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WEALTH MATTERS

Why These Millionaires Are Staying Put Despite a New Tax on Them

The reason has little to do with money. Family and community ties keep them from leaving their state.

By Paul Sullivan

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New Jersey recently decided to impose a so-called millionaires tax — effectively increasing state taxes 20 percent on people earning more than $1 million.

Critics had an immediate, and unsurprising, reaction, arguing that such taxes will push the wealthy to move to lower- or no-tax states. But is that true?

While some wealthy people will move, proponents of these taxes argue, few will make good on the threat to move to Florida (with no state income tax) or, in New Jersey's case, to Pennsylvania (where the state tax rate is one-third its neighbor's rate). They argue that high earners and entrepreneurs have family and community ties that keep them from moving away.

"For a small-business owner or an employee earning $1 million or above, that person is probably pretty well entrenched in New Jersey," said David B. Root, Jr., founder and chief executive of DBR & Company, a wealth management firm in Pittsburgh. "States like Florida, Texas and Tennessee have no state taxes, but they have higher taxes elsewhere — in consumption taxes."

Those who do leave generally work in financial services. One often-noted example is David Tepper, the billionaire founder of the hedge fund Appaloosa Management, who moved to Florida from New Jersey in 2016, when New Jersey was last debating an increase in taxes on earnings over $1 million. The state lost millions in tax revenue after Mr. Tepper's move. But a postscript came out in the debate over the millionaires tax this year: Mr. Tepper has moved back to New Jersey.

Given the financial impact of the pandemic on state revenues and little or no prospect of increased federal aid, higher state taxes could be on the horizon beyond New Jersey. Massachusetts has floated the idea of a millionaires tax in the past. Gov Andrew M. Cuomo shot it down for New York State, but the combined state and city tax for residents of New York City, where most of the state's millionaires and billionaires live, is already higher — at 12.6 percent — than the 10.75 percent on high earners in New Jersey.

If nothing else, rising inequality, along with government budget shortfalls, has put the issue on the table this year.

"In this polarized world, the tax discussion becomes part of the polarization," said Mark Bell, head of family office services and private capital for the wealth management firm Balentine in Atlanta. "What does it mean, practically? There are a few thousand people who have that level of income to be caught in that."

Unlike a sales tax or a limit on a state's estate tax, a state income tax rises is pegged to a taxpayer's ability to pay. Joe Kluemper, a senior tax adviser at Geller Advisors, which works with wealthy families, noted that wealthy people spent far less of their income on items that would incur a sales tax than middle-class and poor people.

"Someone who is spending 95 percent of their paycheck, that sales tax hurts them harder than someone who is spending 2 percent of their income each year," he said.

Ken Schapiro, president of Condor Capital Wealth Management and a member of Tiger 21, an investment group whose members need to be worth tens of millions of dollars, said it would take more than higher taxes for him to leave New Jersey.

"It wouldn't be higher taxes," he said. "I have too many business ties. I own a tennis club here. I have friends and family here. Look, if they double the taxes I might do it."

Still, Mr. Schapiro, an avid skier, said that he planned to work more from the home he has in Colorado, where the tax rate is half New Jersey's, and that the increase might accelerate the decisions of some clients who prefer one of the states without an income tax, like Florida or Texas.

"The difference between 10.75 percent and 8.75 percent won't necessarily pay for a second home, but the whole number will for sure," he said, citing the new and old rates for millionaires in New Jersey. "But in general, I usually tell people to make decisions based on goals and objectives and worry about the taxes secondary."

Leslie Quick III, one of the founders of the discount brokerage Quick & Reilly, which Fleet Financial bought in 1997 for $1.6 billion, has lived in New Jersey since 1980. He has children and grandchildren in the state and said he would be hard pressed to get his wife to move to Florida for six months and a day to avoid the tax increase.

But Mr. Quick said he was bothered by how the state would spend the additional tax revenue. He said giving $500 rebates to families earning less than $150,000 was shortsighted when New Jersey had so many infrastructure needs and had to borrow $4.5 billion because of budget shortfalls related to the coronavirus.

"I'm happy to pay the tax if I see other things being done to solve the problems," Mr. Quick said. "It bugs me that they're going to lay this tax on."

Still, proponents of higher taxes on the wealthy argue that this is a good time to act.

“States have these enormous budget shortfalls, and they can’t borrow like the federal government can,” said Seth Hanlon, senior fellow at the Center for American Progress and a former special assistant on economic policy to President Barack Obama. “States need to raise revenue. But high-income people are less likely to change their consumption patterns because of tax increases.”

Regina M. Egea, president of the Garden State Initiative, a nonpartisan think tank focused on the state’s economy, said that while that might be true, higher taxes were keeping other high-earning people from moving to states like New Jersey. She also argued that the increase would push older taxpayers to move.

There’s concern on the national level, too, about targeted taxes on the very wealthy. Senators Elizabeth Warren and Bernie Sanders both proposed a wealth tax when they were seeking the Democratic nomination for president.

Willie Mandrell, a real estate investor in Boston, said he would not object to the higher tax on the income of millionaires that had been proposed in Massachusetts. But he would feel different about a tax on his wealth.

“Part of me building wealth and buying assets and eliminating liabilities is to set myself up for retirement or a better future,” Mr. Mandrell said. “Now if you’re going to say the government is going to create a disincentive to do so, that’s a different thing.”

A wealth tax is possible only with a Democratic sweep of the White House, the Senate and the House in November. And even then it would be far from a done deal, given both its complexity and questions about its constitutionality.

A more likely outcome is removing the $10,000 limit on the deduction for state and local taxes against whatever federal tax is owed — a particular benefit for residents of states, like New Jersey, with high property taxes. This deduction was limited in President Trump’s 2017 tax law. While the cap expires in 2025, a Democratic victory in November could speed the return of the full deduction.

Then New Jersey’s millionaires would see their tax bill lowered, with the same amount going to the state but less to the federal government.

“It obviously softens the blow,” Mr. Quick said. “But it kicks the can down the road. We have a spending problem, and we can’t afford to keep spending what we’re spending.”