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California Is #1 State People Leave—But Tax Man May Follow Them

According to a U-Haul announcement, California tops the list for a sixth year as having the most people move out in 2025. The news that more Californians are fleeing the state is probably not a surprise to many people. U-Haul says that Texas and Florida but there were other likely suspects too. Texas is the top U-Haul growth state. Of course, most moves are probably not about taxes, but it is hard to ignore tax disparities when comparing states. The top tax rate in the Golden State is 14.4%, though for most types of income, it is a not much better 13.3%.

No Capital Gain Rate

What's more, that 13.3% rate applies equally to ordinary income and capital gain. With the IRS, the capital gain rate is 20% for higher income taxpayers. Add the 3.8% net investment tax under the Affordable Care Act, and you have 23.8%. Say that you are about to sell your stock, large amounts of crypto, or settle a big lawsuit? It might be tempting to move first. Several proposals have been made in the past to increase California's top rate as high as 16.8%. The 14.4% rate came when California eliminated the $145,600 wage limit on California's 1.1% employee payroll tax for State Disability Insurance (SDI). It hits high earners, with the top rate being 14.4% for those earning over $1 million.

Moving Seems Simple

Moving before big stock sales, sale of a company, or a lawsuit settlement are common, but if you aren't careful how and when you do it, you could end up with an audit from California's tough Franchise Tax Board (FTB). Some people have a hard time distancing themselves from California. In an audit, California's tax procedures can be tricky. California, like the IRS, gets unlimited time to audit if you never file a tax return, and that rule catches many people who move away. It can make filing a non-resident tax return—just reporting your California-source income as a non-resident—a smart move.

Residency Audits

Your domicile is your true, fixed permanent home, the place where you intend to return even when you're gone. Many innocent facts might not look so innocent to California's tax agency. For example, do you maintain a California base in a state of constant readiness for your return?

California looks to objective factors to determine residency, including your time in California versus time outside. Consider the size and value of your residences, and the location of the property on which you claimed the homeowner's property tax exemption.

Where your driver's license was issued, cars are registered, professional licenses, registration to vote all counts. So does the location of your banks, doctors, dentists, accountants, church, temple or mosque, and more. What clubs are you a member of, and where? Where do you work, and have business and social contacts? Where do you have all your mail sent?

As you might expect, physical presence is often the biggest issue. If you spend more than 9 months in California, you are *presumed* to be a resident. If you spend 6 months or less in California, you <u>may</u> qualify as a seasonal visitor, but only if you don't work while you are in the state and meet other tests. Yet if your job requires you to be outside the state, it usually takes 18 months to be presumed no *longer* a resident.

Timing

Californians often look to no-tax states like Texas, Nevada, and Florida. Some Californians flee the state before selling real estate or a business. California real estate is taxed here even if you are a non-resident. But settling a lawsuit, or selling stock and other assets after a move can make sense. Some carefully orchestrated moves away from California can work out just fine, but timing and other details are tricky, so be careful. Check out FTB Publication 1031.