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New Tax Law May Make It Easier to Woo Talent to Low-Tax States

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Technology, financial, and medical companies could find it easier to lure talent away from traditional business centers like New York and San Francisco, now that the new tax law restricts the amount of state and local taxes that can be deducted.

The potential migration from coastal centers, where taxes tend to be high, to such low- or no-tax states as Texas, Florida, Nevada, and North Carolina, is one of the unintended consequences of the tax law (Pub. L. No. 115-97) President Donald Trump signed Dec. 22. The tax code sets a $10,000 limit on the amount of state and local taxes an individual can deduct, where previously there was no cap.

State tax rates are often one of many factors that high earners, such as medical professionals and business executives, weigh when they're being recruited to a position in another city. Cost of living is often a key factor in whether they take the job, Neil Sims a managing partner at executive recruiting firm Boyden, told Bloomberg Tax.

"If the job is in North Carolina or Houston, state taxes are one of the talking points in rationalizing a potential decision to leave the Bay Area for an opportunity," said Sims, who specializes in recruiting technology executives.

The $10,000 write-off ceiling amounts to a large tax increase on many high earners who live in places such as New York City, where top-earning residents pay about 12.7 percent in state and city taxes, and California, where the state income tax is 13.3 percent.

Steve Look, an executive vice president in the Medicus Firm's Dallas office, who recruits physicians from around the country, said no-income-tax states consistently rate among the highest on doctors' wish lists. Specialists making $400,000 a year could face a tax bill that is up to $50,000 more in a high-tax state than in a no-tax state.

"It's not like nobody wants to go to California, but it has changed the landscape somewhat," Look said. "It's harder to have the lifestyle, even for a physician, you might want." The new tax act could precipitate "a lot more lateral movements" from high-tax states like New York and California to the lower-tax South, Nashville, Tenn.-based recruiter Barbara Mayden told Bloomberg Tax.

The move from high-cost locales to less-expensive cities has been a trend for at least a decade now, Dan Ryan, partner-in-charge at executive search firm Heidrick & Struggles' New York office. He points to Jacksonville, Fla., where Bank of America Merrill Lynch, JPMorgan Chase & Co., and Citigroup Inc. are some of the largest employers. The tax bill could accelerate moves to those places where there are already jobs in fields that used to be concentrated in the Northeast, he said.

'Last Push'

"This change in tax reform might be the last push for some people," said Mike Campbell, tax office managing partner for BDO USA LLP in San Francisco. Campbell said he has had several high-net-worth clients call him about the possibility of moving to a low-tax state. "If they can save enough money and they're mobile enough, you're going to see some of those people move."

Mayden, a principal at Young Mayden LLC, said she thinks recruiters will continue to successfully sell $180,000 starting salaries to first-year big law associates considering moves to New York and Los Angeles, while more experienced attorneys and partners could be convinced of the payoffs of moving to lower-tax and lower-cost-of-living states due to the $10,000 cap and easier entry into housing markets.

"I just got off the phone with a senior partner in California thinking about moving to Nashville, and we talked about what he could get for his several-million-dollar California home if he sold and moved to Nashville," said Mayden, a former attorney in the New York office of Skadden, Arps, Slate, Meagher & Flom LLP. "I told him he could move into the governor's mansion."

Recent data shows a migration is possible. Up to 37 percent of California homebuyers would have considered a move if the SALT deduction was eliminated, according to a recent survey by real estate brokerage firm Redfin Corp. However, a 2016 study based on Treasury Department data showed that high-income earners are often "embedded elites," and extrapolated that a 10 percent increase in the top state tax rate would only lead to a 1 percent loss of millionaires to out-of-state migrations.

Before the law change, several no-income-tax states were already experiencing population growth. Three of the top five fastest-growing states based on a percentage—Nevada, Washington, and Florida—don't have a personal income tax levy, according to December data from the Census Bureau.

Real Estate Boom

The high-end real estate market in places like Las Vegas, Lake Tahoe in Nevada, Jackson Hole, Wyo., and West Palm Beach, Fla., is bracing for an influx of new buyers as wealthy individuals look at making moves, real estate brokers told Bloomberg Tax.

Matt Faupel, of Graham-Faupel-Mendenhall & Associates, a real estate firm based in Jackson Hole, said he started receiving significantly more calls from potential buyers in mid-December, once it became clear the tax bill would become law.

Faupel said he has seen an uptick in interest in homes in the $3 million to $10 million range. Becoming a Wyoming resident is relatively easy, but the trickiest part is helping his clients "divorce" from their previous states, which requires not only moving one's residence, but also changing financial ties, such as where one's accountant is located and where an individual donates money, he said.

The lack of state income taxes in Nevada is a big selling point for California residents from Orange County or the Bay Area who are looking to move, said Mike Herman, a real estate professional at Oliver Luxury Real Estate in Reno and Lake Tahoe. Nevada saw a large influx of residents after Proposition 30 passed in California in 2012, raising the top rate to 13.3 percent, Herman said.

No Mass Exodus

But the law change is unlikely to drain New York and San Francisco of all their high-earning residents. For many professionals, region is important to their clients, said Avis Caravello, owner of Attorney Search Consultants LLC, based in San Francisco.

"The allure to develop the client base is very region-specific. That's why we see a lot of difficulty moving a client base from other states, such as New York," said Caravello. "I'm just not sure we're going to see a lot of out-migration. Most of my clients and candidates have global practices, but they're representing those clients in California, or they have international clients doing business in California."

Morris Pearl, chair of the Patriotic Millionaires, a group that opposes wealthy people seeking lower tax rates, said he doesn't think the bill will have much effect on people leaving their homes, such as New York, where he lives.

"A lot of things you can't do anywhere other than New York. It's not so much that it matters where you are, it's just that the rest of the people are in New York, the clients are in New York, and the restaurants where you take the clients are in New York," he said.

In high-tax areas, "services are better, costs are higher, wages are higher," Joe Kirchner, an economist for Realtor.com, told Bloomberg Tax. "That's critical to the decision-making process of someone buying a home."

Jennifer E. Myers, president at SageVest Wealth Management in McLean, Va., said this could spur some "easy" moves—New Jersey residents moving across the border to lower-tax Pennsylvania, or New Yorkers planning to move to Florida to retire could move a couple of years earlier than planned to get the tax savings sooner.

"This legislation might be one more little nudge for people," said Look, the physician recruiter.

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