## insights



A Newsletter from Shumaker, Loop & Kendrick, LLP

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## Ohio Brightens its Bright-Line Test

hio has a brightline test (the "Test") for determining when an individual is domiciled in Ohio for

purposes of Ohio's income tax. A bright-line test is an objective test, which is one based upon factual criteria, rather than a subjective test, which is one based upon an individual's subjective intent. As more fully described below, Ohio recently amended its law to allow an individual



to spend an additional 30 days in Ohio (from 182 to 212 contact periods) without potentially being subject to the Ohio income tax.

By David J. Rectenwald

## Contact Periods. The

Test starts with the number of "contact periods" an individual has in Ohio during a tax year. The concept of "contact periods" is different than the number of days or nights spent in Ohio. Ohio law provides that an individual has one contact period in Ohio if:

- (a) The individual is away overnight from the individual's "abode" located outside of Ohio; and
- (b) While away overnight from that abode, such individual spends some portion (however minimal) of two consecutive days in Ohio.
- 2. Critical Number. Ohio law establishes one specific number of contact periods that is critical to the Test. Prior to 2015, that number was 182. Starting in 2015, that number was increased to 212. As more fully described below, this critical number determines how difficult it will be for an individual to prove that he or she was not domiciled in Ohio for income tax purposes in any particular tax year. If the individual has 212 or less contact periods in any given year, then the burden of proof will be fairly easy. If the individual has more than 212 contact periods, then the burden of proof will be much more difficult.
- 3. Irrebuttable Presumption. The Test purports to provide an irrebuttable presumption to any individual who files an Affidavit of Non-Residency (the "Affidavit") by May 31st of the following year verifying that the individual was "not domiciled in Ohio" and has had an abode located outside of Ohio for the entire year. Only those individuals who have



fewer than 213 contact periods during the tax year can file the Affidavit. However, it is very unclear how this presumption applies. Specifically, it is not clear what is meant by the statement that each individual makes in the Affidavit that he or she "was not domiciled in Ohio." Is an individual not domiciled in Ohio if he or she has 212 or fewer contact periods, or is an individual not domiciled in Ohio only if the individual is able to prove (by a preponderance of the evidence) that he



or she has more contacts in another state than he or she has in Ohio. This exact issue is currently being litigated in the Ohio Supreme Court case of *Cunningham v. Testa*, 138 Ohio St.3d 1476, 2014-Ohio-1765, and a decision is due out later this year. Until then, every individual should assume that the more onerous interpretation applies and that changing those domicile factors described below to another state is required to prove that he or she "was not domiciled in Ohio."

4. Rebuttable Presumptions. The Test creates certain rebuttable presumptions that clearly apply to those individuals who do not file an Affidavit. The Cunningham decision will determine if they also apply to those individuals who have filed an Affidavit. If they do, then an individual will only obtain an irrebuttable presumption if the individual can rebut the presumption against him or her. Having to rebut a presumption in order to obtain an irrebuttable presumption is indeed a very strange and nonsensical way to structure an irrebuttable presumption, which is exactly what the Cunninghams are arguing in their case. An individual who has fewer than 213 contact periods in any given vear is presumed to be domiciled in Ohio unless the individual can prove by a preponderance of the evidence that he or she is not domiciled in Ohio.

- An individual who has more than 212 contact periods in any given year is also presumed to be domiciled in Ohio unless the individual can prove by clear and convincing evidence that he or she is not domiciled in Ohio. The preponderance standard is generally considered to be a 51% test, while a clear and convincing standard is much tougher to quantify. It can vary from court to court, but it is roughly equal to a 75% test. Thus, an individual can satisfy the "preponderance" test by proving that a majority of the evidence supports such individual being domiciled in another state. An individual can satisfy the "clear and convincing" standard only by showing that about 75% of all of the evidence supports such individual being domiciled in another state. Therefore, it is significantly easier to satisfy the preponderance standard than it is the clear and convincing standard.
- 5. Domicile Factors. Ohio Administrative Code Section 5703-7-16(A)-(D) (the "Regulation") contains a laundry list of factors that the State will and will not examine when analyzing a person's domicile. The factors to be ignored include the location of certain professionals or entities used by or affiliated with the individual or the individual's spouse, such as their doctors, lawyers, accountants, bankers, insurance companies, charities, trustees and other fiduciaries, the location of their friends and family, or the recitation of domicile in any of their estate planning documents. The Regulation contains a very short list of factors that the State will consider. The State will consider the individual's number of contact periods for the year, the activities of the individual in the prior years and any other factors that

