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California Tax Hike On Ballot, But Some Voters Vote With Their Feet

California has high taxes. And voters have at least a partial say in that. Proposition 55—the ballot initiative that would extend the "temporary" tax increases on California's high-income earners—is on the ballot. Four years ago, California voters approved Prop. 30. That law raised the state sales tax by a quarter cent. More significantly, Prop. 30 raised the top marginal income tax rate on high-earners to 13.3%, the highest marginal tax rate in the nation. Proposition 55 would continue these tax rates instituted by Proposition 30 through 2030. Hey, that is only temporary, sort of.

The ballot question is whether these temporary taxes should be continued on top of California's already pre-temporary high rates. A "yes" vote supports extending the personal income tax increases on incomes over $250,000 approved in 2012 for more 12 years. The goal is to fund education and healthcare. A "no" vote opposes extending these personal income tax increases on incomes over $250,000, allowing the tax increases to expire in 2019. The income tax increases in question impact 1.5% of Californians, those with a single income filing of at least $263,000, or a joint income filing of at least $526,000.

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Many people flock to California, but taxes are high. Many people live and work here, and then later leave. Many people try to have the best of both worlds, making their money in California, and trying to skip out before California can tax it all. But California's tough Franchise Tax Board (FTB) has a thing or two to say about that. Most tax advisers say that the FTB is much harsher than the IRS.

A California resident is anyone in the state for other than a temporary or transitory purpose. It also includes anyone domiciled in California who is outside the state for a temporary or transitory purpose. The burden is on you to show that you are *not* a Californian. If you're in California for more than 9 months, you are presumed a resident. Yet, if your job requires you to be outside the state, it usually takes 18 months to be presumed no *longer* a resident. Your domicile is your true, fixed permanent home, the place where you intend to return even when you're gone.

Do you maintain a California base in a state of constant readiness for your return?Although California taxes residents on all their income, what if you move out of state and then sell your company or collect on that big investment? Year after year, no state has a bigger and more persistent cadre of would-be tax fugitives than California. Some Californians look to flee the state before selling real estate or a business. Some get the travel itch right before cashing in shares, a public offering, or settling litigation. Some of the carefully orchestrated deals and moves can work just fine. Yet many would-be former Californians have unrealistic expectations about establishing residency in a new state.

They may also may have a hard time distancing themselves from California. Finally, they may not plan on California tax authorities chasing them. If you are fighting California tax bills, procedure counts. You can have only one domicile, and it depends on your intent. How do you measure intent? Objective facts, and many are relevant. Start with where you own a home. Where your spouse and children reside counts too, as does the location where your children attend school. Your days inside and outside the state are important, as is the purpose of your travels. Where do you have bank accounts and belong to social, religious, professional and other organizations?

Voter registration, vehicle registration and driver's licenses count. Where you are employed is key. You may be a California resident even if you travel extensively and are rarely in the state. Where you own or operate businesses is relevant, as is the relative income and time you devote to them. Taxpayers with unrealistic expectations can end up with big bills for taxes, interest and penalties. Like other high tax states, California is likely to probe how and when you stopped being a resident.

The state can have a long memory too. Although the IRS can audit 3 Or 6 years, California can sometimes audit forever. In fact, several things give the FTB an unlimited amount of time to audit you. First, California, like the IRS, gets unlimited time if you never file an income tax return. You might claim that you are no longer a resident and have no California filing obligation. The FTB may disagree. That can make filing a non-resident tax return–just reporting your California-source income as a non-resident–a smart move under the right facts.

Federal audits can add complexity and sometimes can add to your California exposure. Suppose that an IRS audit changes your tax liability. Perhaps you lose your IRS case, or you just agree with the IRS during an audit that you owe a few more dollars to IRS. In that event, you are *obligated* to notify the California FTB, within six months. If you fail to notify the FTB of the IRS change to your tax liability, the California statute of limitations *never* runs.

For alerts to future tax articles, email me at Wood@WoodLLP.com. This discussion is not legal advice.