* with your colleagues and visit Blank Rome's State + Local Tax [webpage](#) for more information about our [team](#). Click [here](#) to add State + Local Tax to your subscription preferences.**

---

### Co-Editors, *The BR State + Local Tax Spotlight*

#### **EUGENE J. GIBILARO**

Of Counsel

212.885.5118

[eugene.gibilaro@blankrome.com](mailto:eugene.gibilaro@blankrome.com)



#### **ANNA UGER**

Associate

212.885.5473

[anna.uger@blankrome.com](mailto:anna.uger@blankrome.com)

---



MITCHELL A. NEWMARK

PARTNER

## New Jersey's Unconstitutional Penalties for Transfer Prices Should Fail!

By Mitchell A. Newmark

New Jersey, in advance of examining the facts and the issues, has said it refuses to do its job of auditing and resolving tax disputes involving transfer pricing without imposing penalties unless you do the job for them, do it fast, and do it their way—and all appeal rights are waived. This creates clear violations of State and Federal Due Process, the Manifest Injustice doctrine, and the mandate that government turn “Square Corners” when dealing with taxpayers.

The Audit Branch is opening a transfer pricing initiative in which it will welcome applications to disclose and resolve state transfer pricing issues. For taxpayers that come forward, New Jersey agrees to:

- use principles of IRC Section 482 and its related-party adjustment authority (a big win because the author sat in a Trenton meeting during which the Division of Taxation (“Taxation”) said New Jersey was not bound by Section 482!);
- waive penalties; and
- close settled years.

This sounds a lot like the job Taxation is charged with doing, regardless of conducting a focused initiative on transfer pricing issues.

Further, if you do not come forward or you come forward and think you are getting a raw deal (or just don’t want to waive appeal rights), Taxation says, without regard to your facts or circumstances, it will:

- apply penalties;
- not waive penalties; and
- “will not agree to a methodology or settlement for any unaudited open tax years.”

If you settle, all payments are final and appeal rights are waived. Therefore, you cannot pay to protect under the program to avoid penalties and continue your dispute. If New Jersey wants to continue the dispute, you do not get to add penalties to them when you win.

Due Process requires that taxpayers have an opportunity to be heard (the requirements are found in the Federal and New Jersey State Constitutions). The New Jersey Supreme Court said in my Amnesty Penalty win in 2014 that the penalty for

not paying up in advance cannot stand when you paid the good faith correct amount initially with your return. The imposition of a penalty for not playing New Jersey’s way violates Due Process and cannot be correct.

Taxpayers in New Jersey have two more defenses—the Manifest Injustice doctrine and the Square Corners requirement. That is, even if actions do not violate Due Process, they can still be manifestly unjust (*i.e.*, inequitable) especially when the harm is retroactive. New Jersey’s penalty and non-waiver

### **New Jersey’s imposition of a penalty for not coming forward is a bargaining or litigation advantage that is prohibited by the Square Corners Doctrine.**

will be applied retroactively to years in dispute long after the window to participate in the transfer pricing program has closed.

It is inequitable and it is wrong.

The Square Corners Doctrine requires that government turn square corners when dealing with taxpayers. It may not conduct itself to achieve or preserve a bargaining or litigation advantage even if it means that the government may have to forego the freedom of action that private litigants may employ in dealing with one another. New Jersey’s imposition of a penalty for not coming forward is a bargaining or litigation advantage that is prohibited by the Square Corners Doctrine.

The transfer pricing “invitation” expires on September 15, 2022, information must be provided by October 31, 2022, then Taxation will make a proposal for payment for which Taxation gives you “30 days to accept our proposal.” If you counter New Jersey’s proposal, you still have only 30 days to get agreement (extensions are at New Jersey’s discretion).

My mentor Paul Frankel’s words ring ever more loudly: “Don’t Pay, Don’t Pay, Don’t Pay!” □



KARA M. KRAMAN

OF COUNSEL

## Appellate Division Holds That Existence of Vacation Home Not Enough to Establish Statutory Residency in New York

By Kara M. Kraman

The Appellate Division recently granted taxpayers an important victory when it overturned the decision of the Tax Appeals Tribunal and held that a New Jersey resident's vacation home in upstate New York was not enough to establish his statutory residency in New York. *In re Obus v. Tax Appeals Trib.*, No. 04206 (N.Y. App. Div. June 30, 2022).