- the State deems relevant. According to Matthew Dodovich, Chief Legal Counsel for the Ohio Income Tax Division, the "other relevant factors" includes whether an individual has retained an Ohio residence, maintained the Ohio homestead exemption, retained an Ohio driver's license, remained registered to vote in Ohio and retained any business in Ohio. Thus, an individual should focus on these factors when moving his or her domicile out of Ohio.
- Audit of Contact Periods. If the State challenges the number of contact periods that an individual claims to have during a taxable year, then the individual bears the burden of proof to verify such number by a preponderance of the evidence. Such person is presumed to have a contact period in Ohio for any period in which the individual does not prove by a preponderance of the evidence that the individual has no such contact period. The Regulation contains a laundry list of writings and other evidence that the State will consider in an audit of contact periods. These include any evidence that shows where the person





- was in any particular day, including personal diaries, credit card receipts, utility bills and other records "tending to show the physical whereabouts of the individual." In practice, an individual's cell phone records are very strong evidence of the individual's physical presence and are often subpoenaed by the State.
- 7. Transition Year. The Test specifically does not apply during the year in which the individual changes his or her domicile. Such year is sometimes referred to as the "transition year." In the transition year, an individual is taxed as a resident of Ohio until the date of the domicile change. The individual is then taxed as a nonresident after such date. Thus, an individual who elects to change his or her domicile on November 1st of a year is taxed as an Ohio resident for the first 10 months and taxed as a non-resident for the last 2 months, even though such individual had more than 212 contact periods in Ohio during such year.
- 8. Audit Triggers. Mr. Dodovich has indicated to me that the filing of the Affidavit does not by itself trigger any audits. He indicated that the two primary audit triggers are:
  - (a) If an individual has a pattern of filing Ohio income tax returns and then suddenly stops. It is an even bigger red flag if the individual later starts filing Ohio returns again.
  - (b) If an individual files a nonresident Ohio return reporting Ohio-sourced income, particularly if the individual previously filed Ohio resident returns
- **9. Tips.** Set forth below is the list of tips based on all of this information and on my discussions with Mr. Dodovich:

- (a) Keep a Diary. By far the most persuasive evidence in establishing the number of contact periods is a diary of physical presence. It is extremely important to maintain this diary on a contemporaneous basis. It is very difficult to try to establish contact periods months or years after the year in question.
- (b) Use a Computer Diary. By far the most persuasive type of diary is one that is maintained on a computer software program such as Google Calendar or Microsoft Outlook.
- (c) Consider Filing an Affidavit.

  Many individuals who claim that they are not domiciled in Ohio have to make a tough decision annually on whether to file an Affidavit. The advisability of such a filing will depend largely on how the Ohio Supreme Court rules in Cunningham. This is a very complicated and important issue. Such individuals should talk this issue through with a qualified tax counsel.
- (d) Retain Evidence. A person should retain all evidence of domicile until the statute of limitations has run. The statute for Ohio income taxation is 4 years if an Ohio income tax return has been filed, or 10 years if one has not. Note that the State's position is that the Affidavit is not a tax return, so that the filing of an Affidavit without an Ohio income tax return does not start the statute of limitations.
- (e) Arrange Ties. Any individual seeking to become domiciled outside of Ohio should minimize his or her ties with Ohio and maximize his or her ties with another state. Voter registration

and driver's license should be changed to the desired state of domicile. The number of contact periods in Ohio should stay below 213. The Ohio homestead should be released and any homestead available in the desired state of domicile should be obtained. Significant additional contacts should be established in the desired state of domicile, including those described above.

## CONCLUSION

The increase in the number of contact periods under the Test from 182 to 212 will give many individuals with dual residences the opportunity to avoid Ohio income tax by changing their domiciles to another state. It will also give many other individuals who have already made the change significantly greater flexibility in spending time in Ohio. Nevertheless, for many other individuals the decision to convert their Ohio domicile to another state is an extremely difficult one, especially now when the core of the Test is in limbo and in the hands of the Ohio Supreme Court. The failure either to make the right decision or to make the conversion properly could result in a costly assessment of interest and penalties on top of years of unpaid Ohio income tax. The entire matter should be thought through carefully with the advice and assistance of an experienced tax advisor, and careful and persistent attention to detailed compliance should thereafter be maintained. If you would like to review your specific situation with me, please do not hesitate to contact me.

For more information, contact David Rectenwald at drectenwald@slk-law.com or 419.321.1407.

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