

Missing the Mark on Wealth Migration: Past Studies Drastically Undercounted Millionaires

By Greg Sullivan and Andrew Mikula



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Introduction

Advocates in favor of a constitutional amendment that would apply a 4 percent tax on all annual individual income over \$1 million argue that similar taxes in other states have had little impact on the migration of millionaires.¹ In support of their argument, they cite Cornell University Associate Professor Cristobal Young, whose research suggests that “millionaires’ taxes” similar to the one being proposed in Massachusetts that have been enacted in other states have had little impact on millionaire mobility.

We welcome Professor Young’s work to the debate, but in this paper, we demonstrate that he drastically undercounts millionaires. The paper outlines several ways in which Professor Young and tax advocates underestimate the number of people who will at some point in their lives be subject to a so-called millionaire’s tax and tax flight trends. Flawed public policy analyses have widely cited Professor Young’s work to justify momentous tax hikes.²

What is the Graduated Income Tax?

For the past several years, Massachusetts has been considering a state constitutional amendment that would levy a four percent surtax on annual personal income over \$1 million. The first attempt to do so, filed by initiative petition, failed a Massachusetts Supreme Judicial Court challenge in 2018 before re-emerging as a legislative petition and receiving initial approval at a constitutional convention in 2019. A vote on final approval by the legislature is expected in the spring of 2021. If passed, it will appear on the statewide ballot in the fall of 2022.

Proponents of the amendment, led by the Massachusetts Teachers Association and the Service Employees International Union, together with advocacy and religious groups, call it the “Fair Share Amendment,” a nod to their frequent assertions that the measure would require only the very wealthy to pay what proponents believe is their “fair share” of taxes.

Opponents argue that it would endanger the long-term economic well-being of Massachusetts by prompting high-income residents and businesses to relocate to states that have lower income tax rates and discouraging high-income individuals and businesses from coming to Massachusetts in the first place. They believe that COVID-19 may exacerbate these relocation effects, as the pandemic has made telecommuting much more prevalent, at least in the short term.³

A Narrow Definition: Counting only consistent million-dollar earners

Professor Young does not count taxpayers as being millionaire migrants unless they had filed a federal tax return with adjusted gross income (AGI) of \$1 million or more *in the year before they moved*. In a 2016 research paper, Professor Young and his co-authors define millionaire migrants as “people who earned \$1 million or more in year t , and changed their state of residency between years t and $t + 1$.”⁴ Such a narrow definition of a “millionaire migrant” ignores the possibility that savvy taxpayers changed their domicile to a lower tax state in anticipation of a million-dollar gain from the one-time sale of a valuable asset, thus avoiding the high rates associated with places like New York and California.

