Opinion: Calif. can't sidestep federal tax impact

By Dan Walters, CALmatters

When President Trump signed an overhaul of the federal tax system six months ago, there was much complaining from politicians in California, New York and other high-taxing – and politically blue – states.

They particularly disliked a new $10,000 limit on deductability of state and local taxes because it would make their taxpayers, particularly the most affluent, feel the full financial effects of high state taxes.

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They feared that those highly impacted taxpayers would find ways to reduce or eliminate their state tax liabilities since they could no longer write them off on federal tax returns, and that would cut into state revenue streams.

The potential impact would be especially heavy in California because of the state's lopsided dependence on its highestincome residents. The top 1 percent of California taxpayers account for nearly half of the state's income tax revenues and therefore about a third of its general fund budget.

Gov. Jerry Brown even worried aloud that faced with much-higher tax burdens, the state's wealthy would be tempted to move their official residences to low- or no-tax states such as neighboring Nevada.

California politicians saw it as a sneak attack by Republicans on blue states and vowed to counter it with some clever bookkeeping.

While deductibility of state and local taxes was being severely curtailed, they said, the tax overhaul left charitable contributions untouched so they could give taxpayers an option of making tax-deductible donations to the state in lieu of taxes.

We haven't heard much about that scheme of late, for good reason. Last month, the Internal Revenue Service issued a warning that "federal law controls the characterization of the payments for federal income tax purposes regardless of the characterization of the payments under state law."

Implicitly, in other words, were California or any other state to attempt the charitable contribution ploy, taxpayers who used it would be in danger not only of having their deductions denied, but of being slapped with penalties for trying it.

Call it a political checkmate.

So we're back to where we started when the federal tax law was changed, with upper-middle class and high-income Californians, those paying more than $10,000 in previously deductible state income and local property taxes, facing higher federal tax bills.

And that means we're back to wondering whether a significant number of affluent Californians will feel moved to move.

Earlier this month, the Wall Street Journal reported that real estate professionals are seeing an uptick in inquiries from high-income clients about moving from high-tax states such as California and New York to those with low- or no income taxes, such as Florida and Nevada.

David Hutchinson, who developed the Clear Greek golf community on the Nevada side of Lake Tahoe, told the Journal, “Most of our lot sales are to buyers from California, the vast majority of whom intend to make them a permanent residence.”

Someone earning $3 million a year could move his or her personal domicile from San Francisco to Tahoe, Hutchinson said, and save $399,000 a year in taxes, adding, “That’s a lot of money to spend on real estate.”

Anecdotal stories about tax refugees abound, and in fact, I could cite several well-to-do retirees among my circle of acquaintances who’ve relocated from Sacramento to the Reno area for tax reasons.

So it’s happening, but whether the tax relocations remain just anecdotes or develop into a green wave won’t be known until after those higher taxes come due next year.

Dan Walters is a columnist at CALmatters.