THE NORTHERN TRUST INSTITUTE

# HOW TO RELOCATE WITH TAXES IN MIND

October 2020

There is no doubt: Taxes matter. But before relocating, consider the broader impact of the move, and understand the requirements to establish residency.

Relocation is top-of-mind these days. With potential tax savings growing, more time being spent at home and remote work becoming the norm rather than the exception, many individuals and families are feeling less tied to their current domicile.

This is particularly the case for affluent residents of high-tax states, who were significantly impacted by the 2017 Tax Cuts and Jobs Act's (TCJA) effective repeal of the state and local tax deduction (SALT). Specifically, the TCJA limits the federal deduction to $10,000 for state and local taxes paid — not only for individuals but also for married couples filing jointly. Prior to this limit, high-income taxpayers could much more meaningfully offset their state and local taxes. While experts continue to debate the extent to which taxes alone drive relocation, some point to Florida's nearly $16 billion net gain in adjusted gross income during 2018 as compelling evidence.[1]

The second and more recent reason for high-tax state residents' growing interest in relocation relates to future taxes. Amid the coronavirus pandemic and growing budget holes, legislators in many states are proposing tax hikes targeted at affluent taxpayers. As just a few examples:

- Legislators in New York have proposed higher income taxes and a "billionaire's tax" on unrealized capital gains.[2]
- Governor J.B. Pritzker in Illinois has called for a progressive income tax rate structure on individual income.[3]
- A number of tax changes aimed at the wealthy were proposed (but not passed) in California this year, including a net worth tax with a long-arm statute that would tax former residents for a period of 10 years following their departure.[4]

1 IRS, U.S. Population Migration Data, 2017-2018, Gross Migration Data for Florida, retrieved from https://www.irs.gov/statistics/soi-tax-stats-migration-data-2017-2018 on October 7, 2020.
2 CNBC, Taxes are Likely to Go Up for the Wealthy in these Nine States, retrieved from https://www.cnbc.com/2020/09/25/taxes-are-likely-to-go-up-for-the-wealthy-in-these-nine-states-.html, retrieved on October 9, 2020.
3 The Wall Street Journal, An Illinois Tax Crossroads, retrieved from https://www.wsj.com/articles/an-illinois-tax-crossroads-11601939583?st=mljsvs53907nhx5&, retrieved on October 9, 2020.
4 Andersen Global, Press Room: Tax Release, September 28, 200, California's 2020 Legislative Session Offers Glimpse of Future State Tax Legislation Aimed at Filling Budget Gaps Created by COVID-19, retrieved from https://andersen.com/pressroom/californias-2020-legislative-session-offers-glimpse-of-future-state-tax-leg, retrieved on October 9, 2020.

While some of these initiatives may fail, it seems highly likely that many states with large shortfalls will increasingly turn to affluent taxpayers for lost revenue. This could come in the form of higher (or newly imposed) income, capital gains, real estate, and/or gift and estate taxes.

## THE RELOCATION DECISION

If you are considering relocating for tax purposes, you will want to evaluate the fuller spectrum of financial and non-financial implications. Further, you will also want to make sure your tax-motivated move is not in vain; there are a number of steps you will need to take to successfully establish domicile for tax purposes. To help with your decision to relocate and success thereafter, below are variables to consider and action items for changing residency.

**2020 STATE TAXES AT A GLANCE**

*Rankings based on select areas of taxation*

| High Tax States | | | | | | |
|---|---|---|---|---|---|---|
| Income tax (based solely on rates) | | Estate tax (based on highest maximum rate) | | | Property Tax | |
| | Top Marginal Income Tax Rate | | Exemption Amount | Tax Rate Range | | Property Tax Rate (as a percentage of owner-occupied housing value) |
| California | 13.3% | Hawaii | $5.5M | 10-20% | New Jersey | 2.21% |
| Hawaii | 11% | Washington | $2.2M | 10-20% | Illinois | 2.05% |
| New Jersey | 10.75% | Vermont | $2.8M | 16% | New Hampshire | 2.03% |
| Oregon | 9.9% | Minnesota | $3.0M | 13-16% | Vermont | 1.80% |
| Minnesota | 9.85% | Oregon | $1.0M | 10-16% | Wisconsin | 1.73% |
| District of Columbia | 8.95% | New York | $5.9M | 3.06-16% | Connecticut | 1.70% |
| New York | 8.82% | Illinois | $4.0M | 0.8-16% | Texas | 1.69% |
| Vermont | 8.75% | Maryland | $5.0M | 0.8-16% | Nebraska | 1.65% |
| Iowa | 8.53% | Massachusetts | $1.0M | 0.8-16% | Ohio | 1.62% |
| Wisconsin | 7.65% | Rhode Island | $1.6M | 0.8-16% | Rhode Island | 1.53% |

| Low Tax States | | | | |
|---|---|---|---|---|
| Income tax (based solely on rates) | | Estate tax | Property Tax | |
| | Top Marginal Income Tax Rate | Most state no longer have an estate tax, including the below states with the largest populations | | Property Tax Rate (as a percentage of owner-occupied housing value) |
| Texas | 0% | California | Hawaii | 0.30% |
| Florida | 0% | Texas | Alabama | 0.40% |
| Washington | 0% | Florida | Louisiana | 0.52% |
| Nevada | 0% | Pennsylvania<br>Important note: State does have an inheritance tax, ranging from 0%-15% | Wyoming | 0.55% |
| Wyoming | 0% | Ohio | West Virginia | 0.55% |
| South Dakota | 0% | Georgia | South Carolina | 0.56% |
| Alaska | 0% | North Carolina | Colorado | 0.56% |
| Tennessee | 1%* | Michigan | Delaware | 0.58% |
| North Dakota | 2.9% | Virginia | Utah | 0.62% |
| Pennsylvania | 3.07% | Arizona | Arkansas | 0.64% |

*Applied to interest and dividends only. Tennessee does not tax wages.