Mr. Obus, a resident and domiciliary of New Jersey, worked in New York City and owned a vacation home in upstate New York. Under New York law, a person may be considered a statutory resident if he or she maintains a "permanent place of abode" in New York *and* spends more than 183 days in New York State during the year. N.Y. Tax Law § 605(b)(1)(B). There was no dispute that Mr. Obus met the 183-day threshold for time spent in New York due to his employment in New York City. However,

**The case is a significant victory for taxpayers because the Appellate Division held that in determining whether a vacation or other second home is a "permanent place of abode," the Department must undertake a subjective analysis of the use of the property and may not just rely on an objective evaluation of the potential use of a property.**

the parties disputed whether Mr. Obus's home in upstate New York, which was more than 200 miles from his place of employment constituted a "permanent place of abode" for statutory residency purposes.

The Tax Appeals Tribunal determined that Mr. Obus's vacation home constituted a "permanent place of abode" for statutory residency purposes because Mr. Obus

maintained the home for year-round use and had exercised that right of use, "albeit sparingly, during the years at issue." *Obus*, No. 04206, at \*1. The Appellate Division disagreed, noting that in order to establish statutory residency, the person must be shown to "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." *Id.* at \*4. The Appellate Division explained that in order to determine whether a dwelling is used as a residence, a number of factors must be considered, "including the nature and duration of the use." *Id.* at \*5. In this case, the Appellate Division held that the Mr. Obus's use of the residence for at most three weeks a year, its 200-mile distance from Mr. Obus's place of employment, and the fact that Mr. Obus did not keep personal effects at the upstate

home, established that he did not use the dwelling in a manner that demonstrates he had a residential interest in the property.

The case is a significant victory for taxpayers because the Appellate Division held that in determining whether a vacation or other second home is a "permanent place of abode," the Department must undertake a subjective analysis of the use of the property and may not just rely on an

objective evaluation of the potential use of a property. The Appellate Division expressly recognized that not all vacation homes that are inhabitable year-round will rise to the level of permanent place of abode. As such, this case and its holding has the potential to be very helpful to those challenging findings of statutory residency based on their maintenance of a second home in New York State. □



IRWIN M. SLOMKA

SENIOR COUNSEL

## New York State Tax Department Releases Final Draft Corporate Tax Apportionment Regulations

By Irwin M. Slomka

Since the enactment of New York State corporate tax reform beginning in 2015, the New York State Department of Taxation and Finance (the “Department”) has been periodically posting for comment draft regulation sections interpreting the law. Things took a decidedly more accelerated turn when, this past April, the Department posted two sets of revised “final drafts” covering all topics except apportionment, and announced that it would be posting a final draft of the apportionment regulation sections by this summer. On July 1, 2022, the Department posted the revised apportionment regulations, combining into one final draft what had been three separate sets of regulation sections, which were last updated in 2019.

The newly-released draft apportionment regulations are now broken down into four subparts: (i) General (including discretionary adjustments to the apportionment factor); (ii) Specific Apportionment Rules (17 categories, including net gains from sales of real property and receipts from securities broker-dealer sourcing); (iii) Digital Products and Digital Services (such as rules for determining primary use location and reasonable approximations); and (iv) Other Services and Other Business Activities (addressing the sourcing of receipts and net gains from services and other business activities not otherwise enumerated in the tax law).

Given the broad scope of the apportionment regulations, these latest revisions are surprisingly modest. Among the new revisions are the following:

- With respect to both digital products and other business services and activities, a “billing address safe harbor” has been added for a corporation having more than 10,000 business customers purchasing substantially similar products and services (where no more than 5 percent of those receipts are from a particular customer), whereby

that the “primary use location” of the product or service is presumed to be the customer’s billing address.

