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THE RIPPLE EFFECT: Experts weigh impact of Tepper's exit from N.J. to Florida

By By Martin C. Daks, for NJBIZ, June 27, 2016 at 3:00 AM

Billionaire hedge fund manager David Tepper, formerly New Jersey's wealthiest resident, filed for a legal change of residency last year. He is now a Florida resident. - (AP IMAGES)

David Tepper moved himself and his $18 billion Appaloosa Management hedge fund to Florida last year.

The move had short-term and long-term implications for the state of New Jersey.

Some argued Tepper's move — presumably to lower his taxes — proves the state is too expensive in which to live (and ultimately die). And that it could be a bad sign of things to come.

Others stayed in the present, wondering how a state already hurting for revenue would make up for a loss of about $100 million in taxes.

To be fair, any state would be pained by the departure of an uber-wealthy taxpayer. But in New Jersey, more than one-third of personal income taxes are paid by less than 1 percent of the taxpaying population, so the revenue challenges are magnified when any wealthy individual pulls up stakes and leaves.

"Our personal income tax comprises about 40 percent of our revenue base, and relies on less than 1 percent of taxpayers for nearly one-third of that revenue," New Jersey Legislative Budget and Finance Officer Frank Haines warned the state Senate Budget and Appropriations Committee in early April.

"Other tax and revenue sources are subject to forecast error as well, but even small departures from our expectations for the income tax can make other problems seem small by comparison."

The withdrawal of Tepper — who was No. 1 on the NJBIZ 50 Wealthiest New Jerseyans list last year — could leave a hole in the state's coffers of around $125.6 million a year, based on the state's top personal income tax rate of 8.97 percent.

Some will argue the gap isn't that great, as Tepper undoubtedly used many methods to lower his tax bill.

This much, however, is clear. The gap will certainly grow if more residents follow.

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Tepper has never said he left the state to lower his tax rate. But Mike Karu, a member of the Livingston-based CPA firm Levine, Jacobs & Co. LLC, said it makes the most financial sense.

"It's difficult to speculate exactly why Mr. Tepper moved out," Karu said, acknowledging reports that Tepper has close family members in the Sunshine State. "But Mr. Tepper is an incredibly bright, savvy individual. My expectation is that he would use any legal method to minimize his tax debt."

Florida isn't the only destination that New Jersey should worry about, Karu said.

"Nevada, Texas and other states that don't have a personal income tax can also be tempting destinations for the ultra-wealthy, since a move there would be an automatic tax break," he said. "Additionally, New Jersey has both an estate tax and an inheritance tax — many others only have one and some, like Florida, North and South Carolina and others, have none."

Mike Karu

But the statutory tax rate is only part of the story, says Steven P. Bortnick.

"New Jersey is a gross income tax state that does not allow many deductions, limits the use of losses and does not differentiate by type of income (such as ordinary versus capital gains), so a fairly high tax rate is assessed on even more of your income," said Bortnick, a partner with Bederson, a Fairfield-based CPA firm.

He notes that New Jersey also has a comparatively high unemployment and disability tax rate for both employers and employees — and the tax is levied on a pretty high threshold of wages.

And those taxes are subject to annual increases when statewide unemployment rates are high, driving up the overall tax bite even more.

According to the Tax Foundation, a free market-oriented Washington, D.C.-based organization that collects data and publishes research studies on U.S. tax policies at both the federal and state levels, New Jersey has the highest property tax rate in the nation for owner-occupied housing, Bortnick said.

He noted the state's 7 percent sales tax rate is among the highest in the nation.

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As a result of residing in a state with "very high" income taxes and real estate taxes. many New Jersey residents end up being subject to the alternative minimum tax on their federal returns, which essentially prevents them from offsetting their taxable income with the otherwise-allowable deduction for state taxes.

"So, again, New Jersey residents end up paying more taxes on their income," Bortnick said. "And with a top bracket of 9 percent, New Jersey corporate taxes are also some of the highest in the nation, and can hit companies in fairly low income brackets."

And in unusual places.

"The sarcastic side of me finds it funny that, given that the ways the highway tolls are set up, at almost all crossings, motorists are free to drive into New Jersey, but you have to pay to leave."

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The so-called "death taxes" are driving a significant number of people to flee New Jersey, according to Ed Deutsch, the managing partner of McElroy, Deutsch, Mulvaney & Carpenter LLP, a Morristown-based law firm.