Source: The Tax Foundation, retrieved from https://taxfoundation.org/state-estate-tax-state-inheritance-tax-2020/, https://taxfoundation.org/state-individual-income-tax-rates-and-brackets-for-2020/ and https://taxfoundation.org/facts-and-figures-2020/, retrieved on October 10, 2020.

**Important Note:** The above tables are for illustration purposes only and are not appropriate for helping individual taxpayers assess their potential state tax liabilities. Many variables – well beyond the rates mentioned above – impact your tax liabilities at the state level. Before taking any action, seek the assistance of tax advisors who are familiar with your unique situation.

## NON TAX-RELATED FACTORS TO CONSIDER

Tax considerations do and should play a significant role in managing and protecting wealth. Further, if you already own multiple homes in different states, evaluating the tax impact of your choice for primary residence is a prudent thing to do. That said, you will also want to consider other factors — both financial and non-financial — that risk being underappreciated during the decision-making process. These include:

- **Access to top-tier healthcare:** Make sure you understand your healthcare options in the area in which you will re-domicile. You will likely increasingly rely on medical services in that region, and your quality of life may be impacted by the level and breadth of your options.
- **Lifestyle:** It may go without saying, but you will also want to consider other variables that impact your health and happiness. For example: proximity to loved ones, the desirability of your location for visits from your family, climate, culture and even proximity to the airport if you like to travel.
- **Natural disasters and insurance:** Understand the risk of natural disasters in both your current and potential location and the insurance-related costs associated with changing your primary residence.

## TAX FACTORS TO CONSIDER

While the above variables warrant careful consideration, taxes undoubtedly matter too as you seek to realize the full potential of your wealth. To understand the tax implications of your move, work closely with your advisors and consider the following:

- **"All-in" tax implications:** It is common to consider income and estate taxes and overlook property and sales taxes. But every state requires revenue to provide public services. There are no "tax-free" states.
- **State trust income tax laws:** There are a myriad of state trust income tax laws. If you receive income from a trust, understand how it will be taxed at the state level.
- **Specialized Trusts:** In certain situations, relocating your assets by establishing a trust(s) in a "trust-friendly," tax-efficient state, such as Delaware or Nevada, may offer an alternative to physically relocating in order to achieve tax-related benefits. These jurisdictions limit state income taxation on trusts and also offer a variety of other potential advantages, including creditor protection and confidentiality. Keep in mind, however, that relocating assets out of certain states may not be feasible, given the more restrictive rules they use to tax trust income.
- **Taxes on deferred compensation:** Many executives elect to have their salaries and bonuses deferred and paid out during retirement. If you elect a payout period ofless than 10 years, the compensation payments are taxed in the state in which they were earned rather than paid out.

## ESTABLISHING DOMICILE OR RESIDENCY

Once you have made the decision to change your primary residence, you will need to take a number of steps to successfully establish residency for tax purposes. The following list is representative, but not exhaustive. Also, keep in mind that the state in which your immediate family members reside and attend school will matter too. Seek legal and tax counsel familiar with the requirements of both the old and new domicile.

- Obtain a driver's license in the new domicile
- Register a vehicle in the new domicile
- Register to vote in the new domicile
- If applicable in the new state (e.g., Florida), file a "Declaration of Domicile" or similar statement with the local court
- Review and update estate plan
- Review and update property and casualty insurance
- File federal tax returns using the new domicile address
- File new state tax returns as a resident and former state tax returns as a non-resident (for any state income)
- Reference new domicile in legal documents
- Update mailing address for credit cards and account statements
- Relocate collections and heirlooms to residence in the new domicile

- Change address on passport
- Affiliate with social and professional organizations in the new domicile
- Consult with health care providers in the new domicile
- Host family and social gatherings in the new domicile
- Make phone calls from the new domicile
- Establish religious memberships and affiliations in the new domicile
- Maintain a calendar of days in the new domicile

## NEXT STEPS

The relocation process often feels both exciting and overwhelming. Whether you plan to move imminently or over a longer time period, we can help you streamline the wealth planning aspect of your move by:

- Helping you quantify and understand the financial trade-offs of your current and proposed domiciles, including through our Goals Driven Wealth Management technology.
- Coordinating with your other advisors to understand whether any updates to your powers of attorneys, wills, trusts and other estate planning documents are needed.
- Coordinating with your tax advisors to help you successfully establish residency, and as relevant, appropriately time the realization of income and/or deductions.
- Exploring the appropriateness of specialized trusts in Nevada or Delaware for your specific situation.

For help with any of the above, please contact one of our advisors.