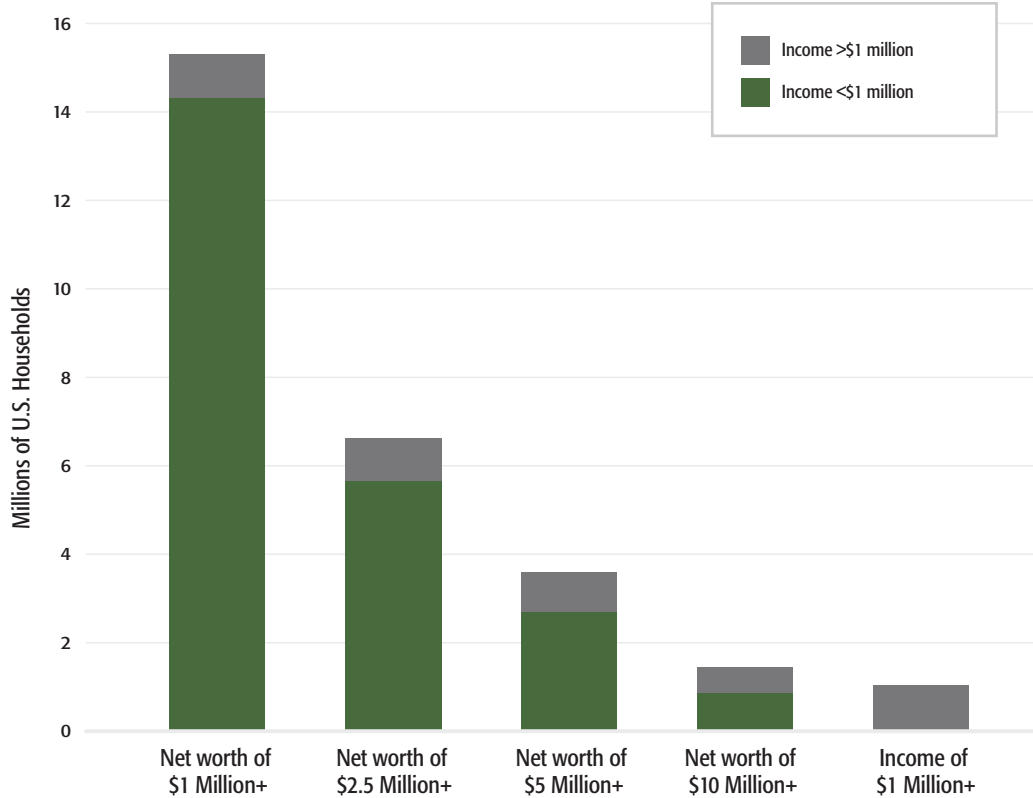
The impact of these “one-time millionaires” will be addressed more thoroughly in future Pioneer research. For now, to grasp the significance of Professor Young’s definitional limitation, consider that it excludes 14.3 million households in the U.S. that had a net worth of \$1 million or more but incomes of less than \$1 million, according to Federal Reserve Board estimates (see Figure 1).⁵ Many of the households portrayed in Figure 1 would be subject to the surtax upon the sale of a portion of their assets, but Cristobal Young’s methodology is inadequate to assess the extent to which they engage in tax avoidance.⁶

Young’s methodology also ignores the fact that the majority of U.S. households with high net worth, defined as more than \$10 million, earn less than \$1 million annually. Among this excluded group are over 850,000 households with net worth of \$10 million or more but annual income of less than \$1 million (see Figure 2). In fact, 58.9 percent of households with over \$10 million in net worth had annual incomes of less than \$1 million.⁷ Cumulatively, these households have trillions of dollars in unrealized capital gains that may be subject to the graduated income tax upon sale.⁸ Future studies of whether millionaire

Professor Young only captures migration among million dollar earners who had seven-figure incomes both before and after they moved

migration is occurring should aim to determine whether graduated income taxes influence the behavior of high-net-worth individuals who happen to make less than \$1 million in income most years. More insidiously, a tax like the so-called Fair Share Amendment would also deter high-net-worth individuals from moving to Massachusetts in the first place.

Figure 1: Number of U.S. households by category of wealth (2019)⁹



Cumulatively, these households have trillions of dollars in unrealized capital gains that may be subject to the graduated income tax upon sale

Figure 2: Share of high-net-worth U.S. households that were million-dollar earners (2019)¹⁰

	Household Income	Net worth of >\$1M	Net worth of >\$2.5M	Net worth of >\$5M	Net worth of >\$10M	Net worth of >\$100M
Number (and percentage) of Households	<\$1M	14,314,529 (93.6%)	5,642,446 (85.2%)	2,687,978 (74.8%)	857,220 (58.9%)	2,645 (7.7%)
	>\$1M	983,540 (6.4%)	980,617 (14.8%)	904,075 (25.2%)	599,115 (41.1%)	31,862 (92.3%)
	Total	15,298,069 (100%)	6,623,063 (100%)	3,592,054 (100%)	1,456,335 (100%)	34,507 (100%)