"I've seen business consultants and other high income earners pull up their practices and move to places like Florida to escape New Jersey's high income and other taxes," Deutsch said.

"If you've got a manufacturing company, with real estate and machinery and equipment, it can be a lot more difficult to pack and move. But if your assets are primarily intellectual, then it's easy to move. Older people, in particular, just don't want to die here in New Jersey and see their estate get unnecessarily reduced by taxes."


Ed Deutsch

High net worth individuals and couples may be able to catch a significant tax break by moving to a state such as Florida, but they should be prepared to prove that they're really living where they say they are, warns Hal R. Terr, a Princeton-based tax partner at the CPA firm WithumSmith+Brown.

"While domicile or residency rules vary by state, you're generally not considered a New Jersey resident if you declare another state as your state of domicile and you spent 183 days or less here in New Jersey," Terr said. "A lot of people ask me about the rules of domicile and I advise them that the more ties you have to your primary residence, the stronger case you can make if you're ever challenged.

"New Jersey, in particular, is being more vigilant about going after people who are pushing the boundary when they try to avoid state taxes."

Outmigration — the phenomenon in which New Jersey residents move to other states — has had a significant impact on the state's economy:

From 2005-2014 New Jersey lost ...

- more than **2 million** residents
- **$18 billion** in net adjusted gross income

Outmigration has also resulted in the loss of:

- **75,000** jobs
- **$11.4 billion** in economic activity
- **$4.2 billion** in labor income
- **$8.4 billion** in househould spending

SOURCE: NJBIA report, February, 2016

So, owning or renting a house is just the beginning.

"Your driver's license should be the same state as the one in which you're claiming domicile," Terr said. "Similarly, you should register to vote in that municipality, your doctors should be located there, and your country club or house of worship, if applicable, should also be in that area, as well as a number of other factors."

What about someone with multiple homes, who spends a few months in different states?

"Some of my clients spend three months in Maine, five months in Florida, and maybe four months in New Jersey," Terr said. "You have to research the domicile tax laws for each state, but generally, the place where you spend the most time — assuming your driver's license, doctors and other evidence check out — will determine where you're domiciled for tax purposes."

Terr, however, said that for most people, taxes alone don't determine where to live.

"You have to consider the overall quality of life," he said. "For example, where do your children and grandchildren live? On the other hand, I've had clients who spend five months a year in Florida, and as they get older I'll likely tell them to spend another five weeks down there, so they can avoid New Jersey's retirement and death taxes."

Interestingly enough, when Terr, a former Connecticut resident, joined Withum's Princeton office in 2004, taxes influenced his choice of residence.

"I could have settled in Princeton, but decided to move to Bucks County, Pennsylvania, right across the Delaware River," he said. "The commute's a snap, but the property taxes and income taxes are both lower in Pennsylvania."

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New Jersey's loss of an individual taxpayer like Tepper is only part of the problem, according to Andrew Ebneter, a Wayne resident and state and local tax practice partner with Marcum LLP.

"Large businesses are also leaving the state, which reduces tax collections here," Ebneter said. "For example, Hertz left Park Ridge for Florida a few years ago, and Mercedes-Benz recently left Montvale for Georgia. So you don't want to look at budget issues purely from a personal income tax standpoint, which would be a myopic viewpoint.

"That said, the state is pursuing measures to attract and retain businesses through tax credit and incentive programs to bolster its tax base, with varying degrees of success."

Keeping people like Tepper is just as hard. And Barbara Taibi, a partner in the personal wealth advisers group of the Iselin-based CPA firm EisnerAmper, said the exodus has been going on for a while.

"I've been working with high net worth people for more than 25 years, and lately I've been seeing more of them thinking about relocating from New Jersey to a jurisdiction with lower state tax or no state tax," she said. "This often happens before they sell a business, or a large block of stock, or in preparing for some transaction that's going to bring in a large block of income or gain and trigger state tax bills.

"You generally can't avoid the federal liability, but if you can avoid a state tax bite by moving, some people will jump at the chance."

Finding replace him won't be easy.

"If we assume that Tepper was paying the maximum state tax rate of 8.97 percent on his reported $1.4 billion annual income — which is, admittedly, unlikely — then he could conceivably have a tax bill of around $126 million," she said. "At the top tax bracket, it would take about 1,400 taxpayers with income subject to state tax of $1 million apiece to fill that gap.

"Of course, I've never seen a $1.4 billion W2 to begin with."

Barbara Taibi

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