A Closer Look

Changing Your State of Residence

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In Brief

- **For a variety of reasons, including changes in tax laws and the effect of the COVID-19 pandemic on work habits, people have become increasingly interested in changing their state of residency.**
- **Establishing residence in a new state is possible, but many steps are involved. Failure to complete them properly could cause unwelcome problems, including having your income taxed by both your old and new state of residence. Careful consideration of the many financial and nonfinancial implications of such a change — preferably with your tax and other advisors — is essential.**
- **In this A Closer Look, we examine some of the most important questions that need to be addressed when contemplating a change in your state of residence.**

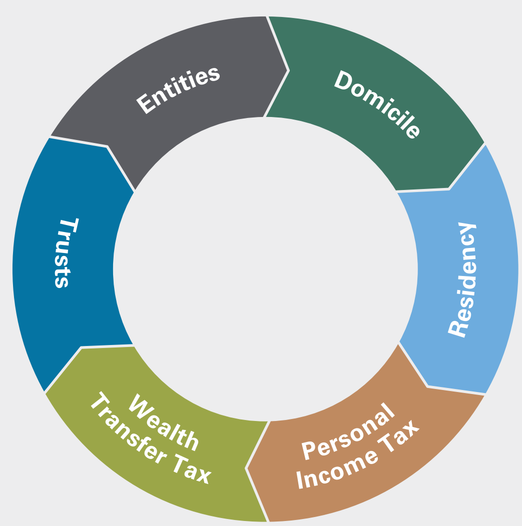
Have you ever thought about changing your residency from one state to another?

If so, you are not alone. A few years ago, the Tax Cuts and Jobs Act of 2017, with its reduction or elimination of the federal deduction for state and local taxes, prompted many to consider a change in residency, particularly those living in high-tax states. And the past year's pandemic, with many individuals working from home, has only increased the numbers of people considering — and undertaking — such a move.

While it is certainly possible to change your state of residency, doing so successfully involves much more than sending a change-of-address form to the local post office. And most articles on this subject won't be much help; a Google search on residency will yield a plethora of results, but they tend to be limited in scope, focusing almost exclusively on one aspect of the process, changing domicile (more on this later). In fact, changing residency is a substantial undertaking with profound implications for both the financial and nonfinancial aspects of your life. Before you make the ultimate decision to move, we encourage you and your advisors to conduct a comprehensive review of the impact it would have to determine whether it makes sense for you and your family.

In this A Closer Look, we review some of the most important questions that need to be addressed when evaluating a potential change in residency.

Evaluating a Prospective Change in Residency



Where Are You Domiciled?

Domicile and residence are terms that are often used interchangeably in everyday conversation, but they have very different meanings in the tax world. It is possible for you to be domiciled in one state and reside in another state. For example, "snowbirds" are people that are domiciled in northern states and yet reside in southern states during the winter months. Understanding how these terms affect you is the first step.

The concept of domicile gives a state the right to tax you in many different ways and is usually defined as your fixed or permanent home to which you intend to return when absent, regardless of whether you live elsewhere. No matter the number of homes you have, you can only have one domicile, and once established, it remains as such unless you successfully change it.

When considering a domicile change, the main goal is to ensure that the state you are leaving respects the change, as it is possible for a state to claim that you did not successfully change your domicile and continue to tax you.

Inherent in the definition of domicile is "intent." Although intent is a state of mind, one's actions, or lack thereof, are often used by a taxpayer and by the state to substantiate one's intent.

Several factors may be considered when substantiating or challenging one's intent to change domicile. These include, but are not limited to, the state that issued your driver's license, where you visit doctors, where you vote, where your personal property is located, where you work, where you have club and/or religious memberships, what state governs your estate planning documents, where your children go to school, and where your family lives. While the focus may vary from state to state, we have included a detailed check list of factors you can consider on page 4.

But perhaps the most critical factor in substantiating intent to change is the time you spend in the new domicile state. Many states incorporate the concept of "leave and land" when challenging the change. Failure to "land" in the new state can have a devastating effect on your claim of change. For example, if you have several homes in different states and you choose to spend time in each home while you are transitioning, your original domicile state may claim that you did not "land" in a new state and continue to tax you. Residency tracking apps — such as Monaeo, TaxDay, and TaxBird — can help keep track of day counts for proving a change in domicile.

Domicile vs. Residence

When establishing residency, it's critically important to understand the distinction between a domicile and a residence and the specific state rules that apply.

Your **domicile** is your permanent home; it's your main residence and the place you intend to return to when away. While you can own numerous homes, you can have only one domicile. The key, when switching domicile, is to do so in a legitimate, thorough way so as to avoid the possibility of both the old domicile state and new domicile state claiming you as a resident and taxing your income accordingly.

Your **residence**, in contrast, is a place you live temporarily before returning to your domicile. This could be, say, a summer or winter home, a home you live in while on a temporary job assignment, or even a college dormitory. You can have a residence in more than one state. Depending upon individual state laws, you could trigger residency status and be liable for paying income taxes to that state — in addition to the taxes you would pay in your domicile state.

Are You a Resident of a Different State?

States also have the right to tax you under the concept of residency. Statutes defining residency can vary dramatically from state to state, but typically include (a) presence in the state for a certain amount of time and (b) maintaining a home or apartment within that state. Once you meet a state's definition of a resident, you may be subject to that state's taxes regardless of whether you are domiciled in another state. This raises the unpleasant possibility of double state tax jeopardy.