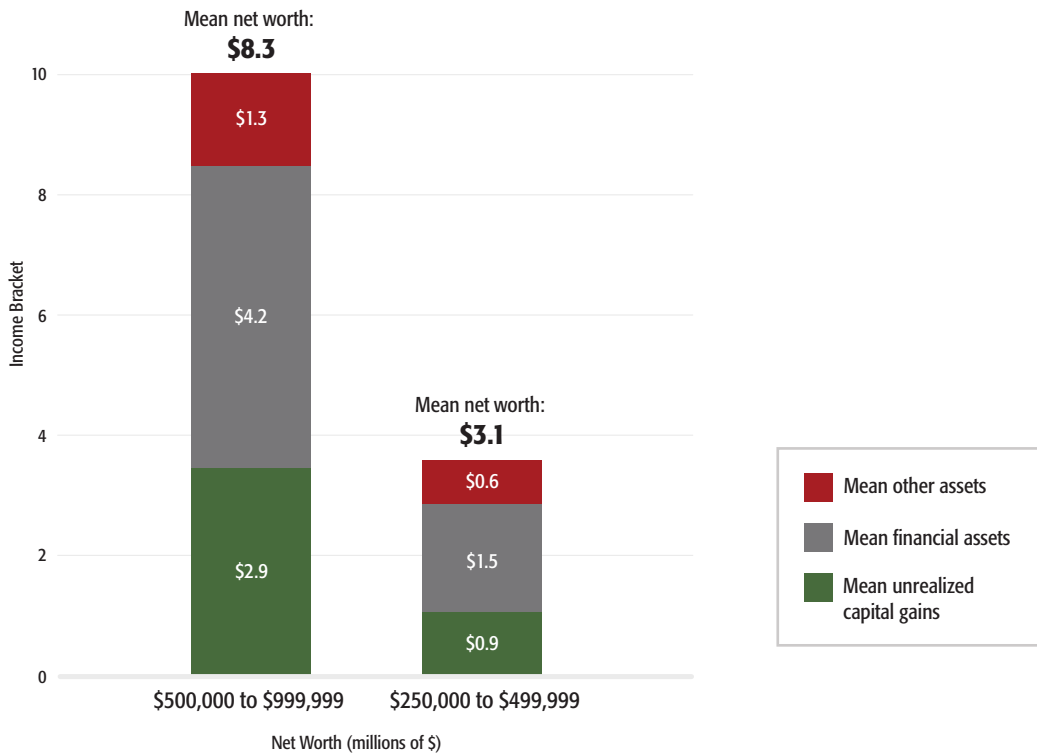
While data on the migration patterns of high-net-worth individuals is scarce, the sheer number of people who could potentially be millionaires in a given year by selling a portion of their assets constitutes a vulnerability to tax avoidance. Thus, net worth is a better measure of wealth than prior year income when analyzing migration in response to taxation.

Another way of making this point is to look at data regarding individuals who earn just under \$1 million annually. These households have a mean net worth of \$8.3 million. Data from the Federal Reserve Board’s 2019 Survey of Consumer Finances, which the American Statistical Association regards as “the most comprehensive [wealth] data available for the United States,” show that nearly 1.6 million U.S. households had incomes between \$500,000 and \$999,999.¹¹ Of these, the mean net worth is \$8.3 million (see Figure 3). While these households would not be subject to the proposed surtax immediately, they may be susceptible to it in the future upon disposition of assets. Also susceptible to future imposition of

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the proposed surtax are the nearly 5.4 million households with incomes between \$250,000 and \$499,999, which have a mean net worth of \$3.1 million (see Figure 4).

Figure 3. Components of net worth among wealthy U.S. households with incomes <\$1 million¹²



Households with annual earnings just under \$1 million have a mean net worth of \$8.3 million. They could be subject to the surtax upon sale of a fraction of their assets, but Professor Young doesn't consider them millionaires.

Figure 4: Mean income and components of net worth among U.S. households with incomes from \$250,000–\$1 million (2019)¹³

