ALJ Rules Nonresident's Severance Pay Is New York Income

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Severance pay received by a nonresident from a New York employer was properly allocated to the state, a New York administrative law judge ruled.

New York Division of Tax Appeals ALJ Jennifer L. Baldwin determined October 31 in *Matter of Vora* that income related to employment previously carried on in the state is New York-source income under N.Y. Tax Law section 631(b)(1)(F).

K. Craig Reilly of Hodgson Russ LLP told *Tax Notes* November 7 that section 631(b)(1)(F) was enacted almost explicitly to deal with this type of post-employment compensation.

Reilly said that before the law, there was at least the argument that the compensation was consideration for the nonresident not doing something in the future instead of being related to employment previously performed in New York. He cautioned that New York has raised the applicability of section 631(b)(1)(F) to other forms of deferred compensation beyond those specifically mentioned in the law, treating it as a broader catchall provision. Taxpayers should be very careful when receiving any type of deferred compensation that could be connected to New York, Reilly added.

But Reilly said it's not always all or nothing in situations in which section 631(b)(1)(F) applies. He noted that subsection (b)(1)(F) directs the reader to 631(c), which covers the general nonresident income sourcing rules.

Ajanta C. Vora was employed by the Washington Market School (WMS), which has a New York City address, but she took sabbatical leave at the end of June 2018 and moved to Hawaii. Vora was terminated at the end of May 2019 and received a severance payment of approximately $112,000 in 2020 while still living in Hawaii.

WMS filed a form W-2 for the 2020 tax year showing the severance amount as New York wages and that $10,744 was withheld in New York state income tax.

Vora filed a nonresident New York income tax return for 2020 that reported the severance payment in the federal amount column and $424 in New York wages, requesting a refund of $10,717.

Vora attached a statement to the return stating that she and her husband had lived in Hawaii and Washington during 2020 and that the W-2 from WMS showing New York wages was in error. She indicated that the $424 was a one-day allocation of wages to New York because the tax software did not allow a New York return to be filed without it.

But the division of taxation notified Vora that it was unable to verify that the compensation from WMS was not allocable to New York, and it reduced the refund to almost $6,000, and applied more than $3,000 of that amount to outstanding New York tax debts.

Vora protested the refund reduction, arguing that the severance payment was not New York-source income.

ALJ Opinion

Baldwin, however, found no indication that Vora's "former employment was not entirely carried on in New York State."

Baldwin noted that the separation agreement with WMS states that Vora would receive the severance payment if she complied with the agreement terms, which included releasing WMS from any claims related to her employment or separation from employment. She added that the severance pay was computed as a percentage of Vora's prior salary plus health insurance costs.

Baldwin said the Tax Appeals Tribunal has explained in previous decisions that section 631(b)(1)(F) was enacted to counter perceived abuse of post-employment severance packages after the tribunal concluded that consideration for post-employment noncompetition agreements was not sourced to New York.

Rejecting Vora's argument that the severance payment was similar to out-of-court tort damages, Baldwin found that a separation agreement providing a general release of a wide range of claims that does not set a payment to a specific claim "is in the nature of severance pay and not damages received in settlement of litigation."

In *Matter of Vora* (DTA No. 830987), the taxpayer appeared by her husband Chetan Vora.