Continuing to maintain a home or apartment in the state you are leaving may require you to pay close attention to that state's residency rules when you visit. It also pays to be diligent with your domicile change planning. For example, if your old state denies your domicile change, you may be in jeopardy of double state taxes, as your new state may deem you a statutory resident.

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Once your domicile and residency questions are addressed, you can focus on the impact on your financial, estate, and income tax planning matters.

What Happens to Your Personal Income Taxes?

As part of the analysis, your tax advisor can provide a comparison of the differences in your income tax liability due to the move. It is also important to identify the assets that would continue to have ties to your old state, such as real property and incentive stock options. Understanding the income tax rules of the new state can allow for some pre- and post-move planning opportunities to effectively mitigate your income tax exposure. For example, you may consider accelerating or deferring income or deductions depending on the tax implications of each state.

Will You Need to Change Your Estate Plan?

Gift, estate, and generation-skipping transfer tax rules differ from state to state. Some states may also impose an inheritance tax or follow community property laws. Knowledge of the application of these rules can allow for some pre- and post-move planning opportunities to effectively mitigate your wealth transfer tax exposure. For example, you may consider accelerating or deferring the setting up of trusts or making outright gifts depending on the rules of each state.

What Happens to the Family Trusts?

Often overlooked when changing domicile is the unwanted effect on the trusts that you or your family members are associated with. Some states subject a trust to taxation based on the domicile of the grantor (the person who created the trust), the trustee, or the beneficiary.

An inventory of all trusts that you or your family members are tied to by any of these positions should be prepared to ensure that a proper evaluation can be made.

With this information, an analysis can be prepared to indicate any areas of exposure and allow for possible pre- and post-move planning. For example, if the new state will tax a trust simply because you are a trustee, you may consider stepping down as trustee and appointing another person who does not reside in that state.

What Happens to Your Investments or Family Entities?

Whether you own an interest in a limited partnership, an S corporation, a limited liability company, or a C corporation, the decision process should include an assessment of the effect that a change in domicile can have on these entities. Some states may subject an entity to taxation or filing requirements based on the residency of its members. An inventory of all investments that you or your family members own should be prepared to ensure a proper evaluation.

Domicile Change Checklist

When changing your domicile, be prepared to demonstrate that you left your old state and moved to a new state with the intent to remain there permanently. While each state may view what is necessary differently, below is a list of factors that can help you substantiate your intent to change the location of your permanent home.

Establish a fact pattern that supports the fact that you have moved to a new primary home:

- ✓ Cell phone, credit card, travel activity, and other accessible data will support your physical location.
- ✓ Acquire a nicer home in the new state; downsize in the old state.
- ✓ Establish a move date (not January 1); take pictures and save receipts evidencing it.
- ✓ Move your most precious sentimental or monetary personal items and save shipping documentation.
- ✓ Move pets and enroll children in school in the new state.
- ✓ Change travel patterns — spend significantly more time in the new state and significantly less time in the former state compared to the past.
- ✓ Move primary vehicles and register them.
- ✓ Move your homestead exemption.
- ✓ File a declaration of domicile if available.
- ✓ Change your address. All mail should be addressed to your new primary home.
- ✓ Submit a permanent change of address request to the U.S. Postal Service.
- ✓ Get a new driver's license and relinquish your old driver's license.
- ✓ Change toll passes and parking permits.
- ✓ Update your homeowner's insurance policy to reflect the new primary residence.
- ✓ Execute new wills, powers of attorney, and other estate planning documents in the new state.
- ✓ Open an account at a local bank and relocate your safe deposit box.

Unplug from your previous community, and plug into your new community:

- ✓ Spend more time where your primary home is located than anywhere else.
- ✓ Join clubs and social and religious organizations near your new home, and change status to "non-resident" or resign from old ones.
- ✓ Look for board and committee memberships in the new state, and resign from previous local leadership positions.
- ✓ Get season tickets, join museums, community groups, and other local attractions.
- ✓ Reduce significantly or do not renew memberships and season tickets in the previous state.
- ✓ Find new doctors, dentists, hairstylists, gyms, therapists, etc, near your new home.
- ✓ Have medical records forwarded from your former providers.
- ✓ Register to vote, and vote in person.
- ✓ Make new friends and connect with extended family near your new home.
- ✓ Change social media profiles; post evidence of local engagement on social media.
- ✓ Host special occasions at your primary home.

Move your business activities or retire/scale back business activities in former state:

- ✓ Even if you don't travel to do business, scale back day-to-day activities and decision making for the business located in your former state.
- ✓ Get a job, establish a business, or otherwise work from your new location.
- ✓ Move professional licenses, business registrations, and professional affiliations.
- ✓ Change online business profiles to reflect your new home state and affiliations.

Is a Domicile Change Right for You?

Changing your domicile can be one of the most profound decisions you can make. In this report, we've addressed the process and the major financial considerations involved in such a change, but other important non-tax issues — access to healthcare and other services, the cost of living, schools, cultural opportunities, and the many other factors that influence the quality of your life — should be considered as well. For example, we have seen many people return to their prior home states because the tax savings they achieved in the new state didn't outweigh the loss of the freedom to be where they wanted, when they wanted. A thoughtful and thorough decision-making process can help avoid regrets and unpleasant surprises — financial and otherwise — and ensure a successful outcome for you and your family.

At Bessemer, we understand the significance of moving to a new state, and we are ready to work with you through the entire process. If you're interested in exploring whether a change of residency could make sense for you, please contact your client advisor.

About Bessemer Trust

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