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What to Consider Before You Change Your Residence Because of the New Tax Law

Limits on deductions for state and local taxes have created a greater incentive for taxpayers living in high-tax states

By
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For some people, saving taxes under the new law could be a moving experience.
Among the biggest changes is a provision limiting deductions for state and local taxes to $10,000 a year ($5,000 for a married person filing a separate return), starting this year and scheduled to expire at the end of 2025. Also, the standard deduction amounts rose sharply.

These changes have created a greater incentive for many taxpayers living in high-tax areas, including New York City, California, New Jersey and Connecticut, to consider becoming tax refugees. This includes upper-income taxpayers who have more than one home and want to claim a home in a lower-tax area as the one that counts for tax purposes. It also includes some taxpayers who are considering fleeing entirely from a high-tax area.

Moving for tax reasons isn't new. But the new law "has unquestionably led increasing numbers of people to consider moving," says Kerry O'Rourke Perri, a partner in the private-clients group at the law firm White & Case LLP. That's especially so among taxpayers in high-tax areas thinking about selling a business, or large amounts of securities, in the not-too-distant future.

People often don't know their true preferences, from where to eat to when to retire. There's a simple solution to this—and it could save you a lot of money.

"There's a real interest in this topic because of the new federal legislation. We have clients where the tax savings run in the millions," says Mark S. Klein, chairman of Hodgson Russ LLP, and a co-author of the 2018 edition of "New York Residency and Allocation Audit Handbook."
Warning: This isn't as simple as it may sound. What may seem like a clear-cut change in your home for tax purposes may strike state tax auditors as a tax dodge. Rules and audit policies can vary by state, and many misconceptions have sprung up, says Sidney Kess, senior consultant at Citrin Cooperman and of counsel to Kostelanetz & Fink.

Here are a few thoughts and recommendations from lawyers and other tax professionals:

New limits: Some people assume the new $10,000 limit applies to each taxpayer, which would be $20,000 for married couples filing jointly. Wrong. The cap is $10,000 whether you're single or if you're filing a joint return ($5,000 if married and filing separately), says Mark Luscombe, principal analyst at Wolters Kluwer Tax & Accounting.

IRS pushback: Some states have taken legislative action, or are considering steps, designed to combat the impact of the new limits. But the Treasury Department and Internal Revenue Service plan to propose regulations likely to be a powerful counterattack. "Despite these state efforts to circumvent the new statutory limitation on state and local tax deductions, taxpayers should be mindful that federal law controls the proper characterization of payments for federal income tax purposes," the IRS said recently.

Key factors in New York: Lawyers say clients often assume the only thing that matters is how much time they spend in a high-tax state. That's typically very important but not the only factor in at least several states, such as New York and California.

Shrinking Tax Break

Because of the new tax law, many fewer taxpayers will benefit from state and local tax (SALT) deductions.

	2017	2018
Returns benefiting from SALT deductions	**42.3 mil.**	**16.6 mil.**
Tax savings for filers claiming SALT deductions	**$109.4 bil.**	**$20.3 bil.**

Source: Congress's Joint Committee on Taxation staff estimates

More Take-Home Pay

States that don't have an income tax

- Alaska
- Florida
- Nevada
- New Hampshire*
- Wyoming
- South Dakota
- Tennessee*
- Texas
- Washington

* New Hampshire and Tennessee generally tax dividend and interest income.
Source: Tax Foundation and TurboTax

Lawyers say New York state typically focuses on five “primary” factors in determining “domicile.” That includes time spent in New York compared with other places. It also includes “active business involvement,” such as “active participation in a New York trade, business, occupation or profession and/or substantial investment in, and management of, any New York closely held business such as a sole proprietorship, partnership, limited liability company and corporation.”

New York also has a “near and dear” test. Where do you keep items “near and dear” to you, or items that have “significant sentimental value”? Examples include “family heirlooms, works of art, collections of books, stamps and coins, and those personal items which enhance the quality of lifestyle.” In addition, “family connections,” such as where minor-age children attend school, can be very important.

Other factors: These include the address on your federal income-tax return, bank statements, and bills such as utilities and credit cards. Also focus on such items as your driver’s license, country-club memberships, vehicle and voter registrations, and hunting, fishing or gun licenses.
Superb record-keeping: This is absolutely essential, says Mr. Klein. “Residency audits—some of the most intrusive audits imaginable—are becoming more and more common,” he wrote in a 2014 essay. “Taxpayers often have the burden to prove their physical location every day of each year under audit.”

Consider appealing: If you disagree with a state agency’s final decision, consider going to court. Some taxpayers have scored notable victories.

Get expert help: Beware of the do-it-yourself approach. If the dollar amounts are significant and the issues even slightly murky, hire a trusted expert.

Before hiring a moving van, remember this: “Nobody knows whether the current law will continue in effect after 2025—or even until 2025,” says Ms. Perri.

Mr. Herman is a writer in New York City. He was formerly The Wall Street Journal’s Tax Report columnist.

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