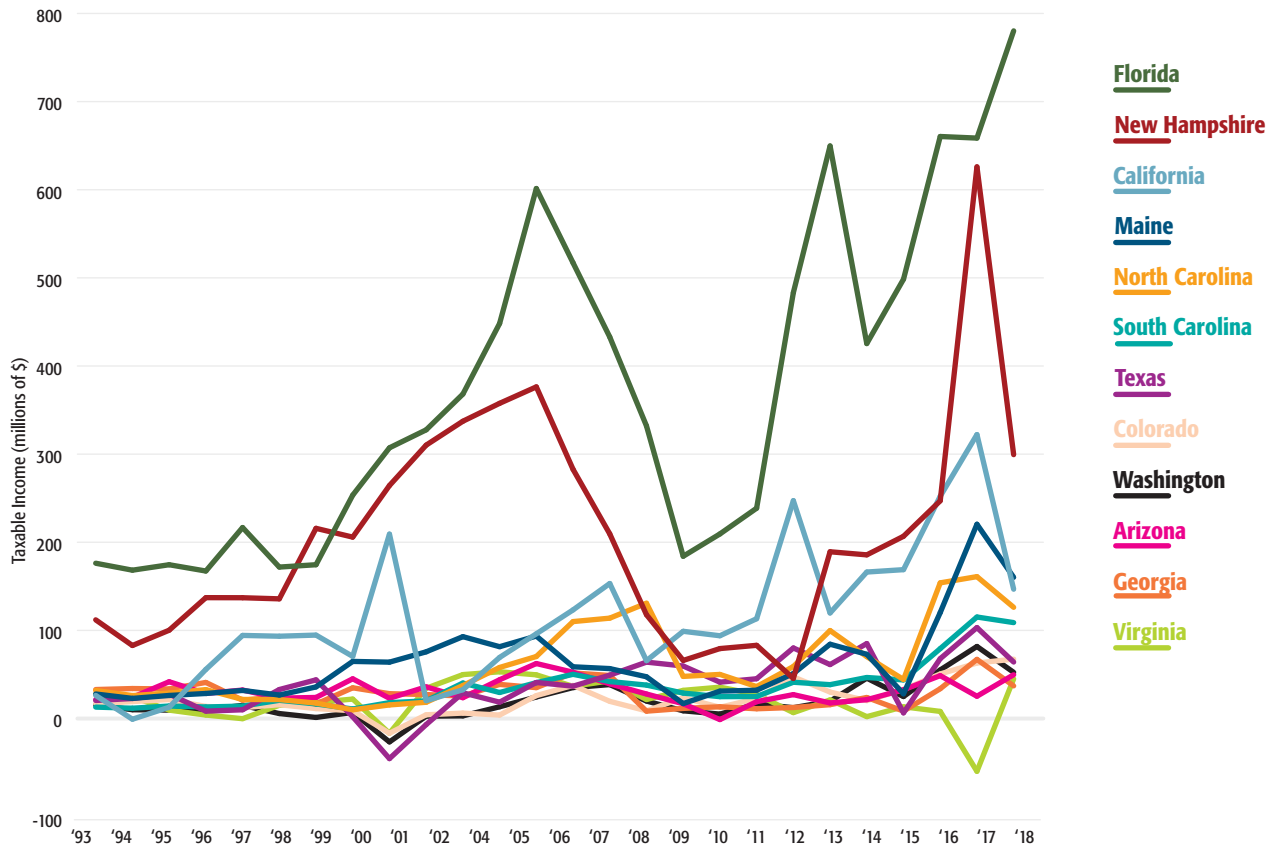
Household income range	Mean income	Mean unrealized capital gains	Mean financial assets	Mean net worth
\$250,000 – \$499,999	\$340,535	\$927,381	\$1,517,720	\$3,051,673
\$500,000 – \$749,999	\$608,147	\$2,541,608	\$3,821,872	\$7,487,182
\$750,000 – \$999,999	\$865,839	\$3,535,194	\$4,959,434	\$10,139,309
\$250,000 – \$999,999	\$420,072	\$1,366,356	\$2,123,898	\$4,252,196

The Florida Effect

Perhaps the biggest caveat in Young's research concerns Florida, a state that has no income tax, capital gains tax, or estate tax, and is by far the leading destination for U.S. millionaires. He writes that "evidence for tax migration is largely driven by Florida as an attractive destination for U.S. millionaires" and that "[t]he uniqueness of the Florida effect is a very robust finding."¹⁴

Indeed, Florida accounts for nearly half of Massachusetts' out-migration of adjusted gross income (AGI), far more even than neighboring New Hampshire, another no-income-tax state (see Figure 5). Yet in "Millionaire Migration and Taxation of the Elite," Young and his co-authors conclude that "when Florida is excluded there is virtually no tax migration; when any other state is excluded, our core finding of tax-induced migration is supported."¹⁵ This is akin to saying that if you exclude Muhammad Ali, Louisville hasn't produced any great boxers.

