The risks of fleeing state taxes

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New Minnesota taxes hit wealthy people, but moving to another state isn't as simple as buying a home elsewhere.

By Neal St. Anthony Star Tribune
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Bruce Bisping – Star Tribune

Attorneys Jeff O'Brien, left, and Bob Abdo say it's too early to tell whether wealthy people and businesses will flee Minnesota after recent tax increases.

The Minnesota Legislature increased taxes on wealthy Minnesotans this year, raising the prospect that some might want to move elsewhere.

Two decisions by the Minnesota Supreme Court this year spell out what it takes to establish legal residency in other states. It's not just a matter of buying a residence.

Bob Abdo and Jeff O'Brien, business and tax attorneys at Lommen, Abdo, Cole, King & Stageberg in Minneapolis, talked about the issue with the Star Tribune.

Q: Is there evidence that higher-earning Minnesotans will leave Minnesota for low-tax states such as Florida in increasing numbers?

Abdo: It is too early to tell given recent enactment of changes, but inquiries into the subject have increased since the tax law changes became law. There has been anecdotal information. For example, a waste-hauling client has advised that at least eight homes to which it delivered containers advised that they were moving to Wisconsin. Another client was looking seriously into moving to Wisconsin. Also we have been told that cities in Florida have had substantial inquiries from Minnesota businesses about the benefits of moving their businesses.

In addition, the Connecticut Department of Revenue commissioned a study in 2008 of the effects of its estate and gift tax on outward migration. Connecticut is the only state besides Minnesota to impose a gift tax, and it implemented an estate tax in 2005. Thus, its tax structure is most similar to Minnesota's. That study did find increased outward migration following the enactment of the Connecticut estate tax, most of it to Florida, which has no state income tax or estate tax.

Q: The Minnesota Revenue Department uses multiple factors in determining residency. Is the most significant that you can't be in Minnesota half the days of the year or more?

O'Brien: The court cases make clear that it is the weighing of all 26 factors to determine whether the taxpayer has overcome the presumption of Minnesota residency. Furthermore, even if all 26 are complied with, it may not be determinative.

Abdo: Maintaining funds in Minnesota bank accounts; club memberships; a home or business; personally guaranteeing the businesses debts and conferring with the businesses managers by telephone and fax; receiving medical care in Minnesota; use of professionals in the state such as accountants, attorneys, loan officers, financial advisers; frequency of travel to the state; [and] keeping a car licensed in Minnesota are all factors the tax authorities will weigh in determining residency.

Q: Please summarize the 2013 Minnesota court rulings that went against people who claimed they had become Florida residents?

O'Brien: One taxpayer [Ken Mauer] was an NBA referee during the years at issue in the case. He purchased a townhouse in Fort Myers, Fla., obtained a Florida driver's license and registered to vote in Florida. Mauer left from and returned to Minnesota on several occasions and his NBA pay was deposited into a Minnesota bank account. Three of his four vehicles were kept in Minnesota and he retained ownership of his Minnesota home. In one of the tax years at issue, Mauer spent 50 percent of his time in Minnesota. The court stated that once an individual's domicile is established in Minnesota it is presumed to continue until another domicile is actually established. The Tax Court applied the Minnesota Department of Revenue's 26 factors and determined that Mauer had not rebutted the presumption. The Minnesota Supreme Court affirmed.

In William Larson vs. the Commissioner of Minnesota Revenue, the taxpayer owned a Peterbilt truck dealership in Minnesota and desired to purchase a second dealership in Las Vegas. In order to do so, he was required to live in Las Vegas and divest himself of ownership in his Minnesota and Wisconsin dealerships. He bought a condo in Las Vegas and moved most of his personal belongings there. He obtained a Nevada driver's license and canceled his Minnesota driver's license. He registered to vote in Nevada. However, he continued to travel frequently to Minnesota and his family resided there. He used Minnesota professional advisers and sought medical treatment in Minnesota. The court found that Larson owned more property in Minnesota than in Nevada, spent more time in Minnesota, registered more vehicles in Minnesota, and maintained bank accounts and mail delivery in Minnesota. Again, balancing the 26 factors, the Tax Court found that Larson was a Minnesota resident for the tax years at issue. The Minnesota Supreme Court affirmed.

Q: What is the major take-away for those who are thinking about changing their legal residence for tax reasons?

Abdo: It is not enough simply to purchase a home in another state and reside there for at least six months. The court cases suggest that a more complete break with Minnesota must be established in order to evidence a taxpayer's intent to change from Minnesota to another state. Further, with the expansion of the Minnesota estate tax as applied to nonresidents to cover ownership interests in [certain partnerships and investments] … will still subject the taxpayer to Minnesota taxes.

Q: Do you think the recent court and legislative moves mean more entrepreneurs and affluent citizens will leave Minnesota?

Abdo: Too early to tell. Even though there is an angel [tax credit] incentive, Minnesota is not an easy state to start a business in if you're in need of capital. Angel networks don't seem to be as vigorous as they are in other states. The angel tax credit is limited to a narrow class of businesses (usually high-tech or green) and the state does not offer much by way of loans or grants or matching funds as do some states such as South Dakota. By taxing higher income individuals more — in essence daring them to relocate to states with lower taxes — Minnesota is creating a negative environment for small-business investment.

Q: Do you give credence to those who say the Twin Cities and other higher-cost areas still will attract entrepreneurs because of business, civic, cultural and other assets?

Abdo: Minnesota has great assets that appeal to entrepreneurs and creatives. It will be hampered in its efforts to continue to attract business and entrepreneurs if state government creates disincentives to investment in Minnesota small businesses. A nonresident must now weigh Minnesota estate, income and gift tax consequences of investing in a small business which owns its own equipment, such as a brewery. When gauging the pros and cons of starting a business … it appears that the Legislature in the last session added to the list of cons that a business must weigh before doing business here.

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