Multistate Tax Update - July 16, 2015

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South Carolina: Gov. Haley approves budget for fiscal year 2015-16

South Carolina's General Assembly ratified its budget bill H. 3701 for fiscal year 2015-16, overriding some of Gov. Nikki Haley's vetoes. The budget is not quite final though; the South Carolina Policy Council (SCPC) pointed out that on July 6, lawmakers returned for a third week of extended session.

According to the *Aiken Standard*, budget highlights include:

- **Roads:** The budget distributes $216.3 million to counties for repair of existing roads. $70 million will partially fund promised roadwork for Volvo's future plant. $50 million will sit in an account for future borrowing, which cannot be used until the legislature passes a long-term fix for roads.
- **State employees:** $23.5 million provides a one-time, $800 bonus to state employees who make less than $100,000, to be paid in October. Another $34.4 million will cover increases in employees' health insurance premiums.
- **School buses:** The budget allocates a minimum of $21 million for new buses, but depending on lottery revenues, as much as $31 million could be available.
- **Department of Social Services:** $8.5 million is to be used to hire 262 employees, mostly caseworkers and assistants, and to provide pay raises of up to 15 percent to help with retention.
- **Body cameras:** $3.4 million will go into a fund that law enforcement agencies can apply to for their officers' cameras.
- **Medical University of South Carolina:** $25 million is apportioned toward a new, $350 million children's hospital.
- **South Carolina State University:** $4 million will be deployed to pay down some of the financially struggling school's unpaid bills.

WISTV.com noted that Gov. Haley vetoed 87 budget items worth about $30 million minutes before her deadline was up. These vetoes mostly concerned projects that are already funded from other sources. For example, according to the governor's staff, a $4.5 million evacuation route through Horry and Georgetown Counties is already paid for through the Department of Transportation.

The SCPC is critical of this year's "sloth-like pace" of the budget process; the group points to the fact that July 1, the start of the new fiscal year, came and went without a final budget. This even though lawmakers have just "one clear task to accomplish every year: pass a state budget."

Two problems the group cited are lawmakers' refusal to consider the executive budget in joint open hearings at the beginning of session and their "tradition of wasting time on floor introductions and symbolic or otherwise pointless resolutions."

In addition, the budget process has turned into a vehicle for addressing every policy issue facing South Carolina. "In other words, lawmakers try to pass measures that won't otherwise pass by putting them into the state budget."

The SCPC highlighted difficulties with transportation, education, and healthcare as three especially thorny areas. With respect to transportation, by only addressing it as a revenue problem and avoiding reforms that could improve infrastructure in a sustainable manner, lawmakers have been unable to overcome disagreements over tax and fee increases.

Education became an issue in November 2014 when the South Carolina Supreme Court ruled that the state was failing to meets its constitutional obligation to provide “the requisite educational opportunity.” SCPC claims that because there is no evidence that funding increases improve education outcomes, lawmakers should reconsider the underlying educational policy. More specifically, they should implement a school-choice system involving vouchers or tax credits and tax credit scholarships, because the “failure of public schools doesn’t stem from a lack of resources but from their nature as quasi-monopolies that feature one-size-fits-all curricula.”

Finally, the SCPC disparages lawmakers’ Medicaid expansion. It draws attention to the fact that South Carolina’s Department of Health and Human Services (DHHS), which administers the state’s Medicaid program and is largely funded by the federal government, will receive a $116 million funding increase in fiscal year 2016. Additionally, over $42 million in the DHHS 2016 budget is specifically designated to cover the cost of increased enrollment in Medicaid.

SCPC insists there were no bills to repeal any of the 30 different insurance coverage mandates that increase health insurance costs. Nor was there traction on the repeal of the certificate-of-need laws, which require medical providers to get government approval before offering new medical services, purchasing certain medical equipment, or generally expanding the size of a healthcare facility.

While the SCPC acknowledges budgetary action that could improve healthcare reform, it decries the lack of effort on that front as well.

Ultimately, SCPC would like to see open debate where the budget is concerned, along with budget details that address South Carolina’s financial needs only. The budget is not a “tool for policy changes that might prove unpopular or politically difficult to pass openly.”

New York: Division of Tax Appeals concludes that taxpayer is domiciled in New York, not Florida

In 2011, the New York Division of Taxation (NYDOT) issued a notice of deficiency to a taxpayer, asserting that he owed nearly $500,000 of additional personal income taxes for 2007, plus negligence penalties and interest. This stemmed from the NYDOT’s decision that the taxpayer was residing in New York in 2007, and thus was subject to New York state and city income taxes.

The taxpayer argued that he was a Florida resident, and was not subject to New York tax laws, but in a case that finally concluded last month, he was not able to prove by clear and convincing evidence that he was a non-resident.

Background

The taxpayer was born in Italy in 1930 and eventually moved to New York. In 1975 the taxpayer started a furniture business in New York. In 1981, he opened a showroom in Miami and also purchased an apartment in Key Biscayne, Florida. He continues to reside there when he is in Florida.

The taxpayer’s furniture business grew, and he began to invest in rental real estate in New York and Florida. Since 1975, the taxpayer has handled the administrative and bookkeeping functions of his furniture business (as well as his Florida corporations) in New York City. The tax filings for the Florida businesses contain a New York address. The taxpayer had long maintained a travel pattern of flying to Florida on Friday and returning to New York on Tuesday.

