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Personal Planning Strategies

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With Recent Court Decision, Out-of-State Owners of New York Houses Can Breathe Easier

A recent New York appellate court ruling has major implications for individuals who own a house in New York State but do not consider themselves New York State tax residents.

Under New York law, an individual who spends at least a portion of 183 or more days per year in New York State and owns a "permanent place of abode" in the state is considered a New York "statutory resident" and therefore subject to New York State income tax on his or her worldwide income even if he or she maintains a primary residence elsewhere.

In *Matter of Nelson Obus et al., v. New York State Tax Appeals Tribunal*, a New York appellate court considered the case of Nelson Obus, a New Jersey resident who owned a five-bedroom vacation house in New York's Adirondack Mountains. New York claimed that Obus was a statutory resident. Obus, who commuted into Manhattan for work, admitted to spending part of at least 183 days per year in the state, but he argued that his vacation house was not a "permanent place of abode." In past cases, New York courts have interpreted the term "permanent place of abode" broadly enough to encompass virtually any house. But the court sided with Obus, noting that the Adirondack house was more than 200 miles from his Manhattan office, Obus did not keep any personal effects at the Adirondack house, he had a tenant in an apartment unit on the vacation property, and he only spent about three weeks a year at the house. New York's tax agency may appeal the decision, but the state's highest court is not required to take the appeal.

The case is a clear win for non-New York residents who own houses in New York, but its exact implications are unclear. For example, can a commuter with a vacation house somewhere closer to New York City, like the Hamptons, or in New York City itself, avail himself of the same tax treatment? Future cases will offer more guidance. In the meantime, commuters from New Jersey, Connecticut and other states can breathe a little easier.

IRS Extends Deadline for Making Portability Election

Under current law, each individual can shield up to $12,060,000 from gift tax and/or estate tax. The tax code describes this as the “basic exclusion amount.” If a married individual dies without using his or her full basic exclusion amount, and it isn’t allocated to gifts on the deceased spouse’s death, the surviving spouse can “port” the unused exclusion to himself or herself by checking a box on the deceased spouse’s estate tax return.

But often, especially if no estate tax is owed, the surviving spouse does not file an estate tax return for the deceased spouse’s estate.

In late June, the Internal Revenue Service (IRS) issued Rev. Proc. 2022-32, which extends the time that a surviving spouse has to make the portability election from two years to five years. This is a significant development and will save some families millions of dollars in estate tax. Surviving spouses who fail to make a portability election within five years of a spouse’s death will have to seek a special accommodation from the IRS.

Rising Interest Rates Have Important Estate-Planning Implications

Each month, the IRS determines four interest rates that are relevant to estate planners. The first three rates, known as Applicable Federal Rates (AFRs), are the minimum interest rates that can be charged on intra-family loans: the short-term AFR applies to loans with terms shorter than three years, the mid-term AFR applies to loans with terms of less than nine but more than three years, and the long-term AFR applies to loans with terms longer than nine years. These rates are derived from the yields on U.S. Treasuries, and they fluctuate accordingly. A fourth rate, the Section 7520 interest rate, which is used to determine the present value of certain annuities (including annuities from grantor retained annuity trusts), life estates, and remainder or reversionary interests, is equal to 120% of the mid-term AFR.

Since last fall, these interest rates have risen significantly while the spread between the short-term AFR and the long-term AFR has compressed. In September 2021, the short-term AFR was 0.17% and the long-term AFR was 1.73%. In August 2022, the short-term AFR will be 2.88% and the long-term AFR will be 3.35% — a spread of just 47 basis points. Some estate-planning techniques are becoming more attractive as a result, while others are becoming less attractive. Please contact us if you would like to discuss possible estate-planning opportunities created by the current interest rate environment.

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