- Now defines a “digital product”—the receipts from which are sourced under a hierarchy, primarily at the customer’s “primary use location”—to include cryptocurrency.
- Substantially changes the rule for “services” provided to “passive investment customers”—defined generally as non-corporate collective investment vehicles that do “not otherwise conduct a trade or business”—presuming the benefit to be received by the customer “where the contract is managed” by the customer. The prior draft applied to management and advisory services, but not to accounting, legal and similar services, and sourced the receipts based on where the customer “makes the decision to utilize the investment or management decisions.”
- Elaborates on the sourcing of lump sum payments received (*e.g.*, when a sale consists of both a digital product and a digital service, the receipt is considered one receipt even if separately stated for billing purposes).

**The Department’s decision earlier this year to finally proceed toward promulgating corporate tax reform regulations is a much needed and long overdue step.**

The Department is requesting comments on the new draft by August 26, 2022. It anticipates commencing the formal promulgation process under the State Administrative Procedure Act by the end of 2022. This would likely mean that the regulations would be effective sometime next year. It has been more than eight years since New York State corporate tax reform was enacted, with no regulatory guidance in place throughout that time. The Department has consistently cautioned that taxpayers could not rely on its posted draft regulations. Its decision earlier this year to finally proceed toward promulgating corporate tax reform regulations is a much needed and long overdue step. □

## What's Shaking: Blank Rome's State + Local Tax Roundup

Blank Rome's nationally prominent State + Local Tax attorneys are thought leaders in the community as frequent guest speakers at various local and national conferences throughout the year. Our State + Local Tax attorneys believe it is necessary to educate and inform their clients and contacts about topics that will impact their businesses. We invite you to attend, listen, and learn as our State + Local Tax attorneys interpret and discuss key legal issues companies are facing and how you can put together a plan of action to mitigate risk and advance your business in accordance with state and local tax laws.

### 29th Annual Paul J. Hartman State and Local Tax Forum

- ▶ [Craig B. Fields](#) and [Nicole L. Johnson](#) will speak at Vanderbilt University Law School's 29th Annual Paul J. Hartman State and Local Tax Forum, being held October 19 through 21, 2022, in Nashville, Tennessee. There will also be a virtual option available for all program sessions. Craig will speak on the "Leading Practices in Audits, Assessments, and Alternative Dispute Resolutions" panel, taking place Wednesday, October 19. Nicole's session, "Allocable Income," will take place the next day, Thursday October 20. To learn more, please click [here](#). □

### Council of State Taxation's North Atlantic Regional State Tax Seminar

- ▶ [Craig B. Fields](#), [Eugene J. Gibilaro](#), [Nicole L. Johnson](#), and [Mitchell A. Newmark](#) will speak at the Council of State Taxation's North Atlantic Regional State Tax Seminar being held on September 20, 2022, from 8:30 a.m. to 3:30 p.m. EDT, in Blank Rome LLP's New York office. The seminar will provide updates on significant state tax issues for the North-Atlantic States: Connecticut, Maine, Massachusetts, New Hampshire, New Jersey, New York, Rhode Island, and Vermont. To learn more, please click [here](#). □

### New Jersey State and Local Tax Day

- ▶ [Eugene J. Gibilaro](#) and [Mitchell A. Newmark](#) will speak at the New Jersey State Bar Association's New Jersey State and Local Tax Day being held September 15, 2022, via webinar. Mitchell and Eugene's topic is "State of the States Litigation." To learn more, please click [here](#). □

### California Lawyers Association

- ▶ [Nicole L. Johnson](#) will serve as a speaker for California Lawyers Association's "State and International Digital Service Taxes" webinar being held Tuesday, July 26, 2022, from 12:00 to 1:30 p.m. PDT. The panel will discuss the latest state and international trends surrounding the taxation of digital services. MCLE credit is available. To learn more, please click [here](#). □

### NYU Advanced Subchapter S Conference

- ▶ [Mitchell A. Newmark](#) and [Eugene J. Gibilaro](#) will serve as speakers for the NYU Advanced Subchapter S Conference, part of the School of Professional Studies Tax Conferences in July, being held July 21 through 22, 2022, in New York, New York. Mitchell and Eugene's session, "Advanced Subchapter S: State and Local Income Taxation of Pass-Thru Entities," will take place on Thursday, July 21, from 1:15 to 2:45 p.m. CLE credit may be available. To learn more, please click [here](#). □