In 2007, the taxpayer sold one of his Florida properties for more than $6.5 million, realizing a long-term capital gain of $5.3 million. Some time after December 2007, the taxpayer filled out a New York state tax form indicating that his address was in Key Biscayne, that his county of residence and school district were in New York—but also that he did not maintain living quarters in New York in 2006.

For the 2007 tax year, he filled out a non-resident and part-year resident income tax return, on which he indicated his address was in Key Biscayne. Once again, he also checked “No” to the question “Did you or your spouse maintain living quarters in New York State in 2007?”

The NYDOT's audit

In 2010, the NYDOT conducted an audit of the taxpayer’s 2007 return. Pursuant to the audit, he declared that he was present in New York for 150 work days and 10 non-work days in 2007. The NYDOT sought documentation to substantiate this claim, which the taxpayer provided but ultimately, the auditor determined it to be insufficient proof to establish his non-residency. The auditor calculated that the taxpayer had actually been present in New York for 169 days in 2007, 150 of which were work days. This, combined with an extensive analysis of the documentation, lead to the conclusion that the taxpayer had failed to show that he had abandoned his New York residence and acquired a new residence in Florida for that year. The NYDOT calculated a total New York tax liability of $488,718, plus interest and negligence penalties of 5 percent plus 50 percent of the interest due.

Competing positions

At the hearing, the taxpayer presented various summary documentation intended to verify his claims. The taxpayer also claimed that while *his* residence was in Key Biscayne, his wife’s residence was in New York, and that he commuted between New York and Florida regularly to spend time with his family in New York.

The NYDOT contended that the limited facts supporting the taxpayer’s position were offset by the many others that indicated that he retained his New York residence. The factors weighing most heavily against the taxpayer were his:

1. Retention and continued use of this New York residence;
2. Unchanged habit of commuting between New York and Florida;
3. Sustained levels of time spent in New York; and
4. Active business ties in New York.

The NYDOT recognized the well-established legal principle that an existing residence continues until a new one is established, the evaluation of which “frequently depends upon a variety of circumstances which differ as widely as the peculiarities of individuals.” The test is “whether the place of habitation is the permanent home of a person, with a wide range of sentiment, feeling and permanent association with it,” ascertained in part by one’s “general habit[s] of life.”

In light of all of this, the NYDOT did not find the taxpayer’s position to be credible regarding his intent to make Key Biscayne his residence during the relevant years.

Cities look to a hotel tax to capitalize on demand during popular events

Philadelphia

The City of Brotherly Love saw big revenue opportunities when the Pope announced his September 2015 visit for the World Family of Meetings and when the Democratic National Convention chose to hold its July 2016 event there.

In mid-June, seeking to capitalize on the influx of visitors, Philadelphia’s City Council unanimously passed a bill allowing for the regulation and taxation—at a rate of 8.5 percent—of short-term rentals, reported *Philadelphia Magazine*. Councilman-at-large Bill Greenlee, at the behest of Mayor Michael Nutter, proposed the legislation in May, and the **law** went into effect on July 1. In so doing, Philadelphia squarely takes aim at Airbnb, the online marketplace that connects renters with people looking to share their properties for a fee, along with others that offer similar services. The new law also requires those who rent out their homes for more than 90 days to get a rental license and precludes rentals for more than 180 days annually.

The magazine explains that some, like the Greater Philadelphia Hotel Association, applaud the changes because they contend that not taxing or regulating Airbnb and others gives those venues an unfair advantage. On the other hand, hosts who merely rent out their rooms “say that they are nothing like a full-staffed hotel operation and are just trying to put a little extra money in their pockets.”

Before the legislation became law, the magazine pointed out that before now, such rentals constituted “lawbreaker wheeling and dealing in Philadelphia’s black market.” It quoted Councilman Greenlee as recognizing that demand for rooms will "hit the roof" during the above-mentioned events. He also wanted to “make sure that visitors, tenants, and landlords are protected…[his] legislation clarifies the rules for new and popular platforms like Airbnb, and ensures that everyone is paying their fair share toward the public services and goods that make Philadelphia a great place to visit.”

Cleveland

The Rock and Roll Capital of the World is the location for the July 2016 Republican National Convention, and it is now considering its own measures to apply its 3 percent **hotel tax** to short-term, online home rental services, revealed *The Plain Dealer*. During the week of the convention, the city expects 50,000 visitors.

For sales tax purposes, Cuyahoga County’s municipal code adopts the Ohio Revised Code’s definition of a hotel as an establishment with five or more rooms offering sleeping accommodations to the public. Cuyahoga County’s version of the law would have to be modified to fit the practices of short-term rental marketplaces.

The paper noted that Cuyahoga County has attempted to persuade Airbnb to collect and remit the sales tax, but that Airbnb ignored its request. The law director conceded that Cleveland’s hurdle is the “practical collection aspect.”

These practical enforcement issues notwithstanding, Airbnb stands to benefit from this kind of legislation because some of its competitors (like HomeAway, Inc.) do not have the capacity to collect taxes from renters. This was the subject of a lawsuit in early December 2014, in which HomeAway sued the city of San Francisco. As we **explained** at the time, the crux of the suit was the claim that an ordinance the city had passed regulating and taxing short-term rentals violated the Constitution’s Commerce Clause. HomeAway’s business is structured differently from Airbnb’s, such that its property owners are not in a position to collect and remit the taxes required by the ordinance.

In February of this year, the court dismissed HomeAway’s lawsuit.

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