Figure 5: Net out-migration of taxable income from Massachusetts among destination states with over \$500 million in total gains (1993–2018)¹⁶



Florida was one of the most attractive destinations for migrating U.S. taxpayers from 1993 to 2018.¹⁷ The Sunshine State added \$182.8 billion in cumulative AGI from net in-migration over this period, according to IRS Statistics of Income data.¹⁸ Analysts of millionaire migration shouldn't immediately write off Florida as a rare outlier, but rather should explore the likelihood that Florida's friendly tax environment, combined with favorable weather and other factors, make it a uniquely attractive destination for the wealthy. They should also seek to isolate the influence of the tax environment on wealth migration by comparing Florida with states with similar coastal amenities, like South Carolina and California.

The IRS' addition of income categories to its migration data reporting beginning in 2012 allows researchers to calculate the percentage of AGI migration attributable to high-income taxpayers by state. The highest income category reported in IRS migration data is more than \$200,000. According to IRS data, Florida had a total of 122,341 migration inflow returns of taxpayers with AGIs of \$200,000 or more from 2012 to 2018, with an average AGI of \$647,305 per return.¹⁹ After taking account of the relatively few people who move from Florida to other places, the state's net inflow returns over this period totaled \$62.6 billion in taxable income among the wealthy.

Some academics have assured voters that adoption of a surtax would spur minimal migration, citing Cristobal Young's finding that "only" 2.4 percent of millionaires move each year.²⁰ But migration patterns create momentous shifts in wealth between states over time, and the relationship between Massachusetts and Florida exemplifies the scale of this cumulative effect. Massachusetts had a net out-migration of AGI to Florida of over \$9.6 billion between 1993 and 2018, representing 46.5 percent of Massachusetts' total AGI net out-migration.²¹ Income tax-free New Hampshire was another big beneficiary, accounting for another 26.1 percent of Massachusetts' net out-migration of AGI. In total, IRS data shows that Massachusetts experienced a cumulative net outflow of \$20.7 billion in taxable income from migration between 1993 and 2018 among people of all incomes.²²

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Conclusion

A change in the state constitution to create a graduated income tax is up for a second and final Constitutional Convention vote in 2021. If approved, it would go before state voters in 2022. The measure would raise taxes significantly on individuals who in any one year have a combination of earnings—from salary, rents, capital gains, investment income, pass-through business income, or any other source—of over \$1 million. As Massachusetts legislators consider this proposal to increase income taxes, they must balance any short-term benefit it might bring against the impact on jobs and the economy.

The following findings must be considered:

- When the Massachusetts Department of Revenue issued its estimate of how much the surcharge would generate, it provided a static analysis. That is why it added an important caveat: “taxpayers may respond to the additional tax by changing decisions on migration, consumption, investment, business location, etc. The number of high-income earners and amount of income reported by those earners could also fluctuate considerably from year to year.”²³
- This paper calls into question Professor Young’s narrow definition of “millionaire.” By ignoring households with substantial net worth but lower annual incomes, he counts only high earners who consistently earn over \$1 million per year as tax-induced migrants.
- Young himself cites Florida migration as the big exception to his thesis that wealthy individuals rarely move because of increases in taxes. Massachusetts has experienced tremendous net out-migration of taxpayers (\$20.7 billion in adjusted gross income) over the past 23 years. About three-quarters have moved to either Florida or New Hampshire, both of which have no personal earned income tax. The lure of tax-free states will be even greater because of the rise in remote work after the COVID-19 pandemic.²⁴
- The adoption of a surtax could spur substantial wealth migration. Already Professor Young finds that 2.4 percent of millionaires move each year.²⁵ The cumulative effect of an annual loss of high net worth taxpayers of that size can add up to big numbers, and exacerbate the already considerable exodus of Massachusetts residents to Florida.

The state legislature should think twice before effectively doubling the state taxes of high-income Massachusetts taxpayers and entrepreneurs.

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